

**The Euro Challenge 2012**

**Key Economic Concepts  
for the Euro Challenge**



# Describe the current season of the Giants



You can summarize their season by focusing on different *indicators*

- Games won, lost, tied
- Total yards, rushing, passing
- Touchdowns, sacks, field goals

These are all indicators

They help to explain the Giants' season

Will the Giants go to the Superbowl?

# GDP growth: a key economic indicator

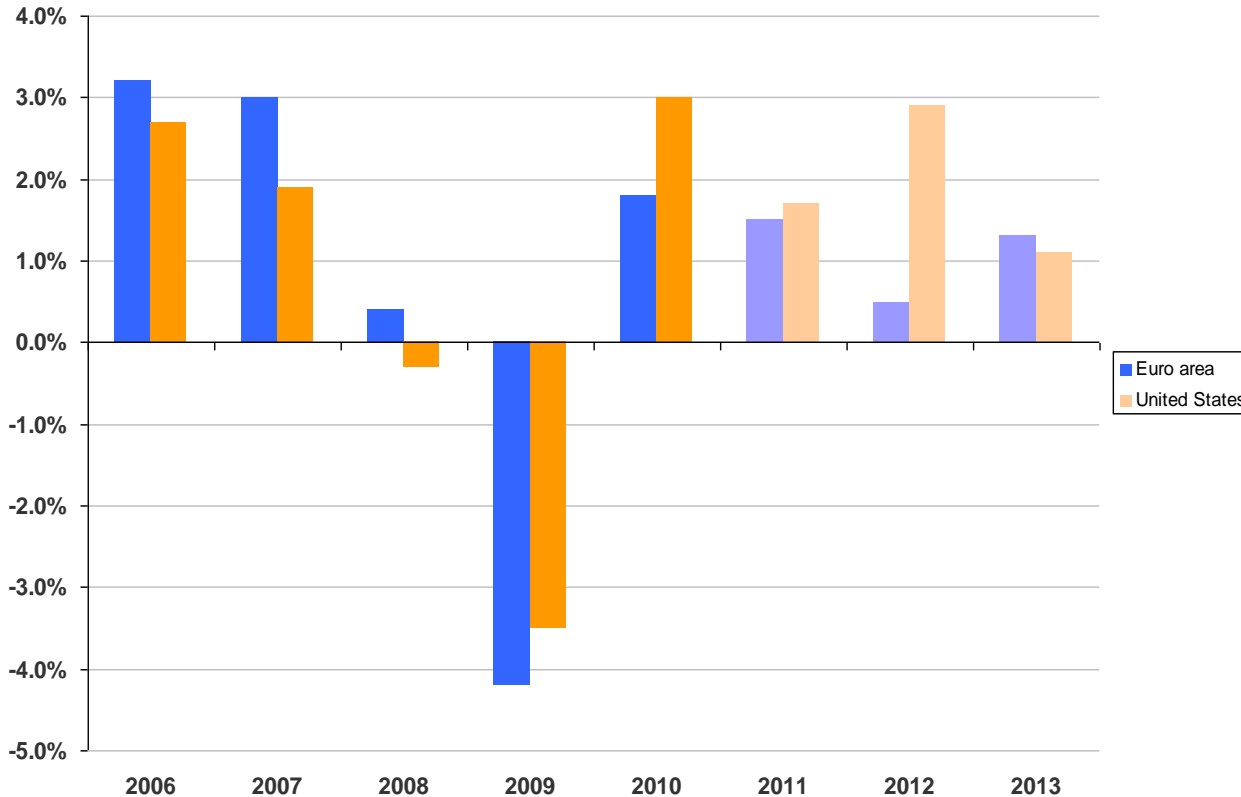


- *Gross Domestic Product (GDP)* is the total value of all the goods (e.g. cars, iPods) and services (e.g. haircuts, insurance policies) produced by an economy
- *GDP growth* tells you by how much GDP has increased compared to the last year (or last quarter)
- GDP growth is expressed as a *percentage*
- When the economy is growing, GDP growth is a *positive number*
- In a recession, GDP growth is *negative* (GDP shrinks)



# Euro area GDP growth is slowing sharply

Euro Area & US GDP with Forecasts



Source: European Commission Autumn forecast, November 2011

The euro area economy as a whole is *forecast* to barely grow at all next year.

Some countries are in recession already (negative *GDP growth*).

**Hint: For explanations and updates, see “Current Economic Situation in the Euro Area” on the Resources page at <http://www.euro-challenge.org/doc/2011/CurrentEconomicSituationOct2011.pdf>**

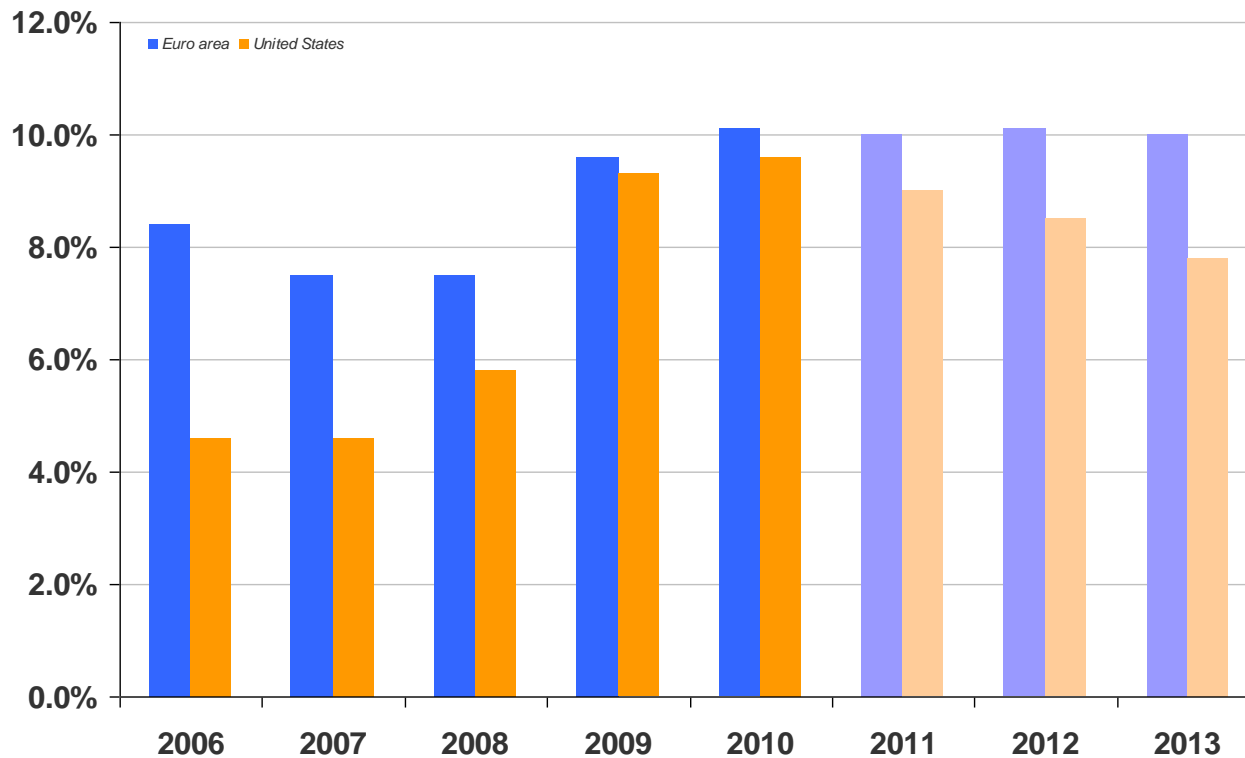
# Unemployment



- The basic definition of unemployment is the number of people that are actively looking for work and have not found it in a certain period.
- The unemployment rate is the share of the working-age population that is looking for work but not employed.
- Unemployment normally rises in times of slow or declining GDP growth, and tends to fall in times of stronger GDP growth.
- As economic activity increases, firms hire more workers to produce the goods and services people are consuming.

# Unemployment: on the rise again

Unemployment: Euro Area & United States



**The unemployment rate in the euro area was falling prior to the 2008-09 crisis, but it is rising again and now stands at 10.3%.**

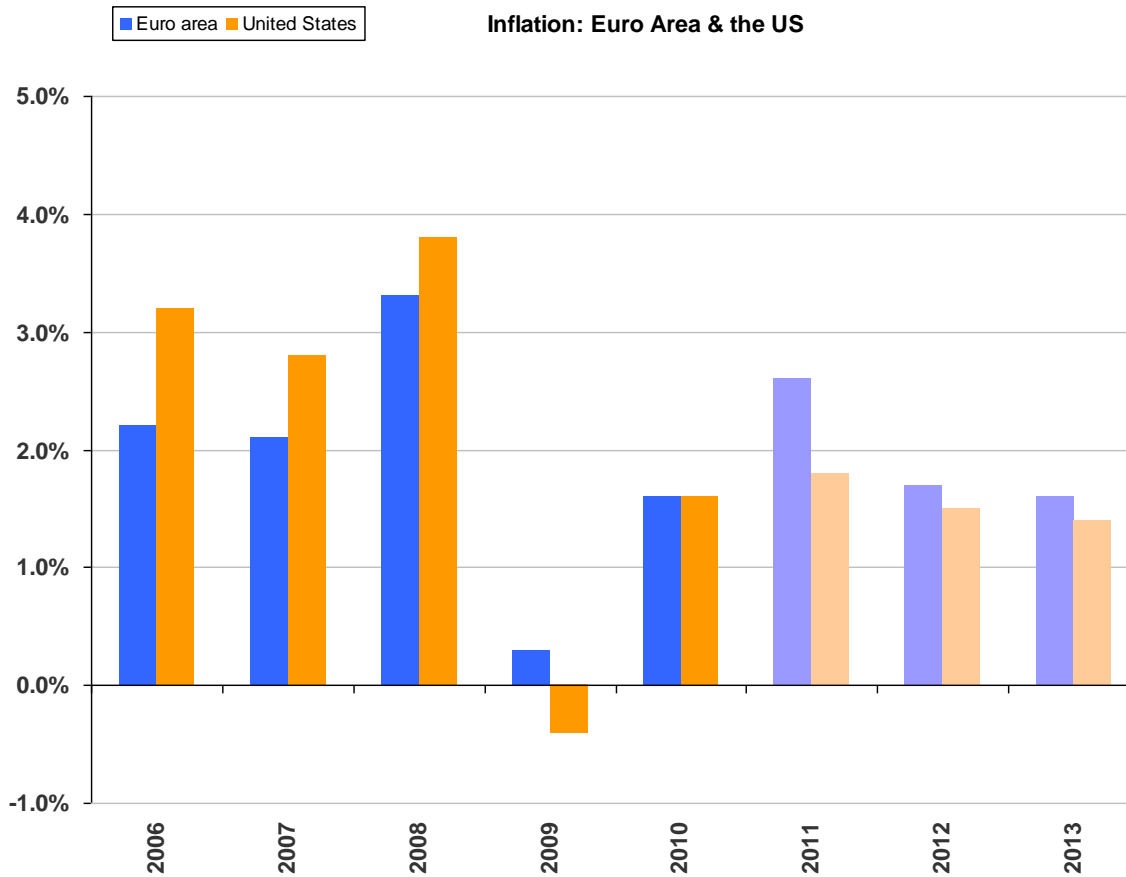
**There are huge differences in unemployment rates among euro area countries (4.1% in Austria, 22.8% in Spain).**



HINT: For all you need to know about inflation/deflation and the ECB, go to <http://vimeo.com/12324309>

- Inflation is the general increase in the level of certain measured prices over a certain period. It is expressed as a percentage change.
- A little inflation is fine, even desirable, but too much of it can be damaging, both to people's livelihoods and to the economy as a whole.
- High inflation usually occurs when an economy is over-heating (growing too quickly). When growth is too weak, there may be a risk of deflation (falling prices) – which sounds great but can be very bad!

# Inflation: elevated but coming down



Inflation is relatively high now due to past increases in oil and commodity prices globally.

But euro area inflation is expected to come down (to below 2%, within the ECB's "comfort zone") due to slow growth and high unemployment.

# What is fiscal policy?

**... But fiscal and other economic policies remain in national hands**



- Fiscal policy is the use of government expenditure and revenue collection (taxation) in an effort to influence the economy.
- Fiscal stimulus is when the government increases spending and/or reduces taxes in order to increase economic activity.
- Fiscal contraction is when the government cuts spending and/or increases taxes in order to control deficits and debt.

*How well has this model worked in the crisis?*

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## High debt and deficits



- The *deficit* is the difference between the amount of money a government takes in (revenue) and what it spends (outlays) in a given year. If that number is positive, there is a *surplus*.
- The debt is the total amount of money the government owes. It is usually expressed as a percentage of GDP
- A debt level that is too high can lead to higher borrowing costs and slower economic growth. And slower GDP growth makes it more difficult to reduce deficits and debt!

# What is monetary policy?

**The euro area has a  
single monetary  
policy run by the ECB**



Mario Draghi,  
ECB President

- Monetary policy is the process by which a central bank controls the supply of money for the purpose of steering economic growth and controlling inflation.
- By setting interest rates, central banks can influence borrowing and lending decisions by households and firms. Lower interest rates generally spur economic activity, while higher interest rates slow inflation down.
- Monetary policy can be described as *neutral*, *expansionary* (“loose”), or *contractionary* (“tight”)