

## WHEN SAVING IS NOT A VIRTUE

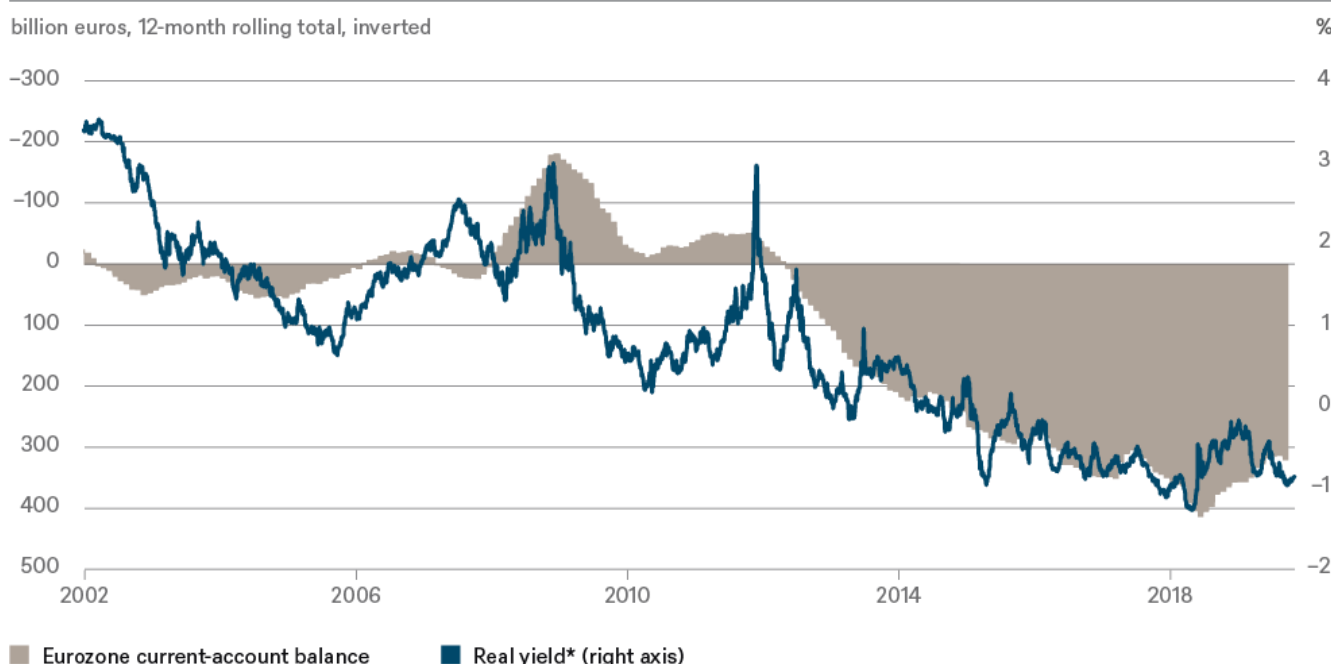
What is to blame for low interest rates? Many pundits point accusingly at central banks. However, the savings and investment behavior of the private sector is just as important.

Eurozone sovereign-bond yields have risen from their August lows, but remain firmly in negative territory. In this environment, one must either invest for the very long term, or be willing to take some credit risk, just to find a security with a positive yield. Quite often, people blame central banks for the widespread savings dilemma, in particular the European Central Bank (ECB). By contrast, ECB board member Philip R. Lane gave a bunch of explanations for the low-yield environment. In a recent speech, Lane cited a declining potential growth rate, demographics, and an increasing desire for safe and stable investments as reasons leading to a declining "natural rate of interest  $r^*$ ."<sup>1</sup>

Our "Chart of the Week" points towards another way of explaining the low level of bond yields. Listening to many discussions, especially in Germany, saving is deemed as a virtue, while borrowing is seen as a vice. All too often, the basic logic of how interest rates are generated is missing: savers lend their savings to a borrower (typically a corporation), who then makes an investment in the real economy (e.g. by building a plant), which generates a return. Part of

that return is then passed on back to the saver. If the private sector is either unable or unwilling to borrow, as it seems to be the case in much of the Eurozone, one might also make the case that finance ministers should step in. But there are hurdles: As many borrowers have overdone it in the past, pundits, especially German ones, have kept lecturing the world about the merits of saving. The same people often urge caution when it comes to taking on new debt. Many people seem to have listened. Hence, the Eurozone now runs a savings surplus of more than 300 billion euros per year, observes Oliver Eichmann, Head Fixed Income Rates EMEA at DWS. Comparing the Eurozone's current-account balance, i.e. the flipside of the savings balance, with real yields reveals a stunning correlation, as our "Chart of the Week" demonstrates. From this perspective, the question is not whether the ECB will hike rates again, but how to create an environment where the corporate sector is willing to invest, thus achieving a return, and passing on part of this return to creditors. That is something monetary policy cannot achieve on its own.

<sup>1</sup> [https://www.ecb.europa.eu/press/key/date/2019/html/ecb.sp191128\\_1~de8e7283e6.en.html](https://www.ecb.europa.eu/press/key/date/2019/html/ecb.sp191128_1~de8e7283e6.en.html)



Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 12/2019

\* Yield of ICE BofAML 1-10 Year Euro Inflation-Linked Government Index

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/ 1

## GLOSSARY

**Correlation** is a measure of how closely two variables move together over time.

The **euro (EUR)** is the common currency of states participating in the Economic and Monetary Union and is the second most held reserve currency in the world after the dollar.

The **European Central Bank (ECB)** is the central bank for the Euro-zone.

The **Eurozone** is formed of 19 European Union member states that have adopted the euro as their common currency and sole legal tender.

The **ICE BofAML 1-10 Year Euro Inflation-Linked Government Index** tracks the performance of euro-denominated inflation-linked

sovereign debt with a remaining term to maturity of more than one less than 10 year(s) issued by Euro member countries in either the eurobond market or the issuer's own domestic market.

**Monetary policy** focuses on controlling the supply of money with the ulterior motive of price stability, reducing unemployment, boosting growth, etc. (depending on the central bank's mandate).

The **neutral real interest rate** is the official interest rate, adjusted for inflation, which is estimated to allow an economy to grow at its trend rate.

In economics, a **real** value is adjusted for inflation.

**Yield** is the income return on an investment referring to the interest or dividends received from a security and is usually expressed an-

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