

EU-IMF assistance to Euro Area countries: An Early Evaluation

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This study

- **Two innovations in financial assistance programme:**
 - Adjustment within monetary union
 - Institutional set-up of EU-IMF cooperation (the 'Troika')

- **Our aims:**
 - Assess programme outcomes (irrespective of institutional set-up)
 - Assess institutional set-up
 - Draw lessons for future programmes

- **Basis for assessment:**
 - Comparison with other programmes
 - Comparison between initial programmes and outcomes
 - Interviews with policymakers

Crises in the euro area: what is special?

▪ **Economic constraints**

- Irrevocably fixed exchange rates, single monetary policy
- Large cross-border exposure, unrestricted capital mobility (in principle)
- Prohibition of monetary financing

▪ **Policy constraints**

- No EU institutions in place that could provide assistance
- No experience of assistance, therefore IMF participation indispensable

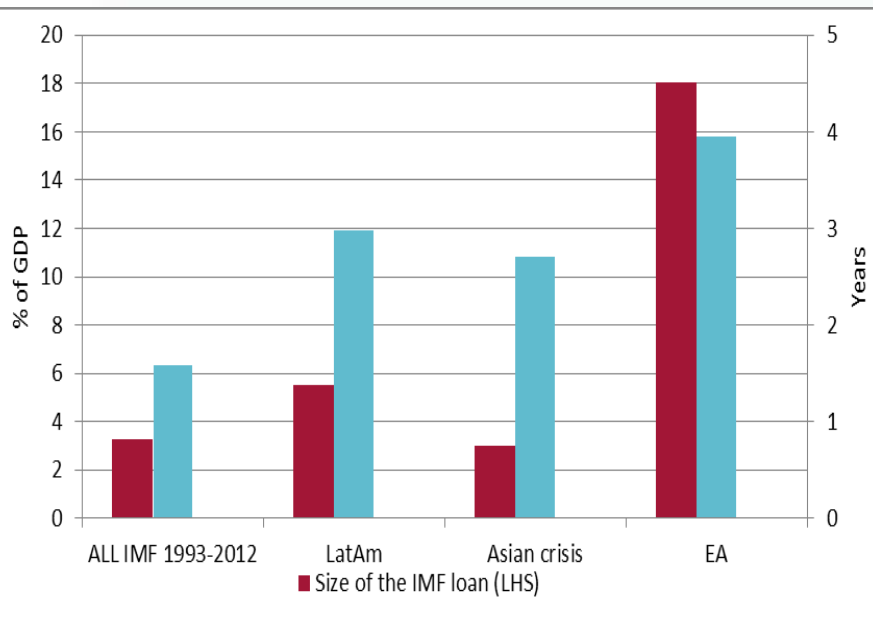
▪ **Legal constraints**

- Financial assistance to sovereigns regarded by some as illegal.
- European Commission bound by the Treaty in giving policy recommendations to member states

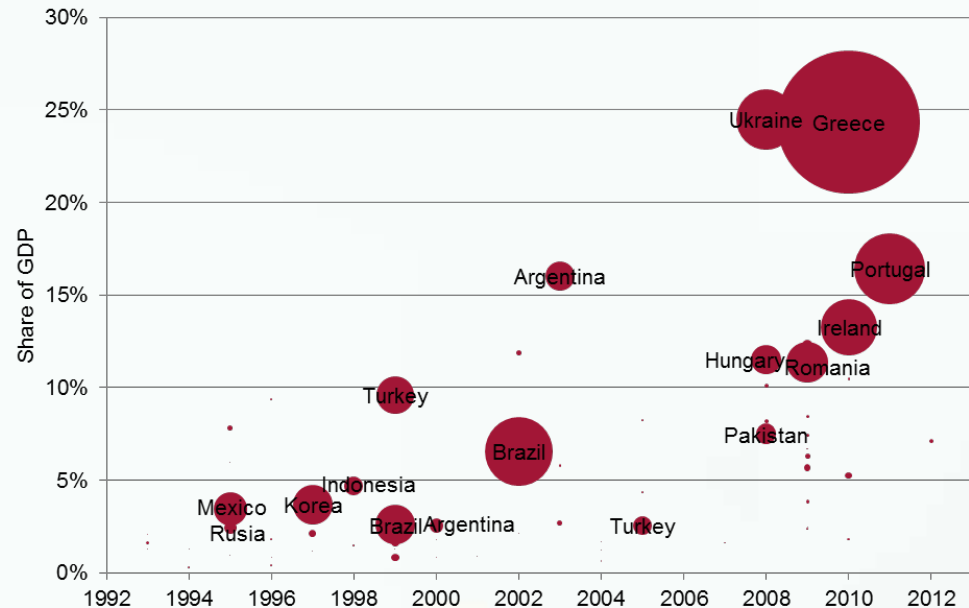
Very big programmes (note: IMF only)

- Size and length of IMF programmes by region (note: IMF only!)

Size and duration



Relative and absolute size

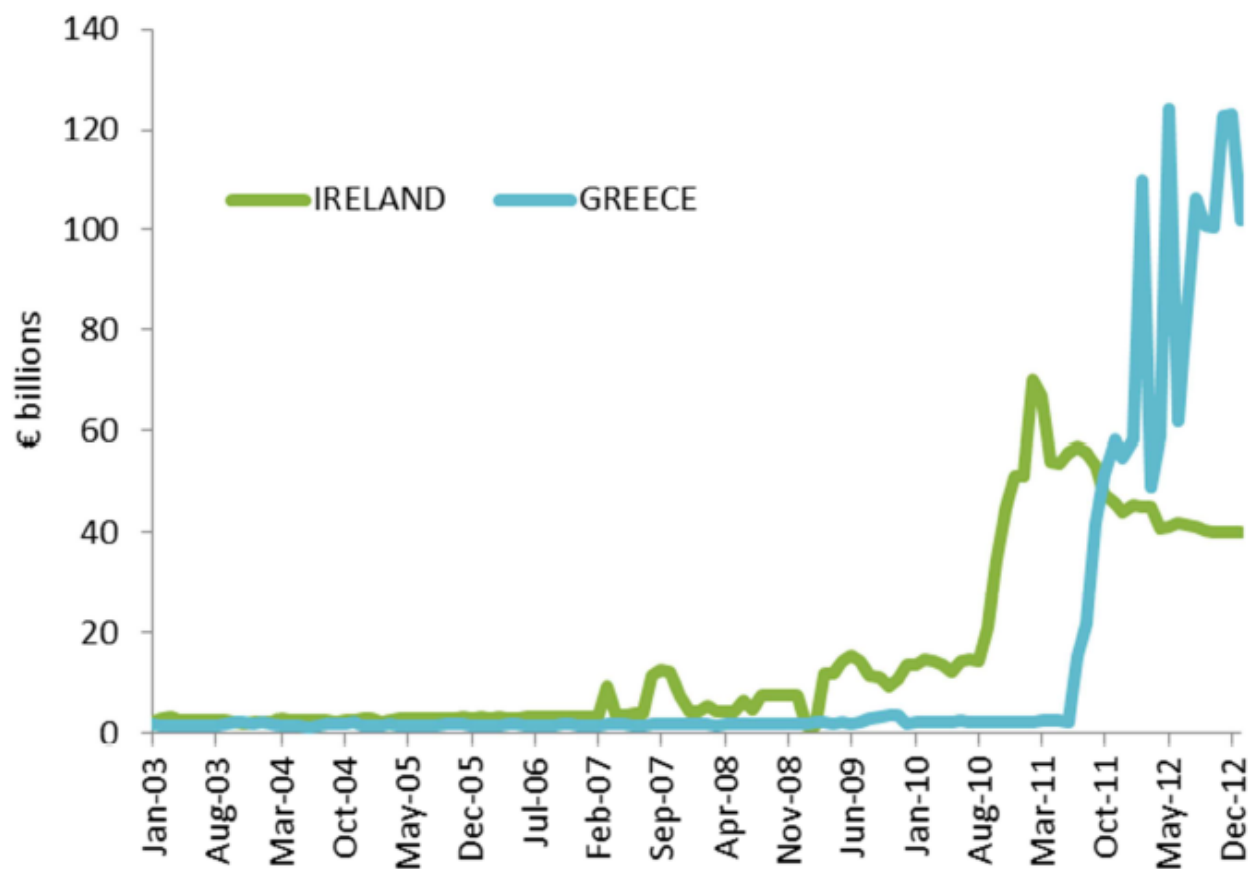


Note: in the case of the EA countries the length is taken as currently scheduled. On RHS graph diameter of bubbles indicates absolute size of the loans in US dollars.

Source: IMF MONA database and IMF WEO (October 2012).

ECB exposure

Figure 3: Emergency liquidity assistance provided by the Greek and Irish central banks, 2003-12



Source: Bruegel based on national central bank balance sheets. Data for Portugal is not available. Note: Buiter and Rahbari (2012b) provide estimates consistent with ours.

Table 4: Economic indicators for 2013: projections vs. outcomes

	Greece		Ireland		Portugal	
Source	Programme May-10	AMECO Feb-13	Programme Feb-11	AMECO Feb-13	Programme Jun-11	AMECO Feb-13
<i>Projection*</i>	<i>2009-2013 cumulated</i>		<i>2010-2013 cumulated</i>		<i>2010-2013 cumulated</i>	
Real GDP (% change)	-3.5	-21.0	5.4	2.4	-2.8	-6.5
Domestic demand (% change in volume)	-11.8	-28.4	-3.4	-11.1	-10.5	-14.0
HICP (% change)	3.4	8.3	2.6	2.8	6.9	7.0
<i>Projection</i>	<i>2013</i>		<i>2013</i>		<i>2013</i>	
General government deficit (% of GDP)	-4.9	-4.6	-7.5	-7.3	-3	-4.9
Current external balance (% of GDP)	-5.6	-4.3	2.6	3.4	-3.9	-1.4
Unemployment (%)	14.8	27	11.6	14.6	12.4	17.3
General government debt	149.7	175.6	120.5	122.2	108.6	123.9
Net IIP (negative)	106.0**	97.6	n.a.	n.a	123.4**	106.1

Source: European Commission economic adjustment programmes, European Commission forecasts as of February 2013 retrieved from the AMECO database. Note: * Data for 2009, respectively 2010 refer to end of year data. The date is the year before the programme started. **Taken from IMF programme documents as not available in European Commission economic adjustment programme.

Greece

- **Major imbalances at start of programme**
- **Initial programme was not robust**
 - Optimistic privatization and tax revenue assumptions
 - Punitive rates initially
 - Debt sustainability doubtful
- **Shift of programme focus from fiscal to structural**
- **Major setbacks**
 - Revision of starting conditions
 - Political-administrative weaknesses
 - Major European turn arounds on debt restructuring
 - Talk of Grexit
- **Greece still in euro but market access far off**

Reasons for the worse debt levels

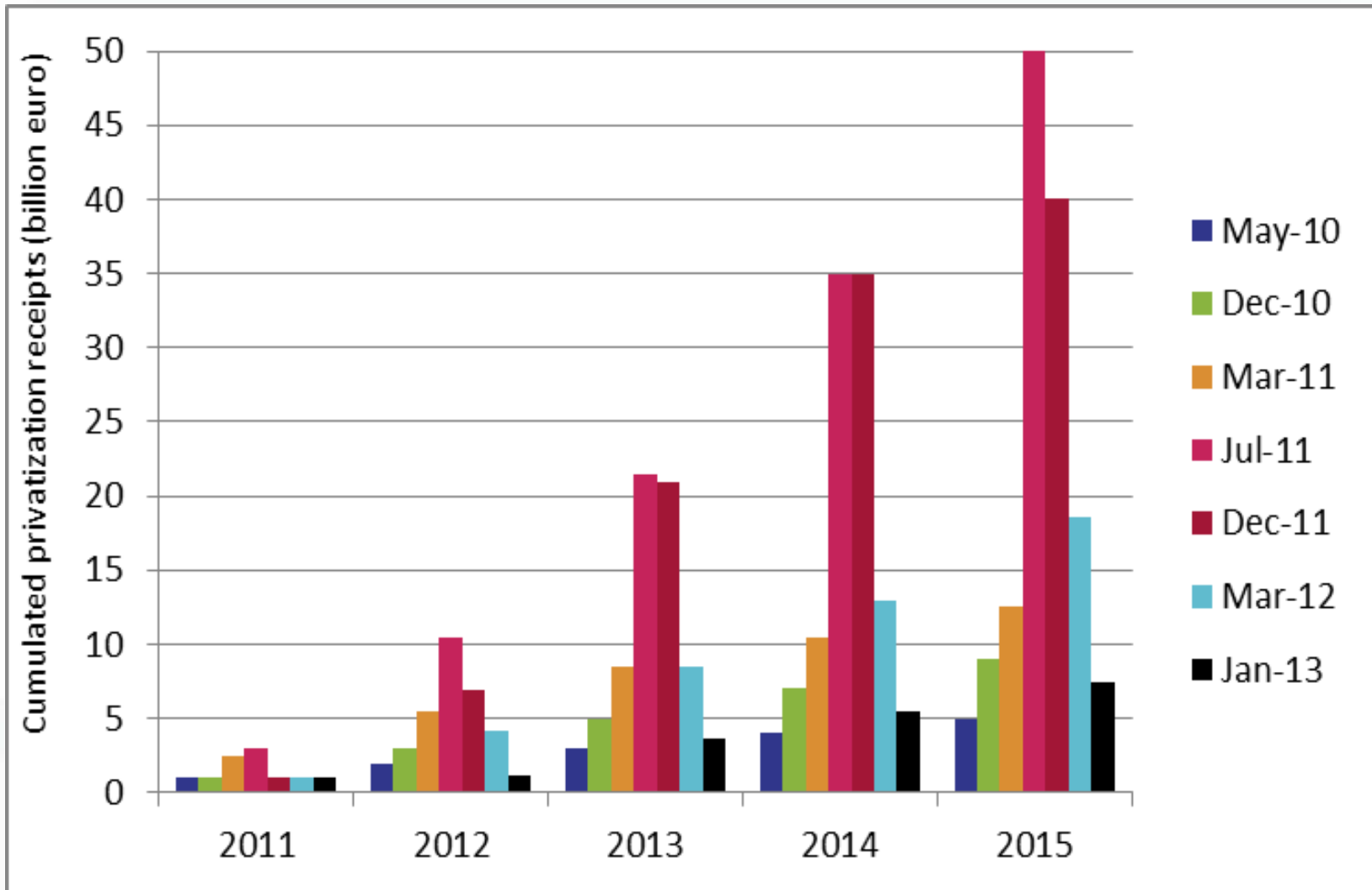
Table 6: Greece - breakdown of the gap between May 2010 and Jan 2013 fiscal targets for 2013

(All variables expressed as % of GDP)

	Primary balance	Overall balance	Gross debt
2013 target as set in the May 2010 SBA programme	3.1	-4.8	149.0
- Worse 2009 initial conditions	-1.8	-2.0	14.3
- Revenue shortfall due to adverse GDP developments	-9.0	-9.0	
- Effect of lower nominal GDP		-1.0	38.4
- Interest rate on public debt		4.5	
- Larger than expected overall deficits			1.7 ³³
- Fiscal consolidation effort (residual)	7.7	7.8	
- Debt accumulation residual			1.7
- Debt restructuring			-26.6
2013 result as forecast in the January 2013 review	0.0	-4.5	178.5

Source: Bruegel calculations, IMF programme documents. Note: See methodology in Appendix 2.

Greek privatisation plans



Ireland

- **Major housing bubble and credit exuberance**
- **Initial 2008 guarantee**
- **Senior creditor issue**
 - Around 19bn of senior unsecured debt (going and gone concern)
 - Burden for tax payer could have been reduced by perhaps 5-10bn
 - Financial stability issue also for non-Irish banks acknowledged
 - IMF-ECB difference?
- **Speed of deleveraging**
 - High speed at beginning of programme, was justified by ECB exposure
 - Costly due to asset price collapse in firesale
 - Speed was reduced
- **Fiscal**
 - Major imbalances as revenues heavily relied on bubble
 - Irish government/EC had initially quicker adjustment path foreseen
- **Full market access appears possible**

Portugal

- **Compliance to Troika programme quite high**
- **Growth underperformance is major issue**
- **Long-standing structural growth weakness**
- **Markets have turned relatively optimistic**
 - Relatively high domestic consensus on programme, but risk due to unemployment
 - Troika and authorities mutually trusting
 - Markets believe PT will get support
- **Tradable sector remains weak, labour market reform incomplete**

Expectations vs. reality

■ Overall

- Larger fall in domestic demand and output (fiscal multiplier, confidence effects, financial fragmentation)
- Much worse unemployment
- Worse debt ratio despite larger fiscal efforts (GDP collapse)
- Better current account position

■ Differences

- Greece much worse on all accounts
- Ireland stands out for exchange rate improvement, export performance
- Portugal much better than Greece on implementation, but remaining structural weaknesses

Success or failure?

▪ **Success**

- No exit
- Prospects for market access: Ireland, Portugal

▪ **Failures**

- Slower-than expected adjustment (Greece, Portugal)
- Higher-than expected economic and social cost
- Political sustainability

▪ **What could have been done differently?**

- Time-consistent EU stance
- Better economic environment in rest of EU
- Early restructuring for Greece, Senior creditors' bail-in for Ireland?
- Less austerity (= more financing)?

3. Institutional issues

- **Troika set-up without precedent**
 - IMF cooperation with regional entity (remember AMF!)
 - Commission: broad-mandate entity rather than specialised agency
 - Central bank on the lending side of the table
- **How the Troika works**
 - Neither a decision-making nor a lending institution
 - No Troika conditionality but separate IMF and EU conditionalities
 - Three unequal partners

Table 2: Distribution of roles in IMF and European assistance

	IMF	Euro area
Programme negotiation and monitoring	IMF Staff	Commission services in liaison with ECB
Decision to assist	IMF Board	ESM Board of governors (aka Eurogroup)
Lending	IMF	EFSF/EFSM ²⁰ /ESM

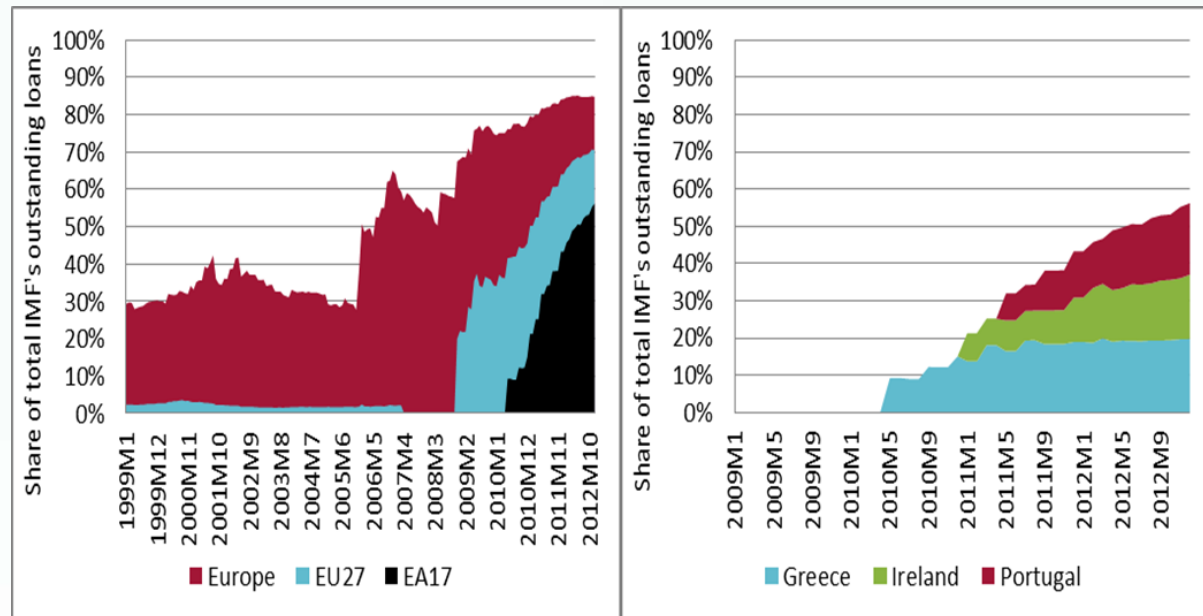
Assessing the Troika

- **Indispensable cooperation**
 - Financing
 - Technology transfer
- **Less problematic than could have been expected**
- **But questions going forward**

EU-IMF cooperation

- **Equality of treatment**
 - Exceptional access policy criterion
 - Weight of euro-area and EU-specific rules
- **Superposition of conditionalities**
- **Decision-making procedures**
- **Resources**
- **Junior role?**

Shares of Europe in IMF lending



Commission role

- **Learning and effectiveness on the ground**
- **Problems:**
 - Commission as 'agent of the EA lender countries
 - Commission as principal: political entity, guardian of the treaty
- **Conflict of interest**
- **Political risk**

Recommendations

- **Involvement of IMF advisable as long as EA governance incomplete**
- **Role of IMF**
 1. Provision of technical assistance but no financial assistance
 2. Keep an important lending role
 3. **Function as a ‘catalytic lender’**
- **Role of EC**
 1. Give EC full responsibility for negotiation, financing and monitoring
 2. **ESM becomes EMF (European Monetary Fund), with staff seconded from Commission**
- **Role of ECB**
 - **Becomes a (mostly) silent participant in the Troika**
- **Improve accountability**
 - Oversight by European Parliament

Thank you!