

The global crisis: a European viewpoint

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Impacts of and Lessons Learned from the Global Economic Crisis in 2008
Chung-Hua Institution for Economic Research (CIER)
Taipei, May 15-16 2009

Outline

- The EU deeply hurt by the crisis
 - but large differences across EU members
- A heterogenous area
- Actions taken so far
 - at the EU level
 - at the Member-State level
- Actions *not* taken so far
 - at the EU level
 - at the Member-State level
- Key issues for the future

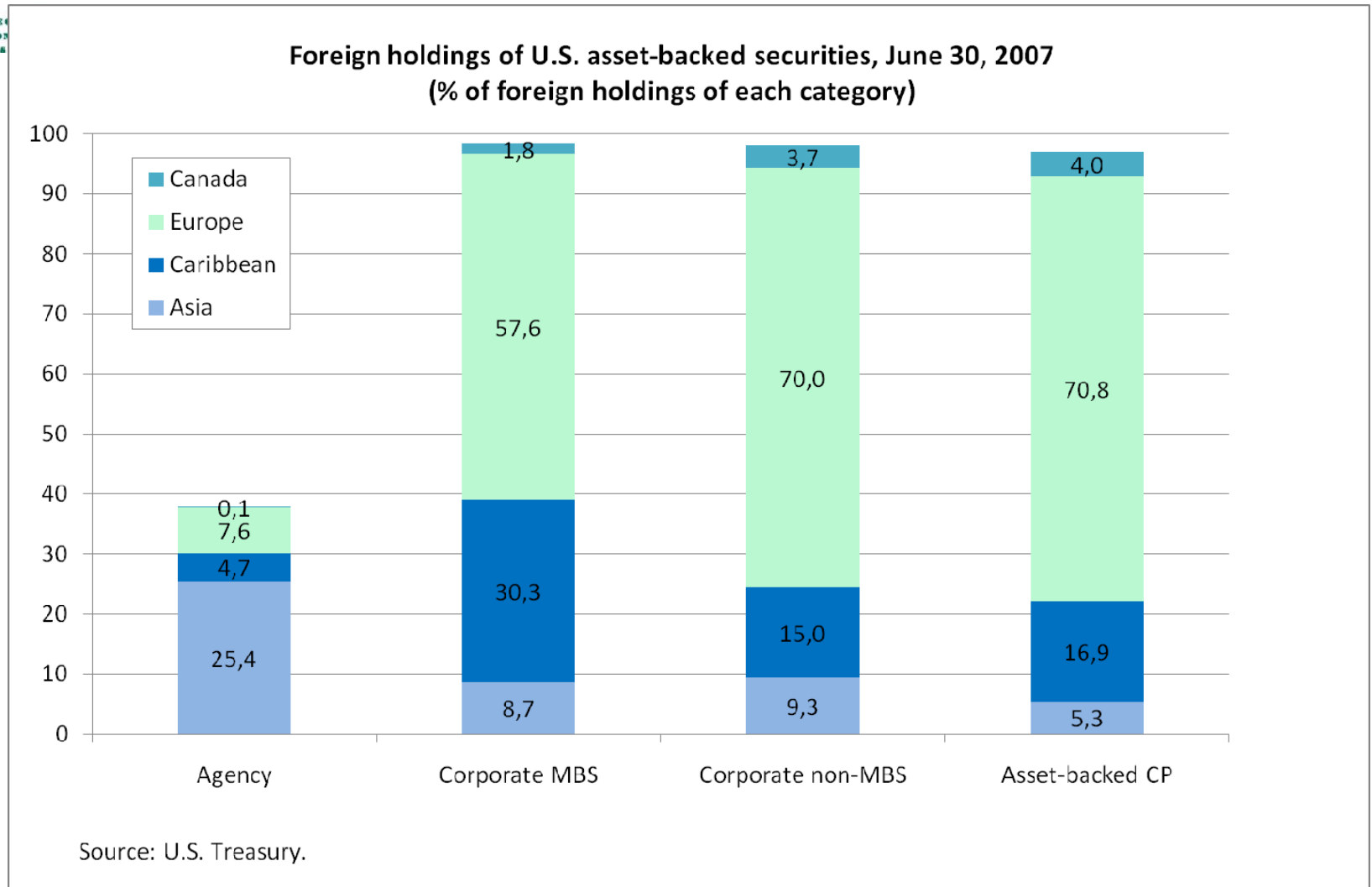


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The Euro area deeply hurt by the crisis

Exposure to « toxic » assets



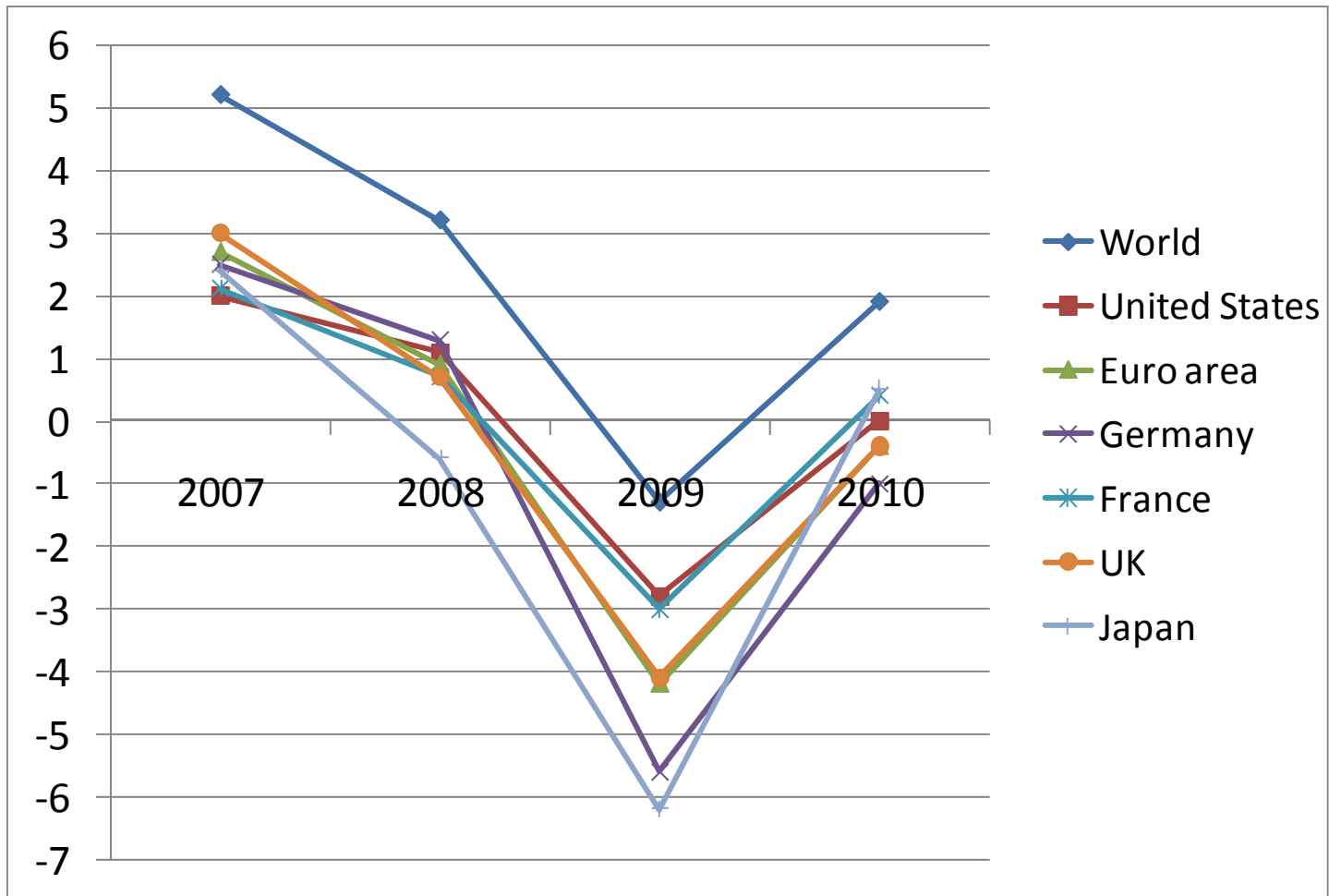


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The Euro area deeply hurt by the crisis

GDP growth forecasts



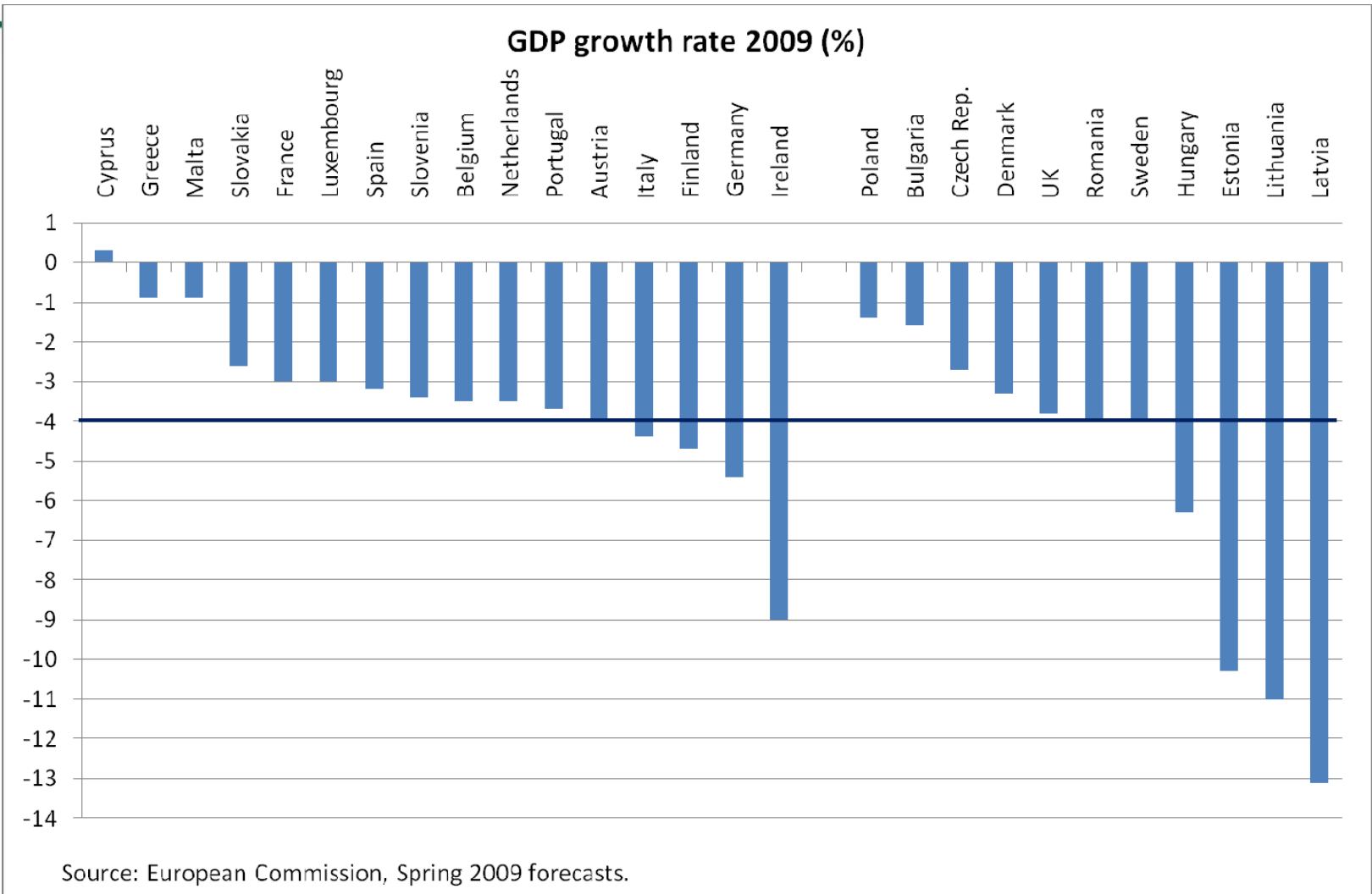
Source: IMF, WEO April 2009.



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With large differences across countries





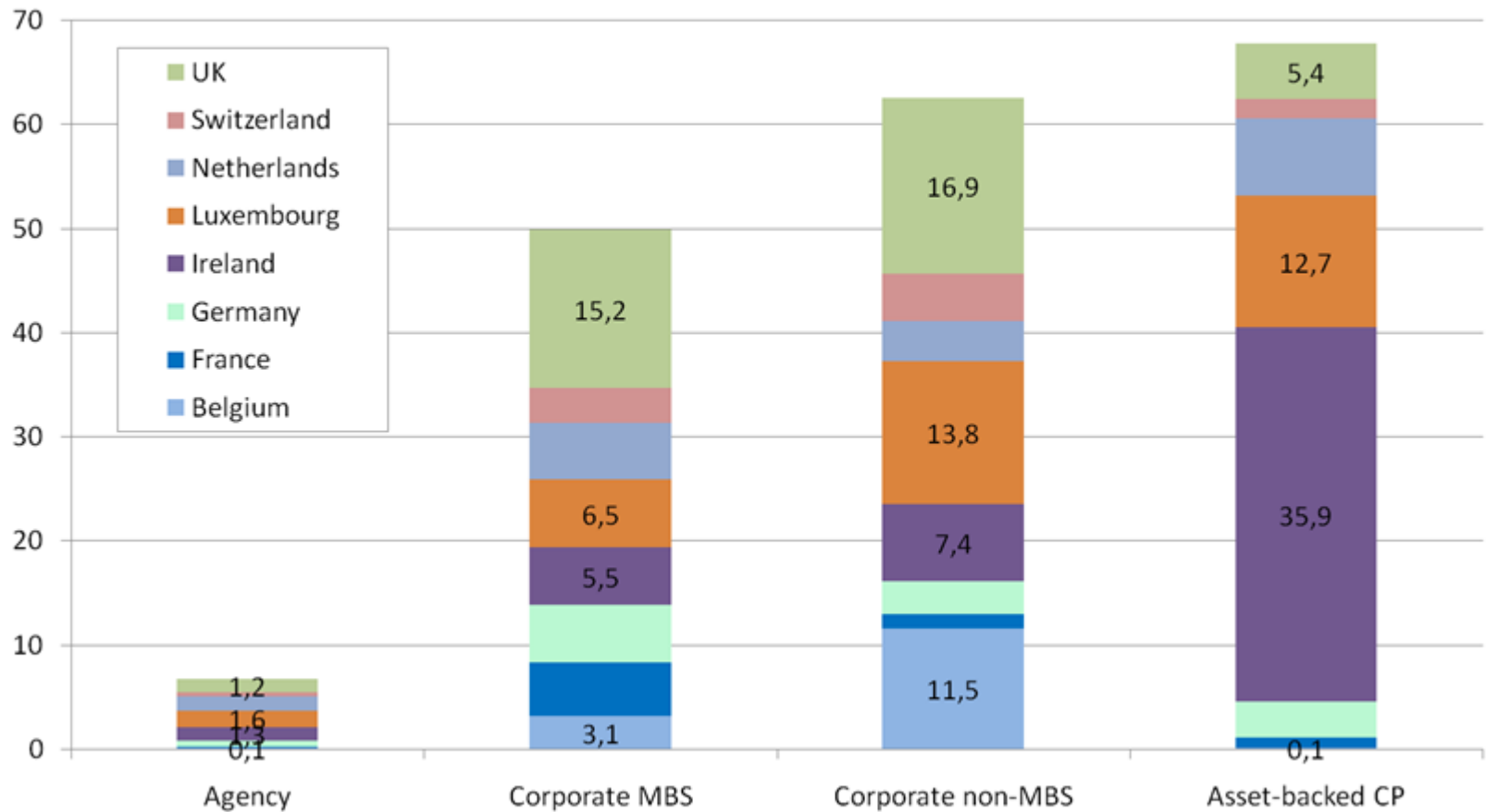
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A heterogenous area

1. Different exposures to « toxic » assets

European holdings of U.S. asset-backed securities, June 30, 2007
(% of foreign holdings of each category)



Source: U.S. Treasury.



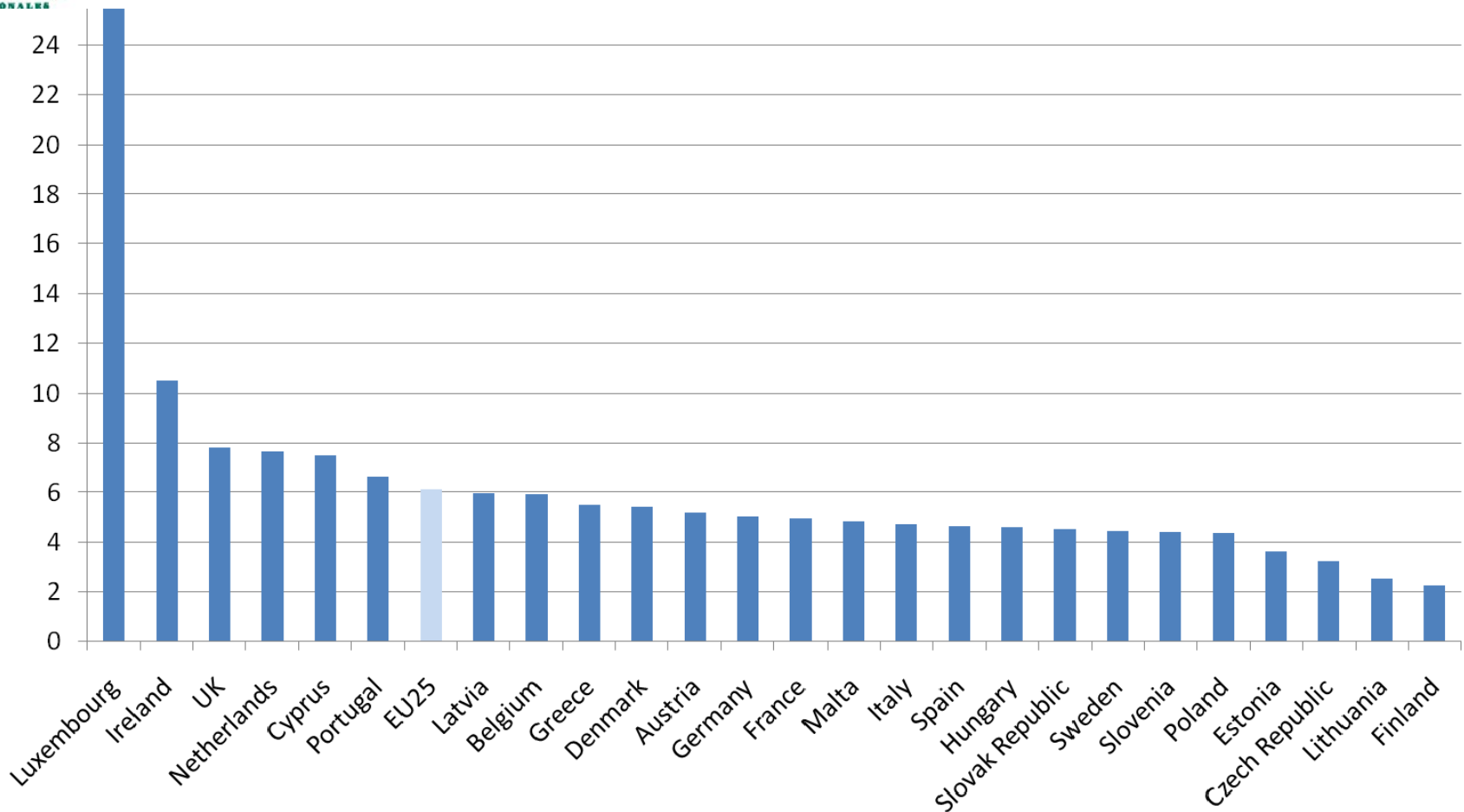
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An heterogenous area

2. Financial intermediation in value added

Share of financial intermediation in value added (% in 2005)



Source: EUKLEMS database.



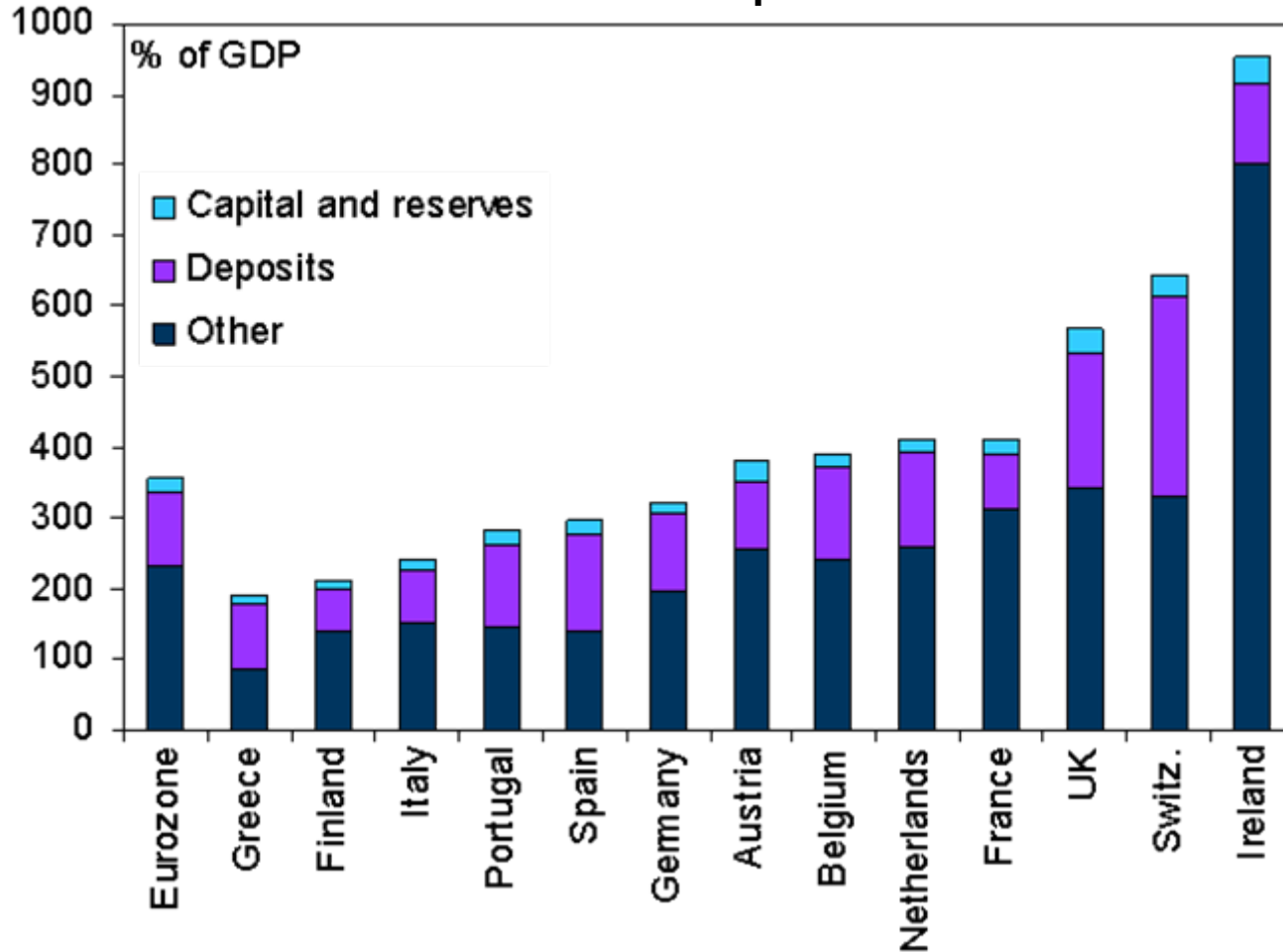
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A heterogenous area

3. Balance sheets

Banks' balance sheets as percent of national GDP

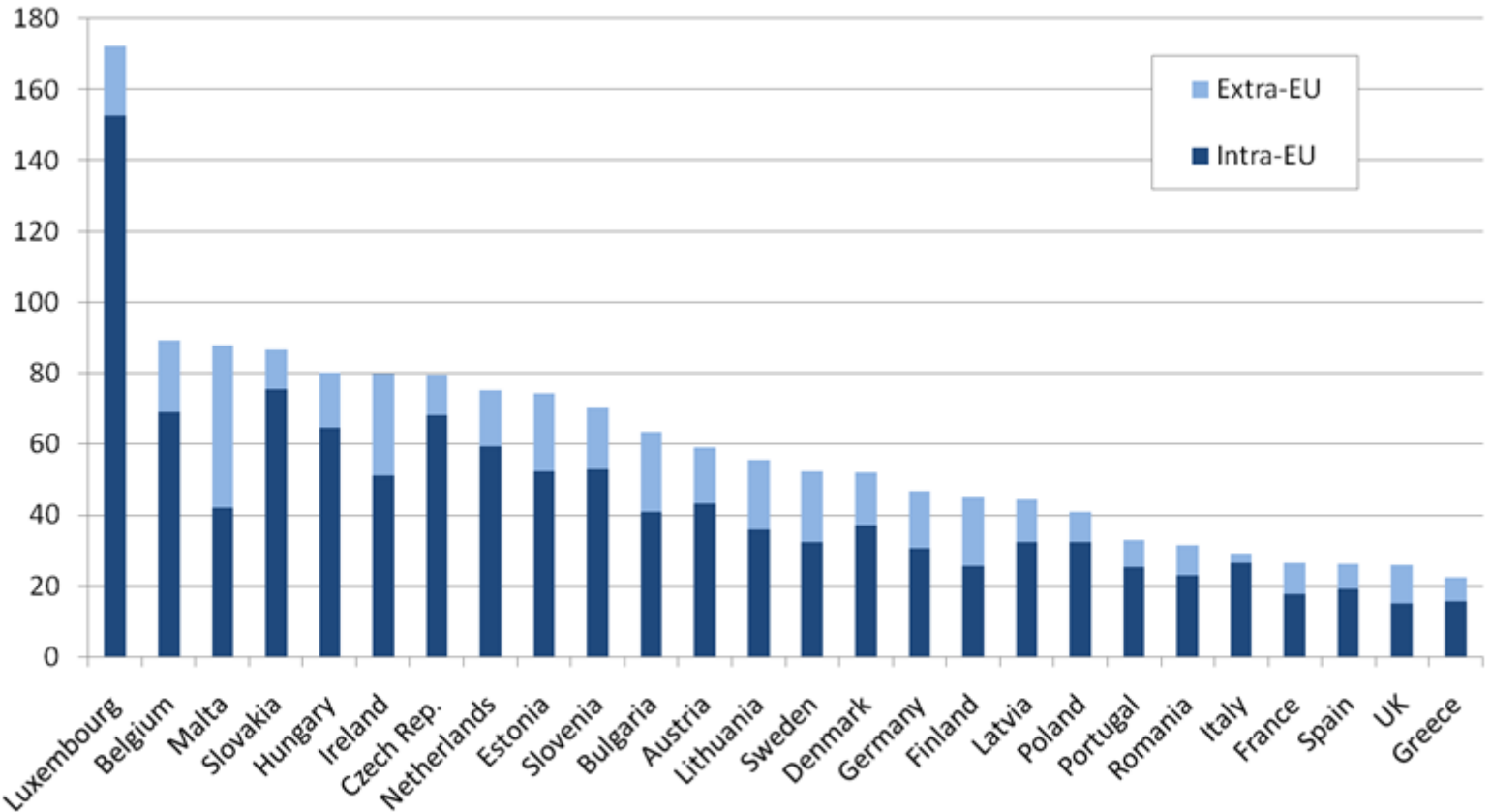


Source: Goldman Sachs Economics Research.

A heterogenous area

4. Openness

Exports of goods and services as a percentage of GDP (2007)



Sources: WDI and European Commission.

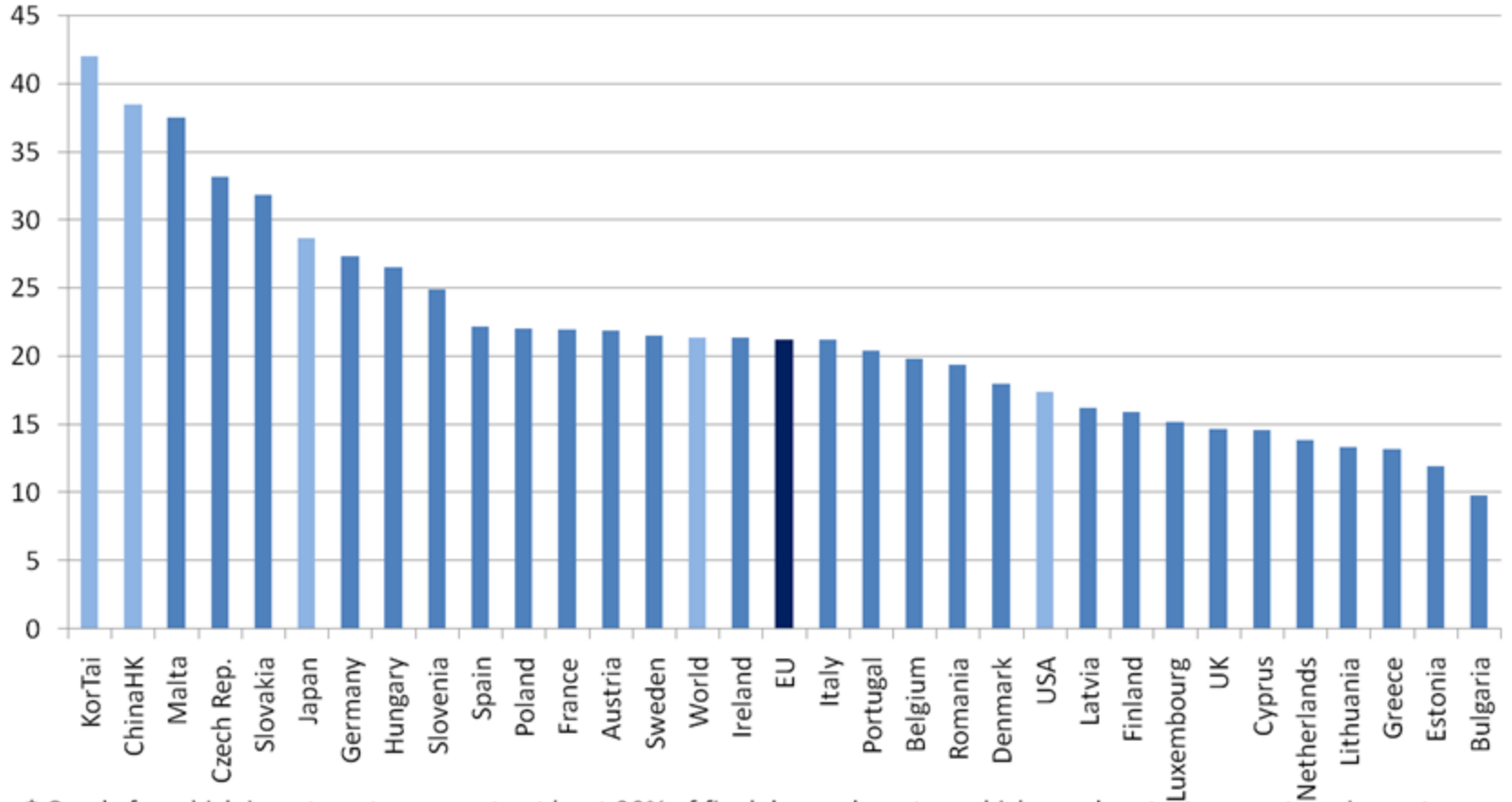
A heterogenous area

5. Specialization



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Share of investment goods* in value added (% in 2004)



* Goods for which investment represents at least 30% of final demand: motor vehicles and parts, transport equipment nec, electronic equipment, machinery and equipment nec, construction.

Source: GTAP database.

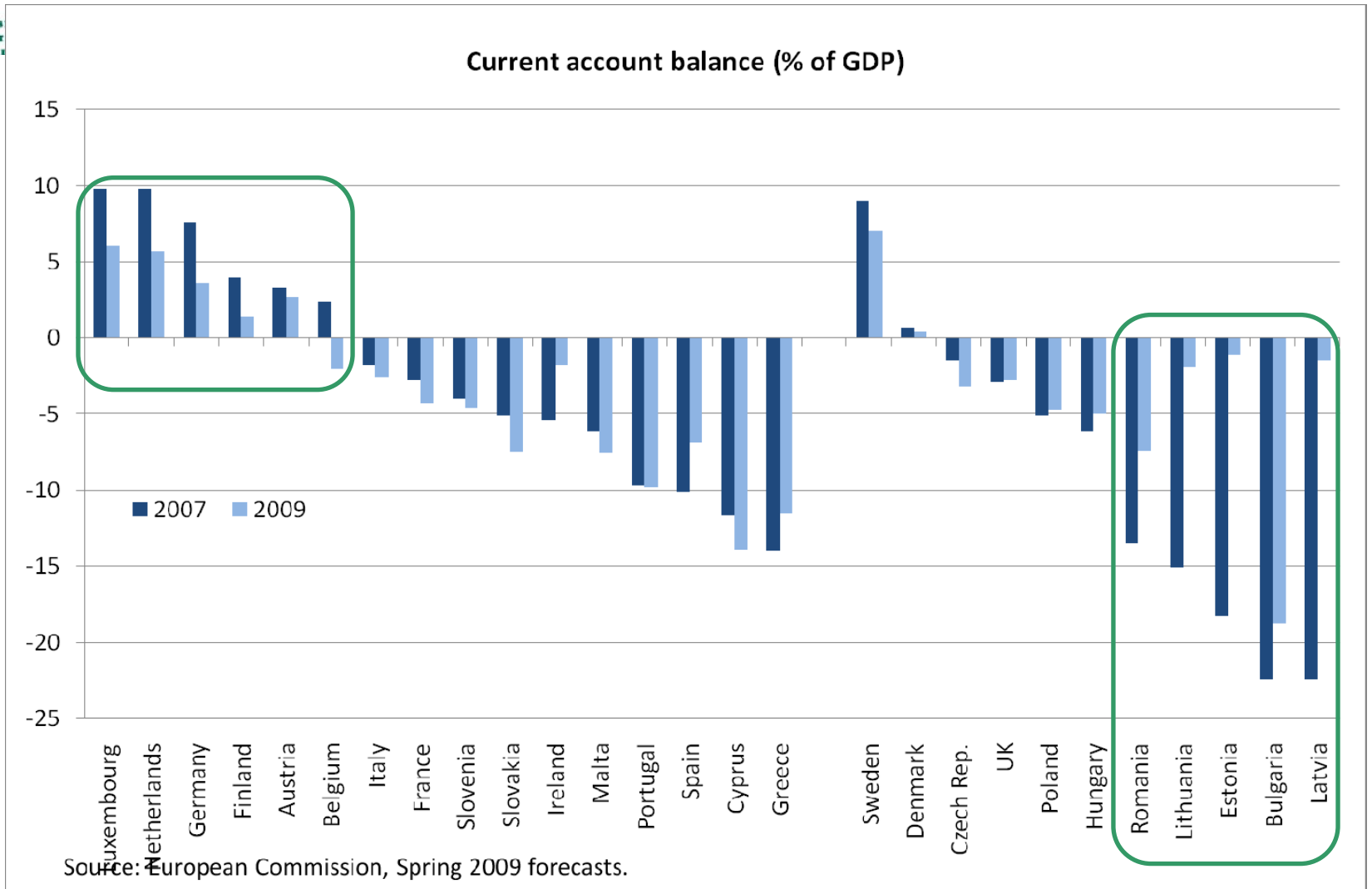


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A heterogeneous area

6. Sudden stops





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A heterogenous area IMF intervention

(As of May 5, 2009; millions of U.S. dollars)

Country	Date	Total Amount Agreed/Type	Drawn	Other Collaborators
Moldova	May 2006	166 (PRGF)	152	
Ukraine	Nov 2008	16,446 (SBA)	4530	
Hungary	Nov 2008	15,754 (SBA)	9453	EU, WB
Latvia	Dec 2008	2,275 (SBA)	800	EU, Nordic and other bilateral donors, WB, EBRD
Belarus	Jan 2009	2,419 (SBA)	774	
Serbia	Jan 2009	524 (SBA)**	0	
Romania	Mar 2009	17,100 (SBA)	0	EU, WB, EBRD, EIB
Poland	Apr 2009	20,500 (FCL)**	0	

*PRGF stands for Poverty Reduction and Growth Facility; SBA stands for Stand-By Arrangement; FCL stands for Flexible Credit Line.

Source: IMF, *Regional Economic Outlook Europe*, May 2009.

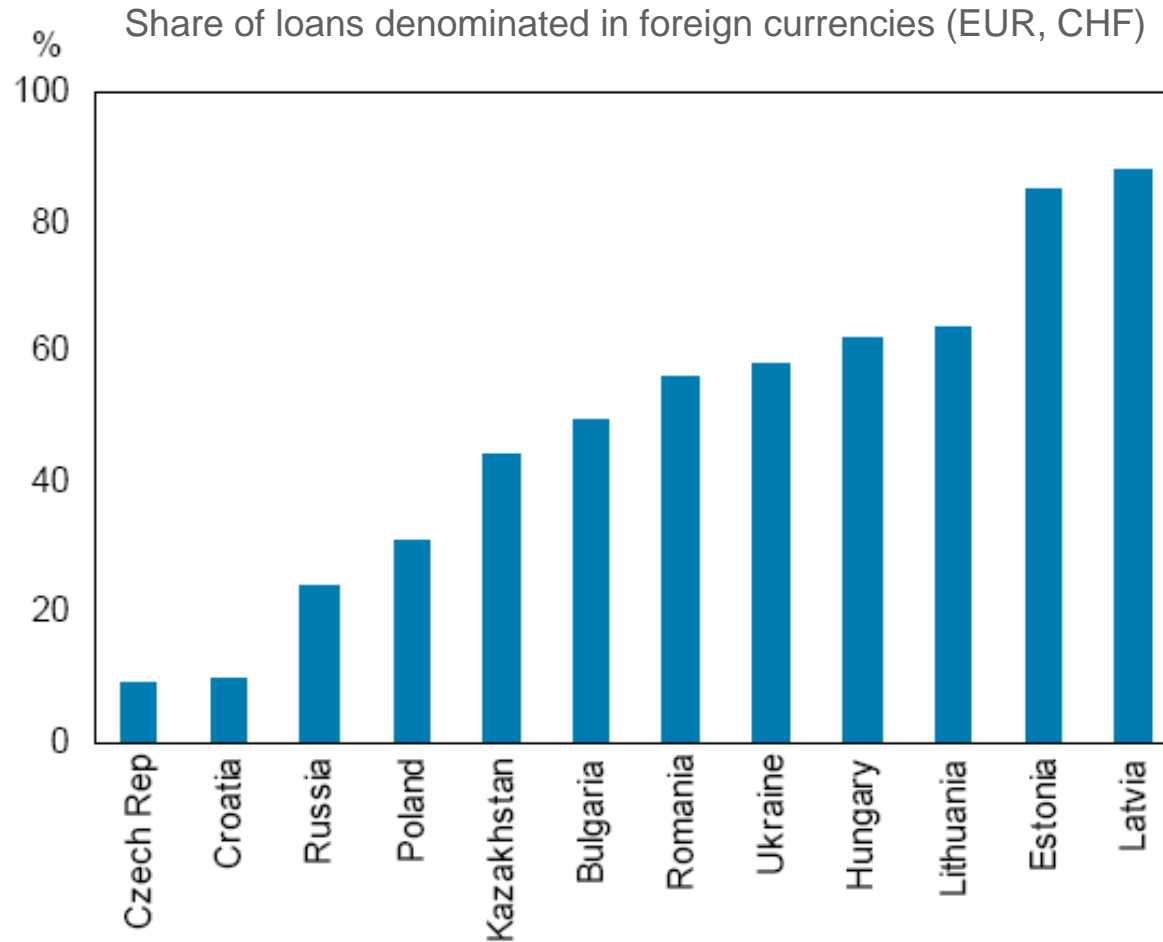


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Why such differences ?

7. « Original sin »



Source: Goldman Sachs.

Policy actions so far



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EU/Eurozone level

Monetary policy (ECB)

- Interest-rate cuts
- Quantitative easing (?) May 7, 2009

Fiscal policy

- 1.5% of GDP (€ 200 bn)
- “TTT” (targeted, temporary, timely)
- European Investment bank: € 30 bn loans to SMEs
- Trans-European infrastructure projects (€ 5 bn)

Banks

- Refinancing (ECB)
- All systemic institutions will be rescued
- Minimum deposit guarantees (€ 50 000)
- DG competition
- Colleges of supervisors

Financial markets

- Rating agencies
- de Larosière Report

Member-State level

Monetary policy (UK)

- Interest-rate cuts
- Quantitative easing

Fiscal policy

- Automatic stabilizers
- Public investment
- Targeted loans (transport equipt, SMEs)
- Social relief
- Tax cuts

Banks

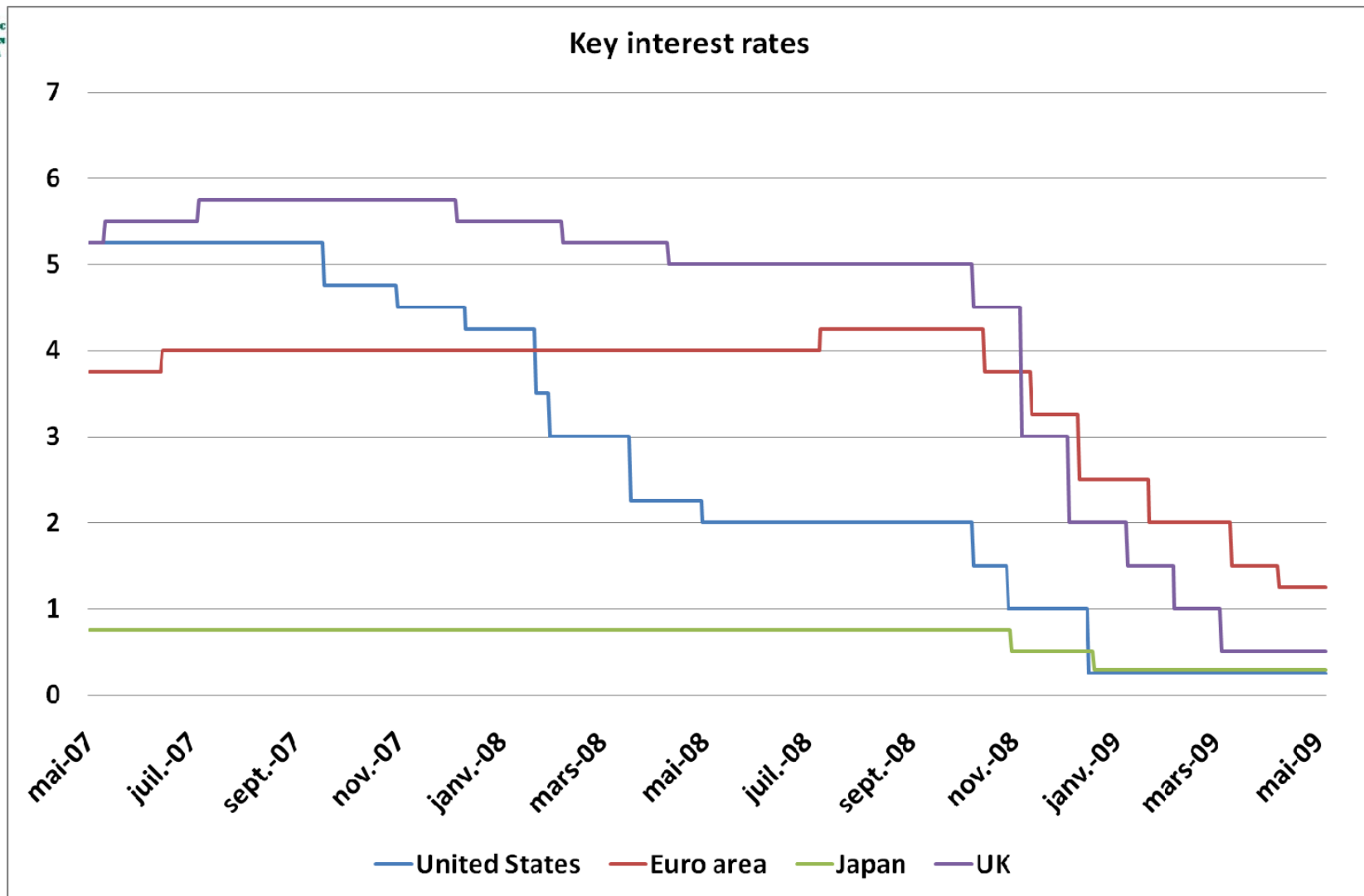
- Refinancing (UK)
- Public guarantees
- Recapitalizations



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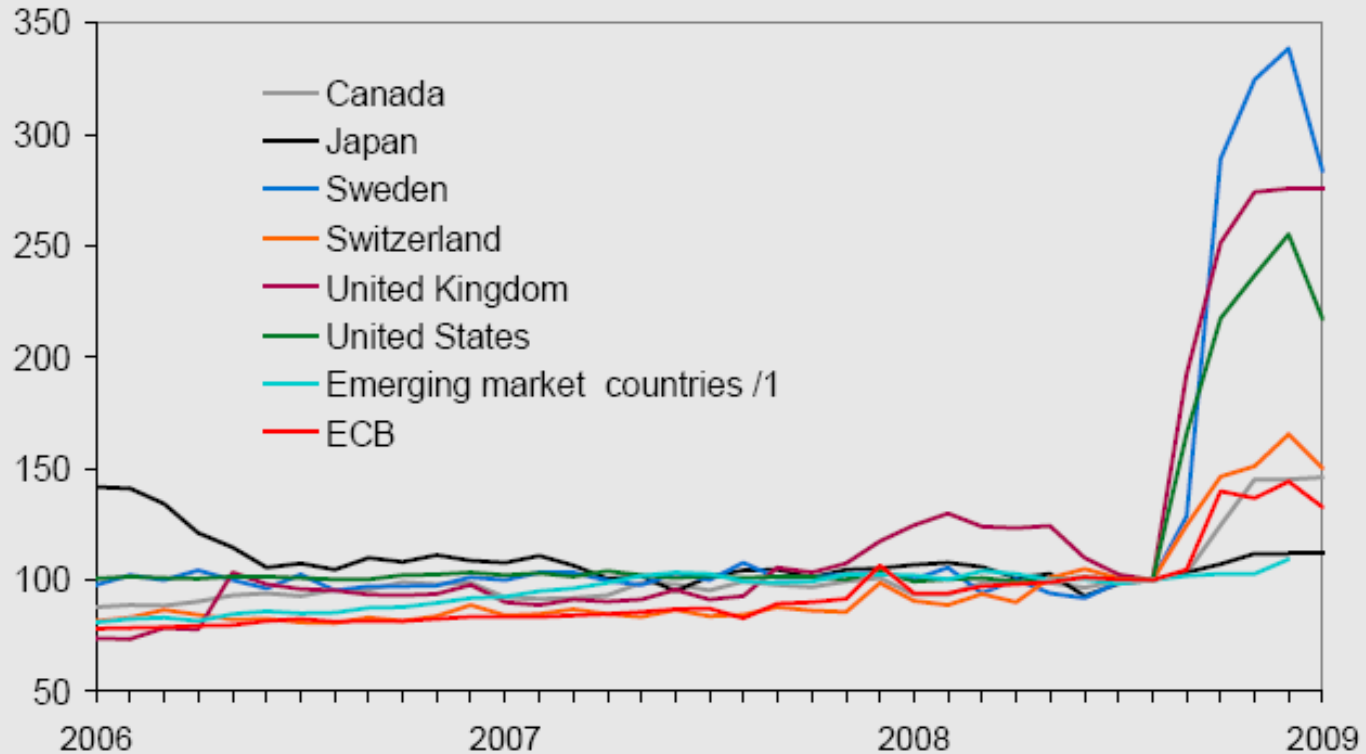
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Interest-rate cuts



Liquidity provision and quantitative easing

Real Central Bank Assets of Selected Countries, January 2006-March 2009
(August 2008 = 100)



Source: IMF, International Financial Statistics database.
/1 Median for 27 medium and large emerging market countries.

Source: IMF, *Financial Stability Report*, April 2009.

Government support to banks

Government Support to Banks, 2008-2009

(As of April 15, 2009; percent of 2008 GDP)

	Capital Injection	Purchase of Assets and Lending by Treasury	Guarantees 1/
Austria	5.3	0.0	30.0
Belgium	4.7	0.0	26.2
France	1.2	1.3	16.4
Germany	3.8	0.4	18.0
Greece	2.1	3.3	6.2
Ireland	5.3	0.0	257.0
Italy	1.3	0.0	0.0
Netherlands	3.4	2.8	33.7
Norway	2.0 2/	15.8 2/	0.0
Portugal	2.4	0.0	12.0
Spain	0.0	4.6	18.3
Sweden	2.1	5.3	47.3
Switzerland	1.1	0.0	0.0
United Kingdom	3.9	13.8	51.2
Average 3/	2.5	3.7	25.0

Source: IMF, FAD-MCM database on public interventions.

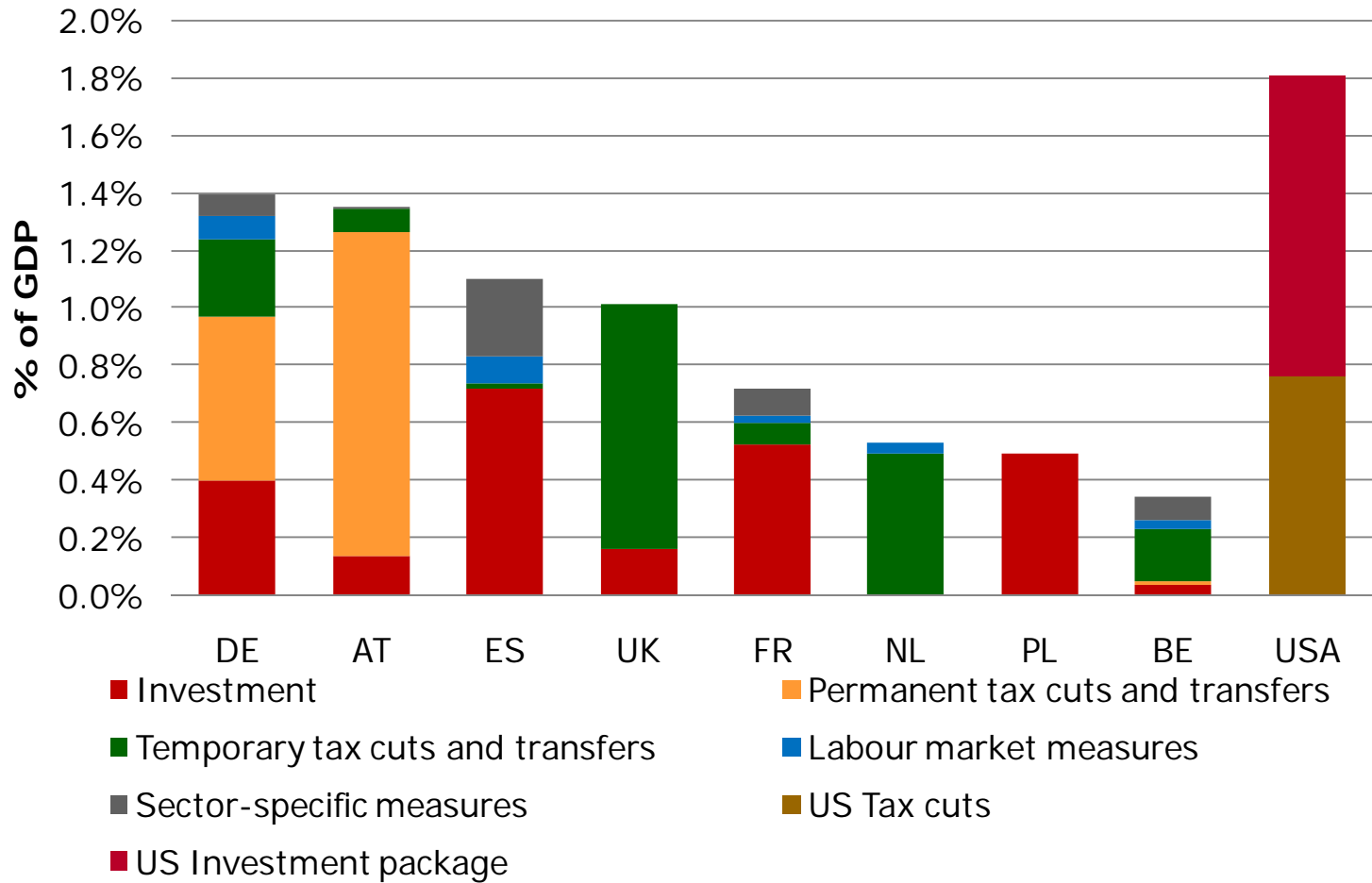
1/ Excludes deposit insurance provided by deposit insurance agencies.

2/ Maximum amount allowed under the legislation.

3/ PPP GDP weights.

Source: IMF, *Regional Economic Outlook Europe*, May 2009.

Heterogenous fiscal packages



Source: Bruegel.

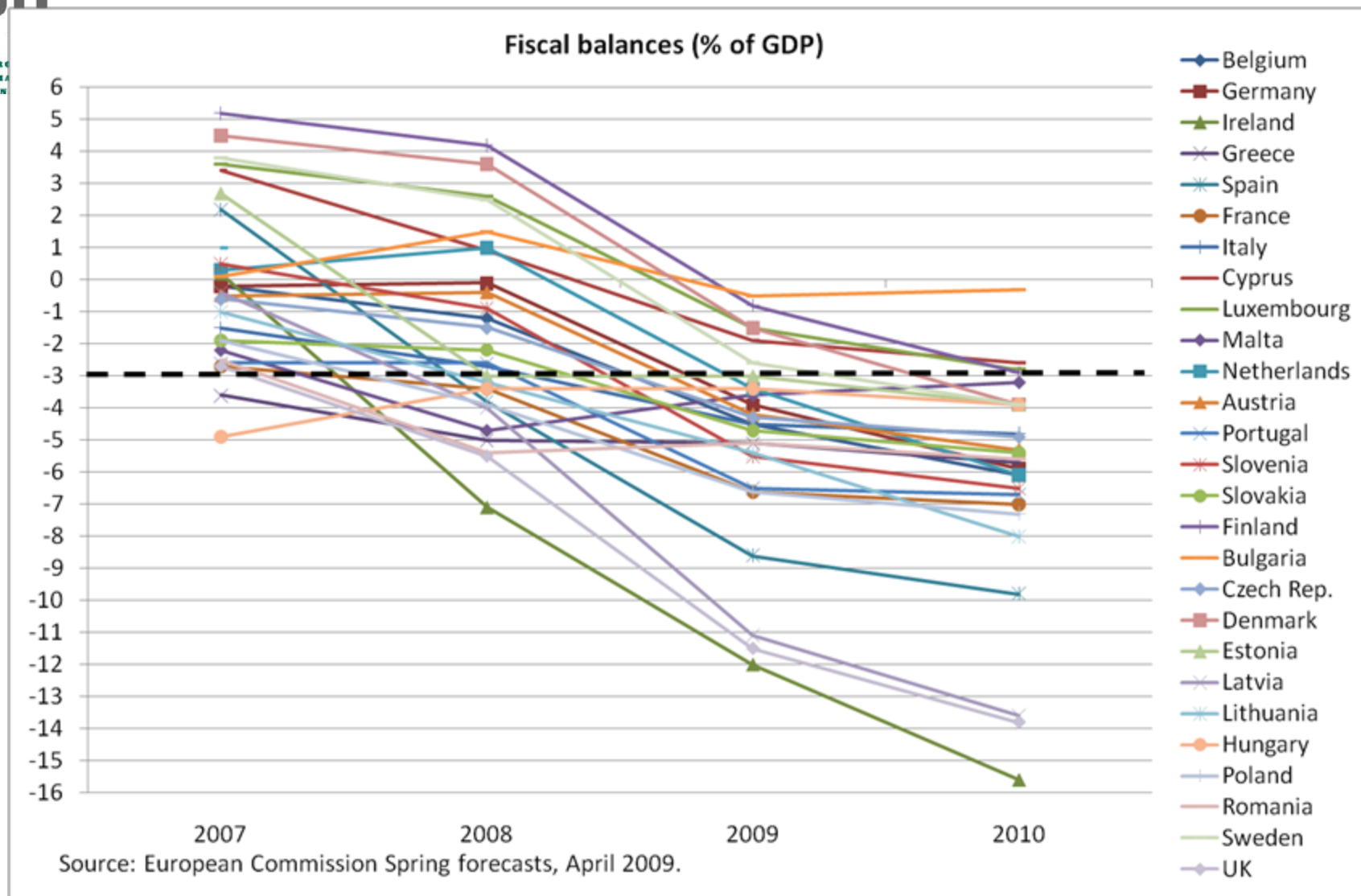
Policy actions taken in France

- **Bank rescue**
 - Recapitalisations:
 - Dexia (€ 1 bn)
 - Super-subordinated debt (through *Société de prise de participation de l'Etat*): € 10.5 bn
 - Medium-run refinancing
 - *Société de Refinancement de l'Economie Française*
 - Public guaranteed debt (up to € 265 bn)
- **Fiscal stimulation package** (Dec. 4, 2008) : € 26 bn (1.3 % of GDP)
 - € 11.6 bn: support to corporate sector (accelerated depreciation, early tax refunds, cuts in social contributions for SMEs)
 - € 10.5 bn: public investment
 - € 2 bn: housing and car sector (scrappage incentive, loans to industry)
 - € 2 bn: unemployment benefits, subsidized jobs, support to low and medium-income households (minimum income , personal income first bracket tax cut, school allowance)
- **Support to SMEs**
 - € 17 bn: use of regulated savings to finance SMEs
 - Public guarantees on SMEs borrowings (through *OSEO*)



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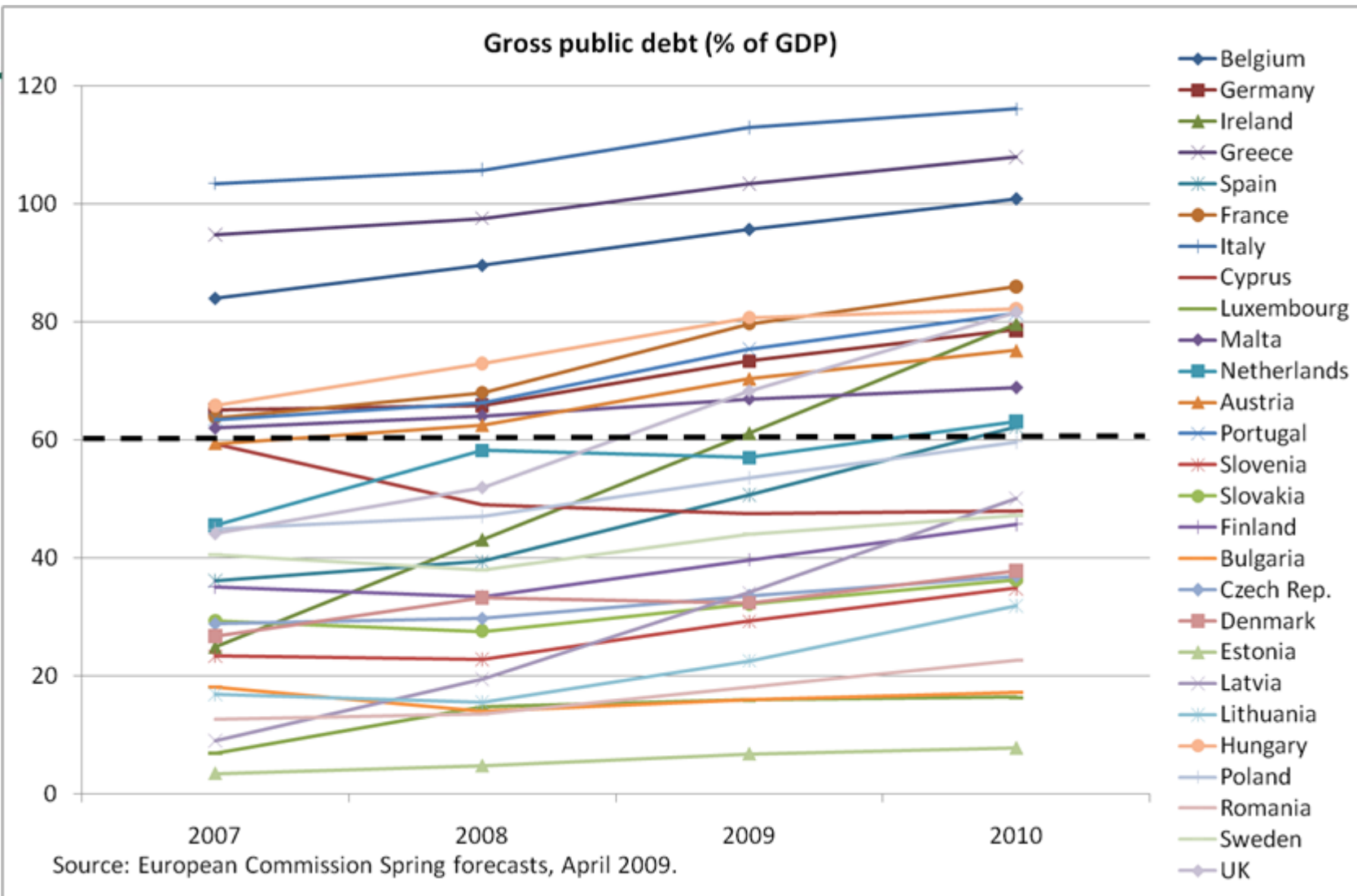
SGP: exceptional circumstances





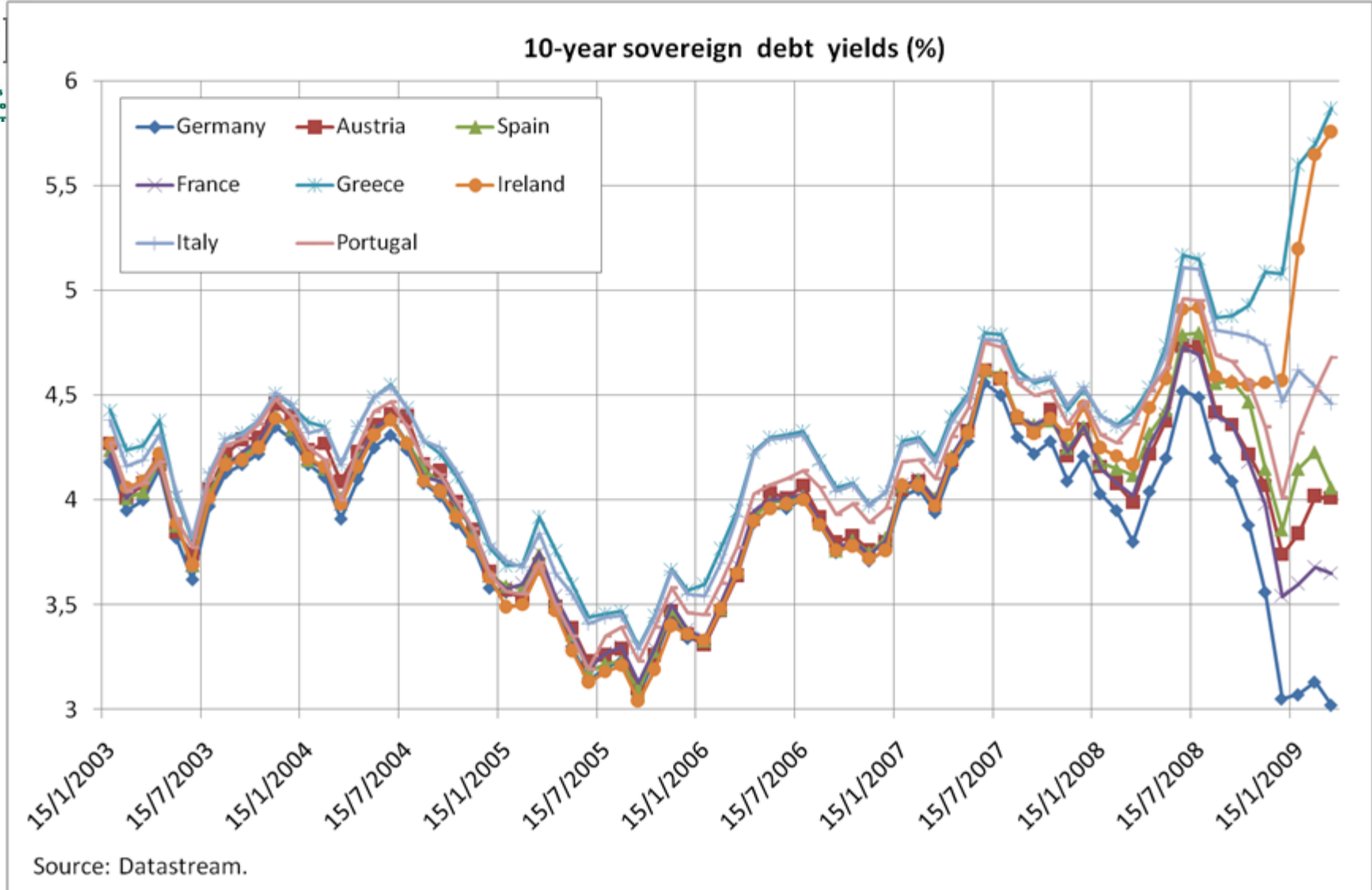
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SGP: exceptional circumstances





But constrained policies





Banks: limited writedowns

Table 1.4. Bank Equity Requirement Analysis

(in billions of dollars, unless shown)

	United States ¹	Euro Area	United Kingdom
Estimated Capital Positions at end-2008			
Total reported writedowns to end-2008	510	154	110
Capital raised to end-2008	391	243	110
Tier 1/RWA ratios at end-2008	10.4%	7.3%	9.2%
TCE/TA end-2008	3.7%	2.5%	2.1%
Scenario Bringing Forward Writedowns			
Expected Writedowns 2009-10 (1)	550	750	200
Writedown-adjusted Tier 1/RWA ratio	6.7%	1.1%	4.7%
Writedown-adjusted TCE/TA	0.1%	-0.2%	0.4%
Allowance for Expected Earnings			
Expected net retained earnings 2009 and 2010 (2) (after taxes and dividends)	300	600	175
Net drain on equity (retained earnings) 2009 and 2010 (3) = (1) - (2)	250	150	25

¹Excludes government-sponsored enterprises, which are expected to receive equity injections from the government of up to \$250 billion to help support writedowns.

²Denmark, Iceland, Norway, Sweden, Switzerland.

³The approximate leverage assumed in the GFSR deleveraging scenario (a 4 percent TCE/TA ratio).

⁴The approximate leverage multiple of U.S. banks in the mid-1990s (a 6 percent TCE/TA ratio), prior to the build-up in leverage in the banking system that contributed to the crisis.

Note: Tier 1 = Tier 1 capital; RWA = risk-weighted assets; TA = tangible assets; TCE = tangible common equity.



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Policy actions *not* taken so far

Banks:

- Systematic stress-testing
- Temporary nationalization/restructuring + bad bank schemes
- EU-wide credit growth requirements

Monetary policy:

- Quantitative easing (Eurozone)

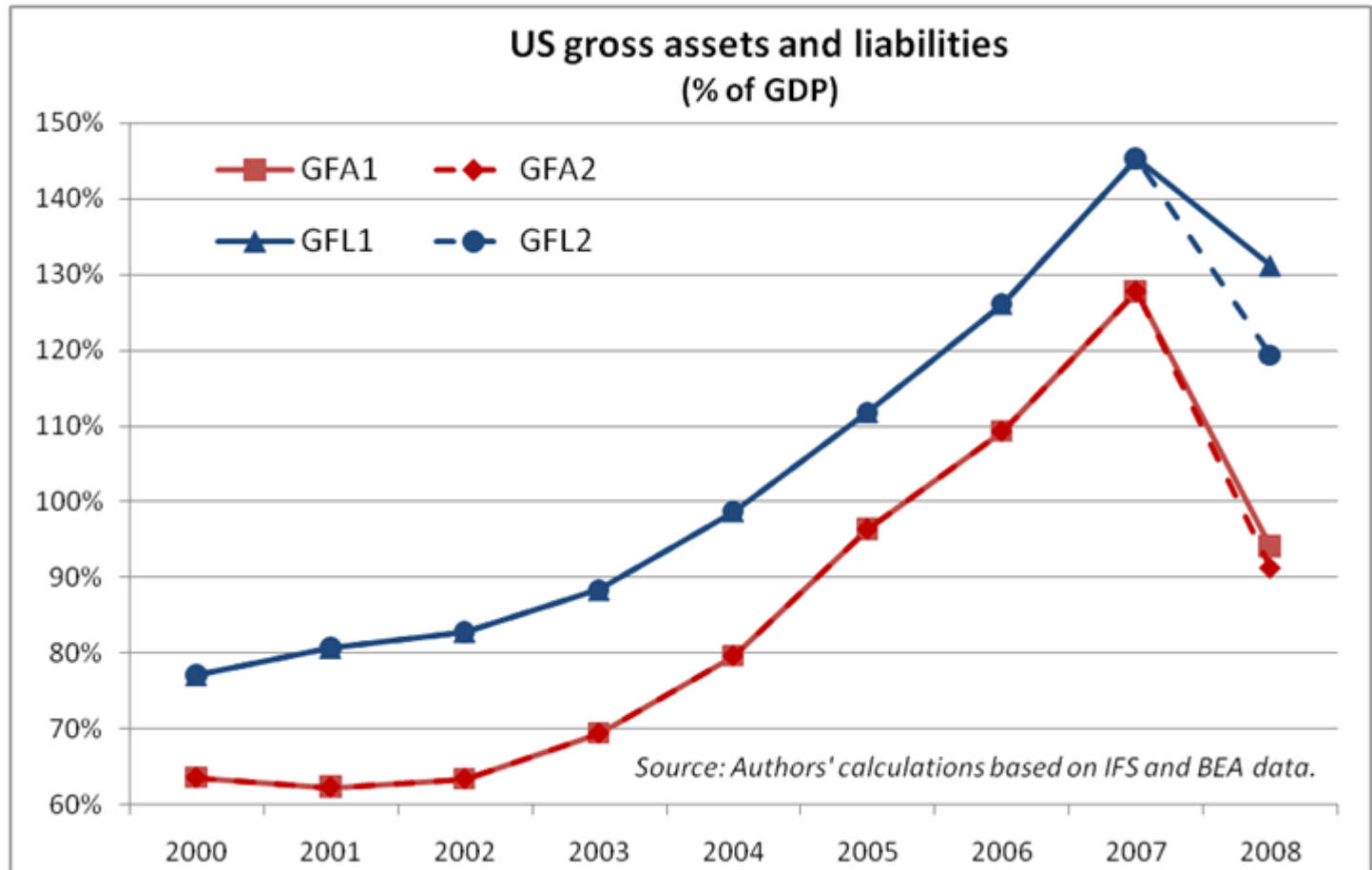
Fiscal policy:

- Coordinated stimulus
 - size
 - composition (consumption/investment, temporary/permanent)
- EU-level support to industries
- Exit strategies

Exchange-rate policy:

- Risk of a dollar crisis
 - Fall in US NFA by 15 to 25 % of GDP between end-2007 and end-2008

The US NFA has deteriorated

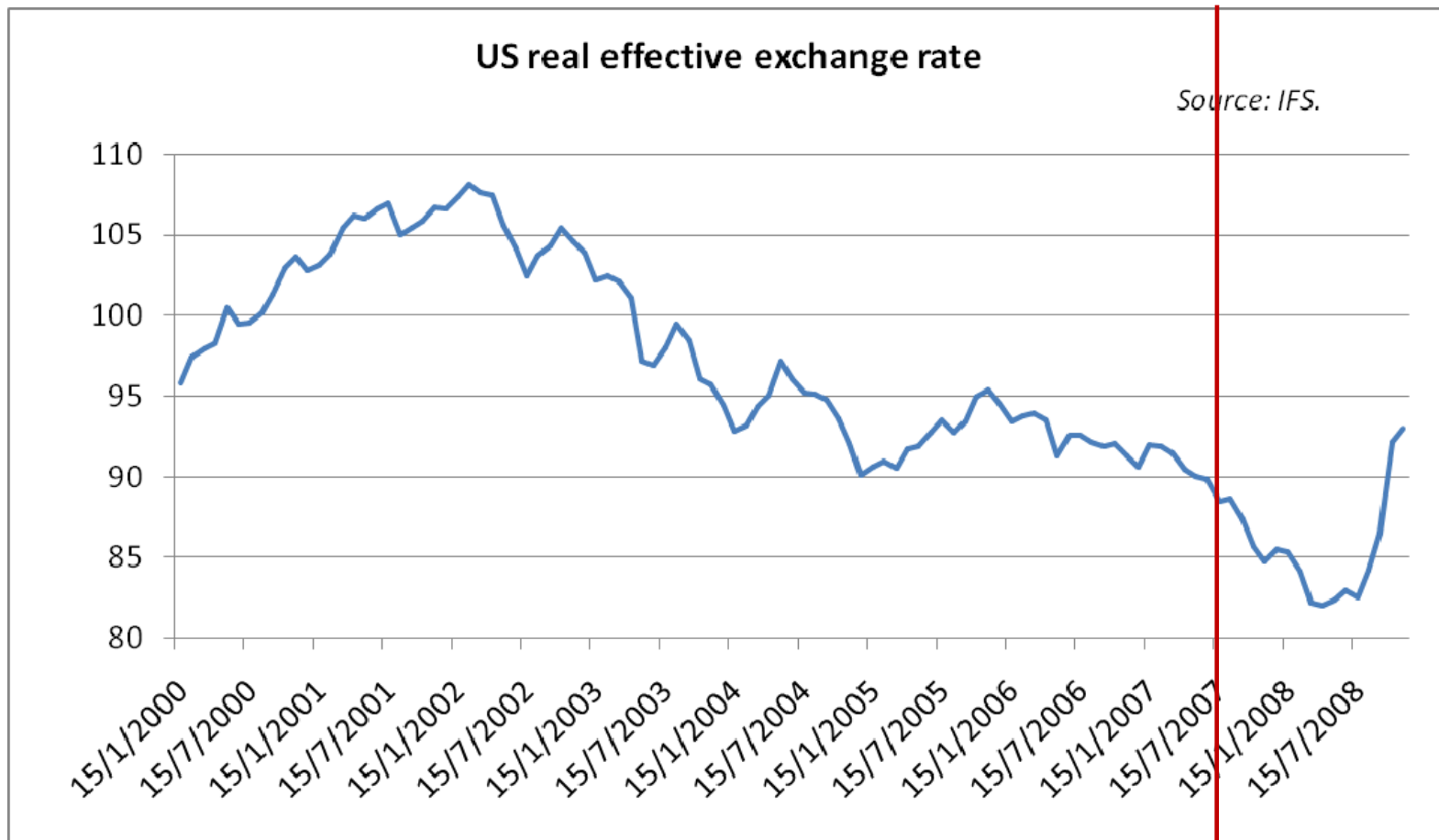




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A risk on the US dollar





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Key issues

Banks: a European plan

- Systematic stress-testing
- Temporary nationalization/ restructuring + bad bank schemes
- EU-wide credit growth requirements

Coordination between monetary and fiscal policy:

- Quantitative easing:
 - ✓ secure ECB's independence: risk sharing, public debt sustainability
 - ✓ provide credible fiscal commitments:
 - tax bases
 - contingent commitments beyond present SGP
 - ✓ ECB should take the lead

Exchange-rate policy:

- Get ready to issue exchange-rate policy orientation (consensus between Eurogroup and ECB)

Prepare for the future:

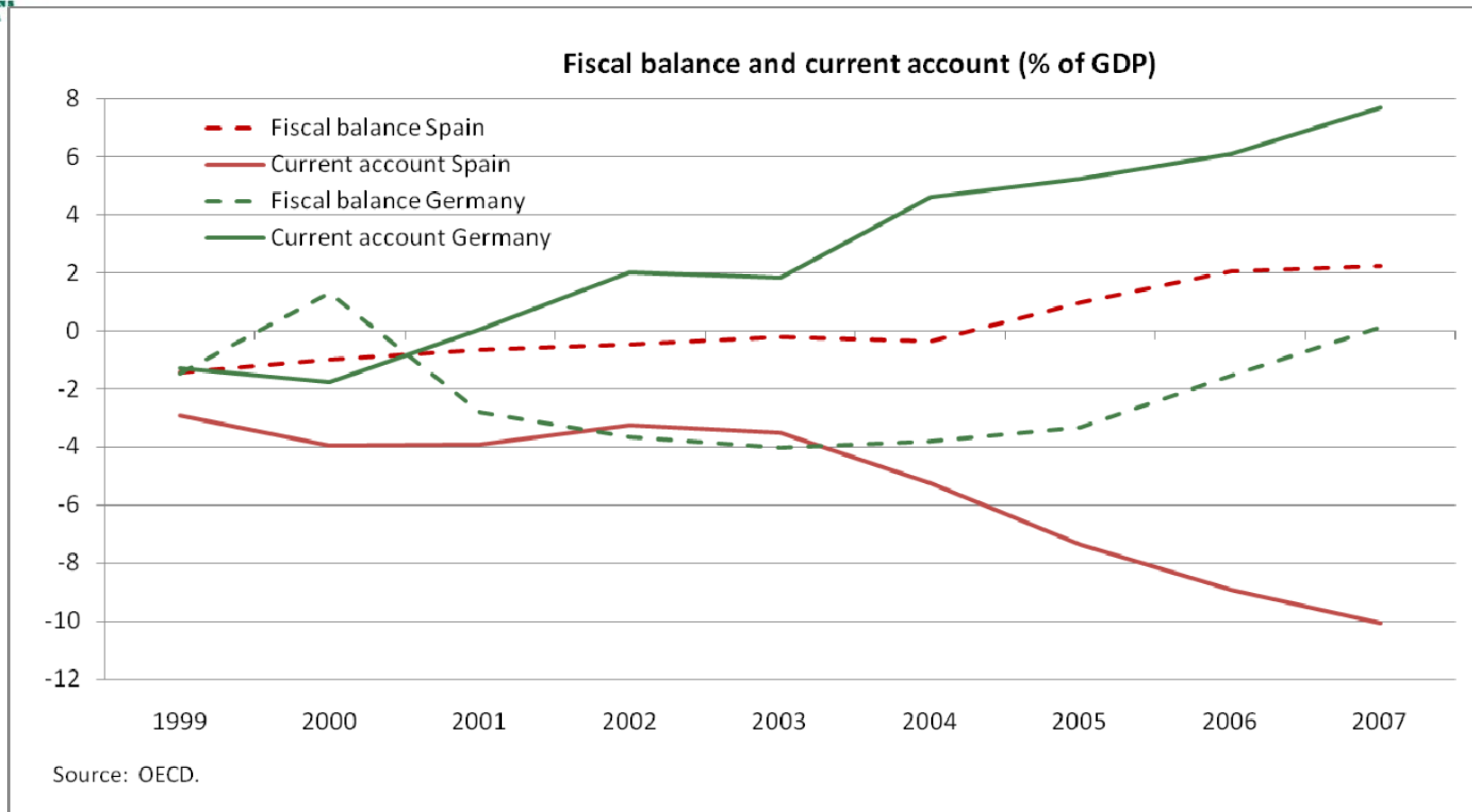
- Broad Economic Policy Guidelines
 - ✓ Public/private spending
 - ✓ Mortgage market rules
- Tax coordination



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Policy surveillance: too much focus on public savings

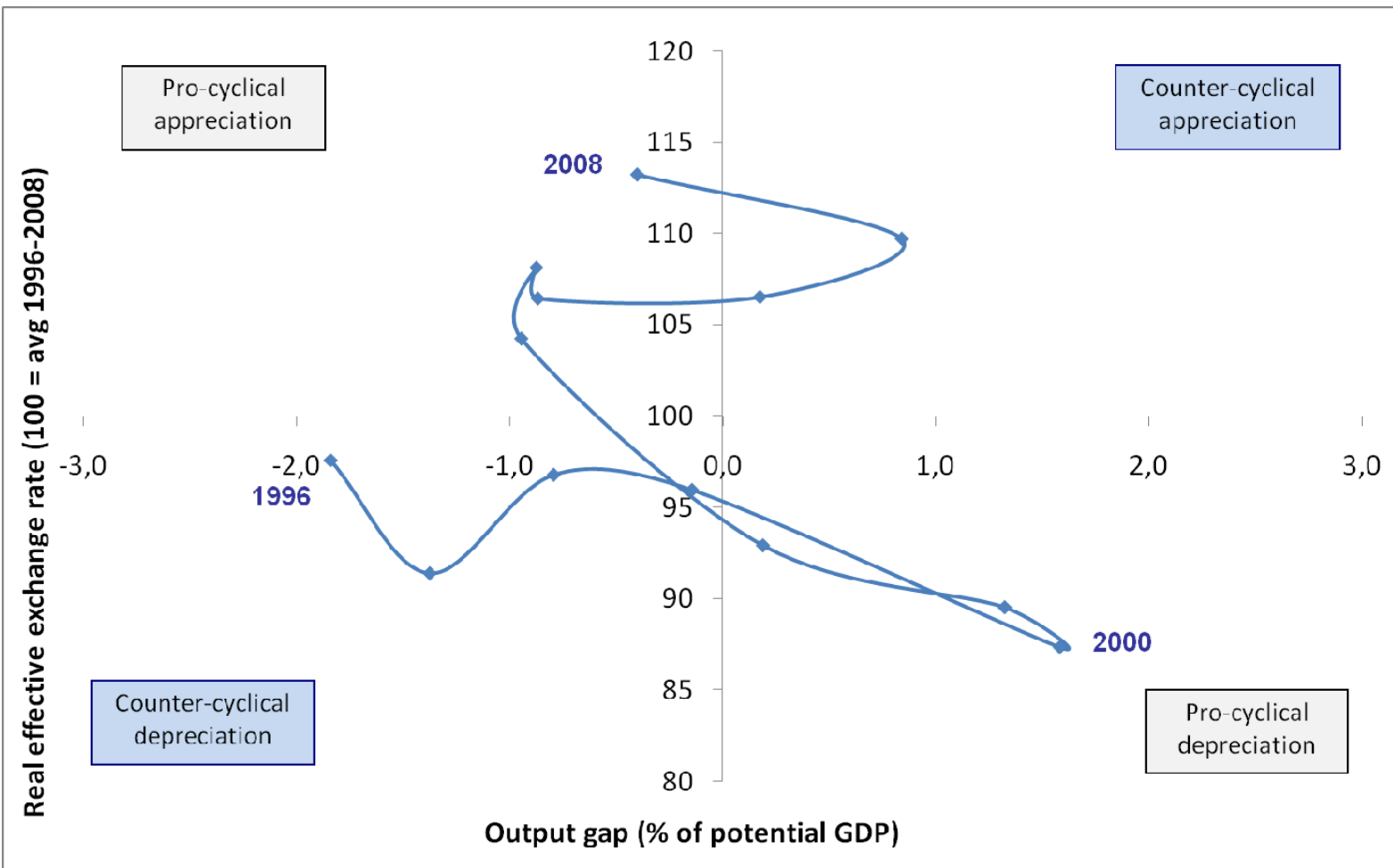




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An exchange-rate policy in Europe...



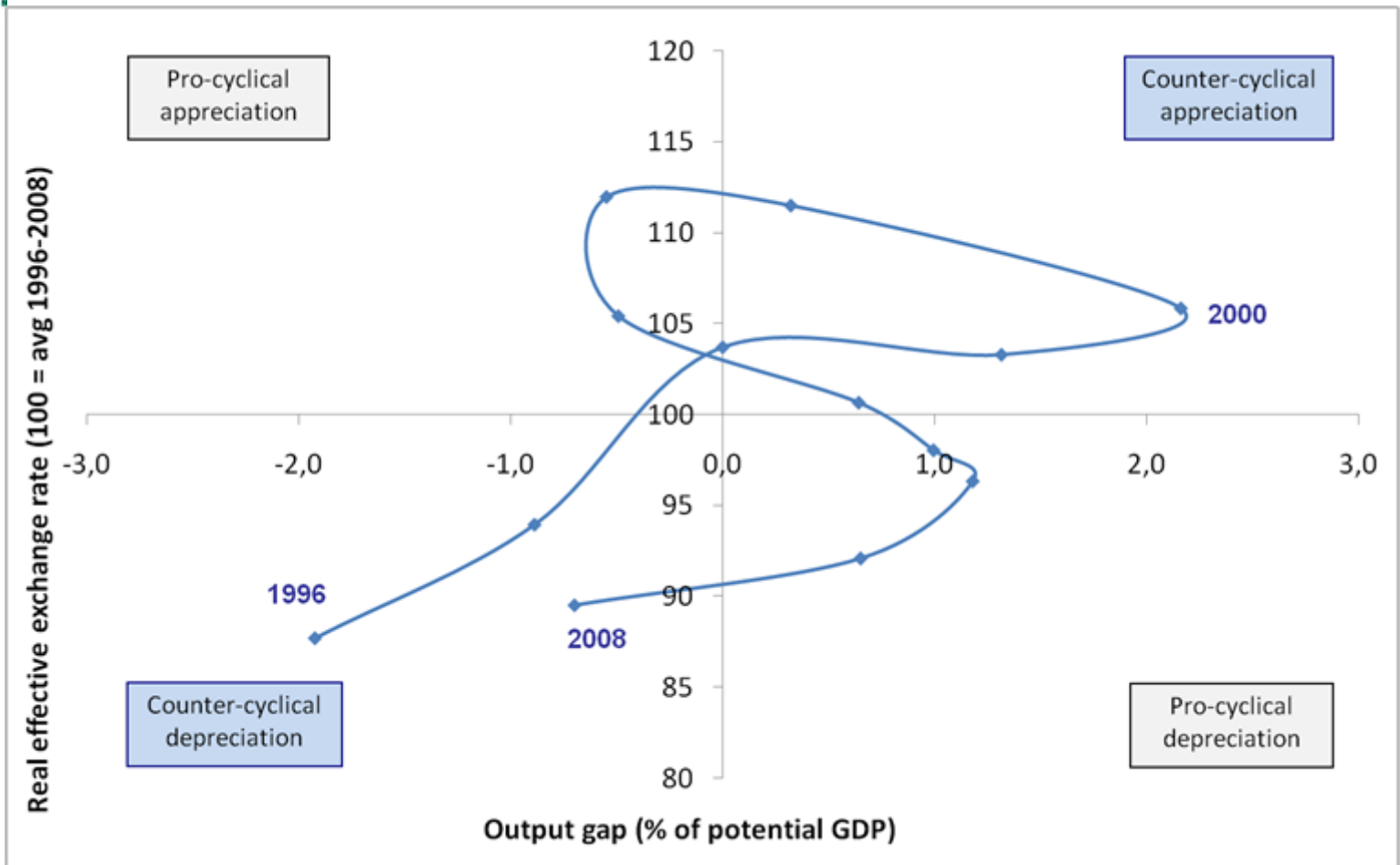
Source: Bénassy-Quéré, Coeuré, Jacquet and Pisani-Ferry (2009).



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... like in the United States ?



Source: Bénassy-Quéré, Coeuré, Jacquet and Pisani-Ferry (2009).