



The European economy after the crisis

Klaus Regling, Managing Director ESM

Singapore

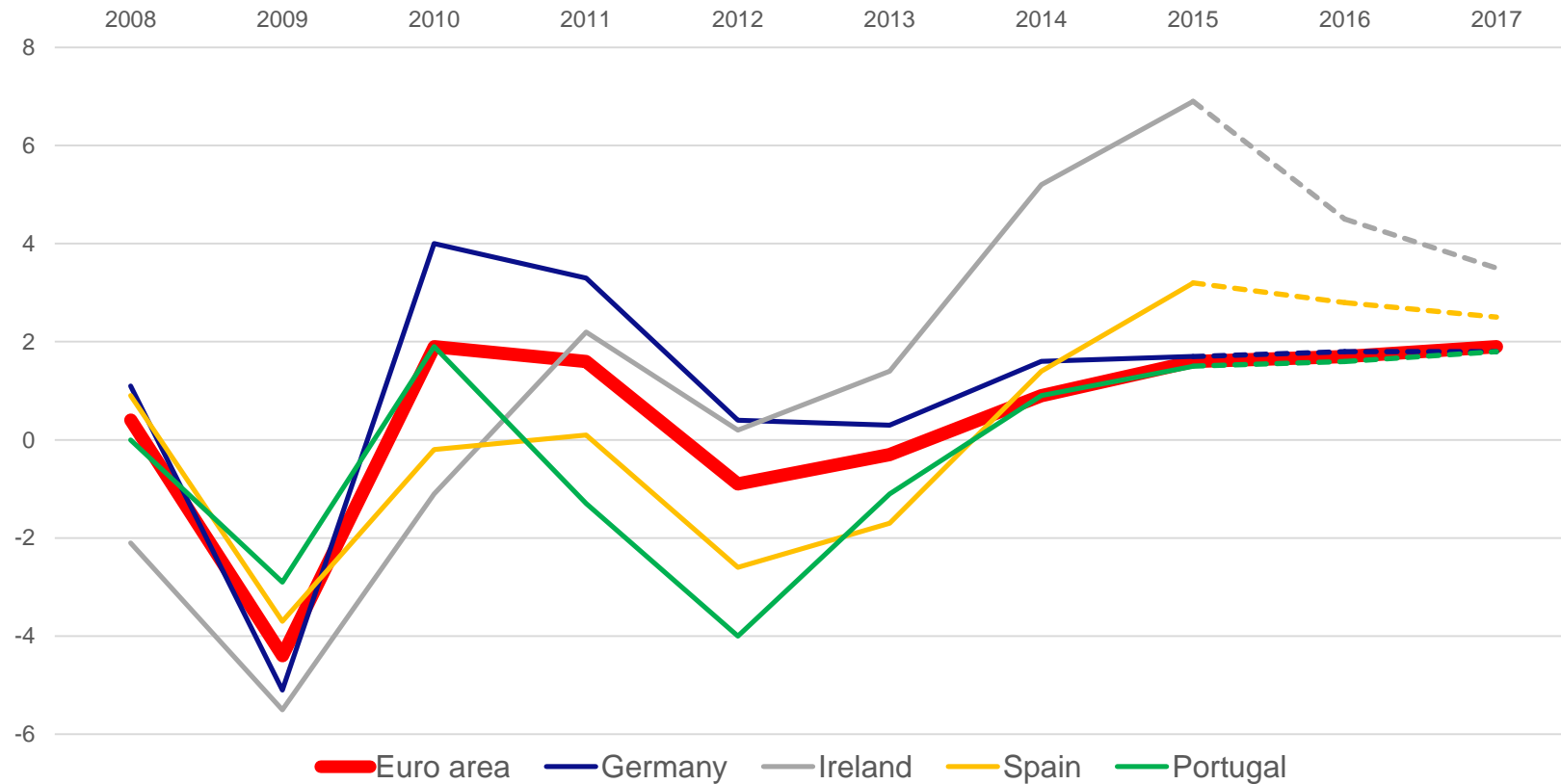
18 February 2016

The European economy after the crisis

1. Growth in Europe back to normal - some bright spots, some weaknesses, some risks
2. Europe's comprehensive crisis response
3. What remains to be done?

1. Growth in Europe: back to normal

Real GDP growth year/year (%)

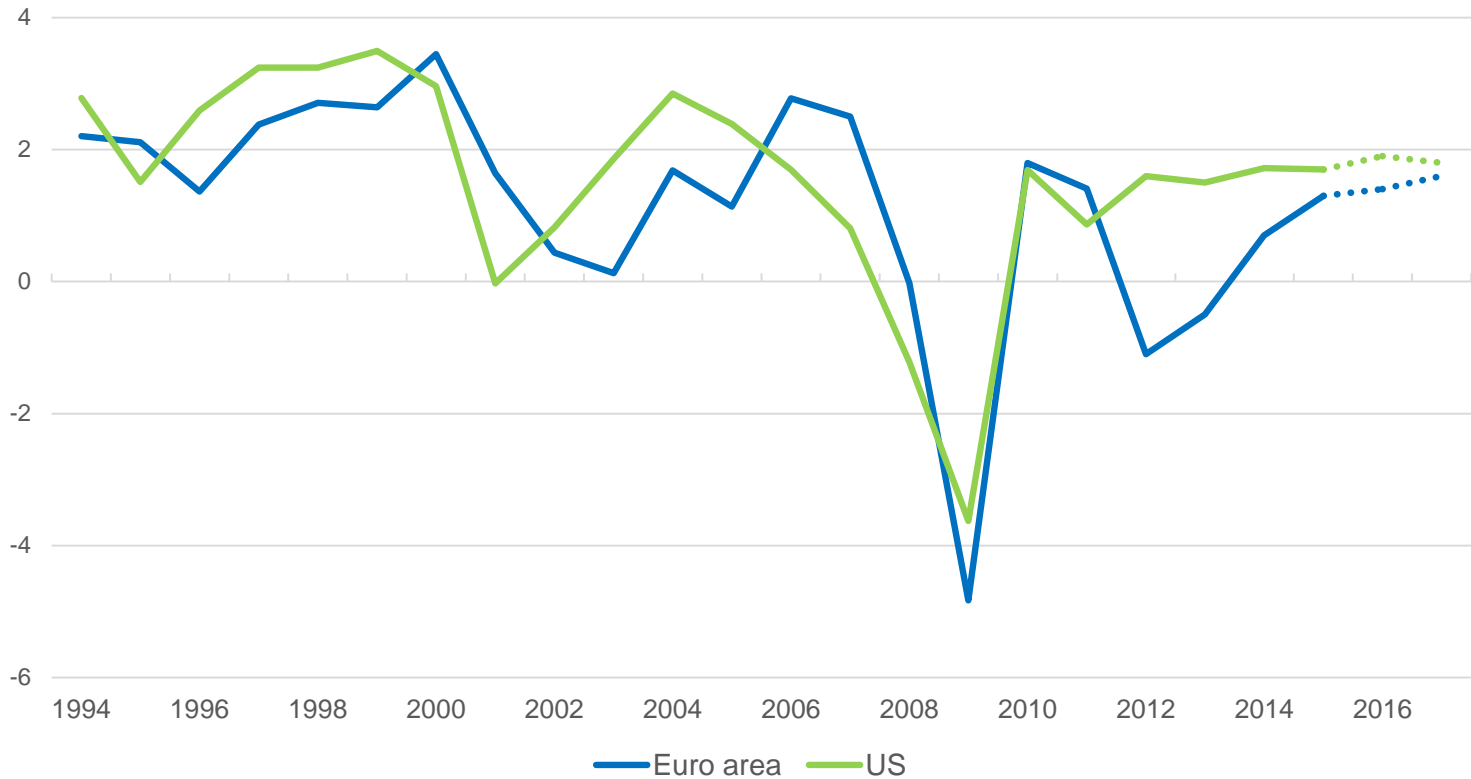


But: new headwinds

Source: EC European Economic Forecast – Winter 2016
Figures for 2015 – 2017 are forecasts

Growth in Europe is moving in line with the U.S. again...

Per capita growth in US and EU is similar



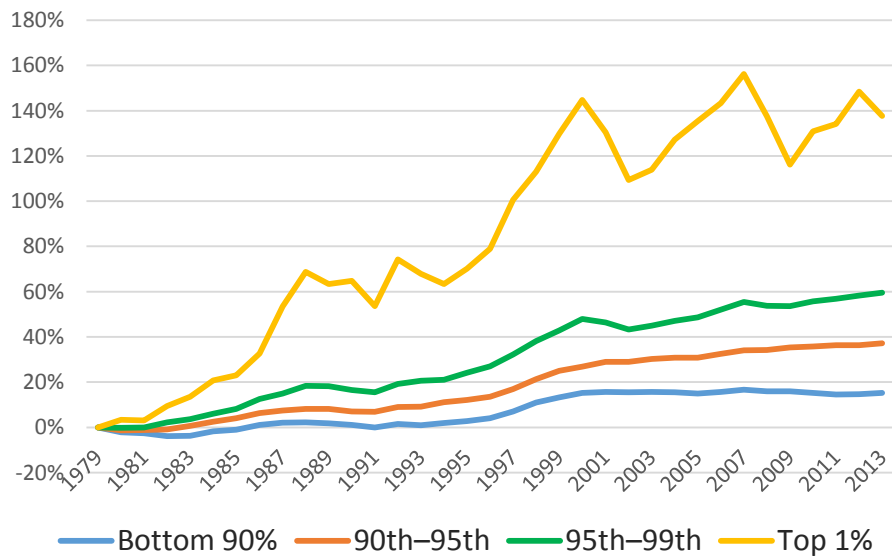
Average GDP growth per capita, 1999-2008

euro area	1.6%
US	1.6%

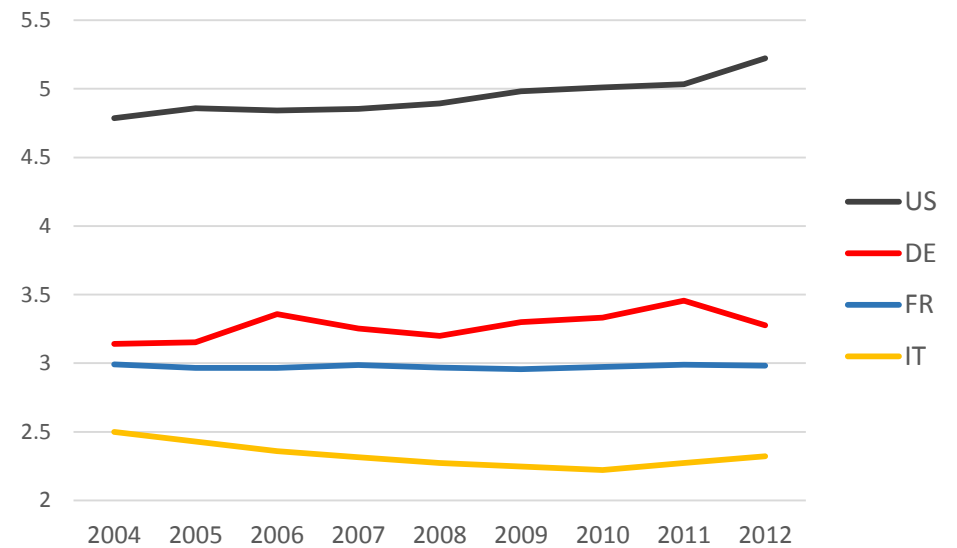
Source: EC European Economic Forecast - Winter 2016

...but income equality in Europe is much greater than in the U.S.

Cumulative % change in real wages by wage group in the US



Ratio of highest 10% earners vs lowest 10% earners in U.S. and European countries



Source: Economic Policy Institute (left chart), OECD (right chart). Right-hand chart data are for gross earnings of full-time dependent employees.

Europe was confronted by two crises

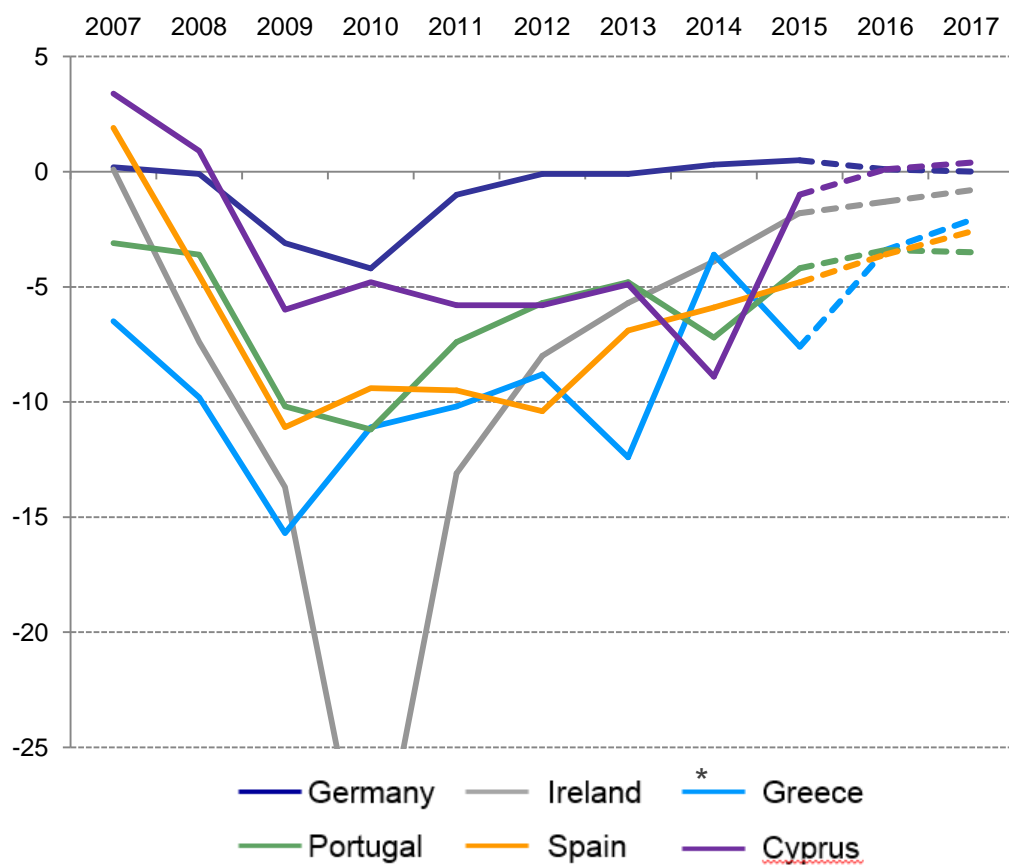
- Global financial crisis in 2008-09
 - Sub-prime mortgage collapse, triggered in US
 - Excess liquidity, risk premia too low
- Sovereign debt crisis in Europe followed in 2010
 - Unsustainable budget deficits and debt, lack of competitiveness and housing bubble in several countries
 - Gaps in the EU institutional set-up
 - Insufficient supervision of the financial industry
 - The unthinkable happened: several countries lost market access
 - A break-up of the euro area became a real threat
- A comprehensive response: Europe has made great strides towards closer integration

2. Europe's comprehensive response to the crisis

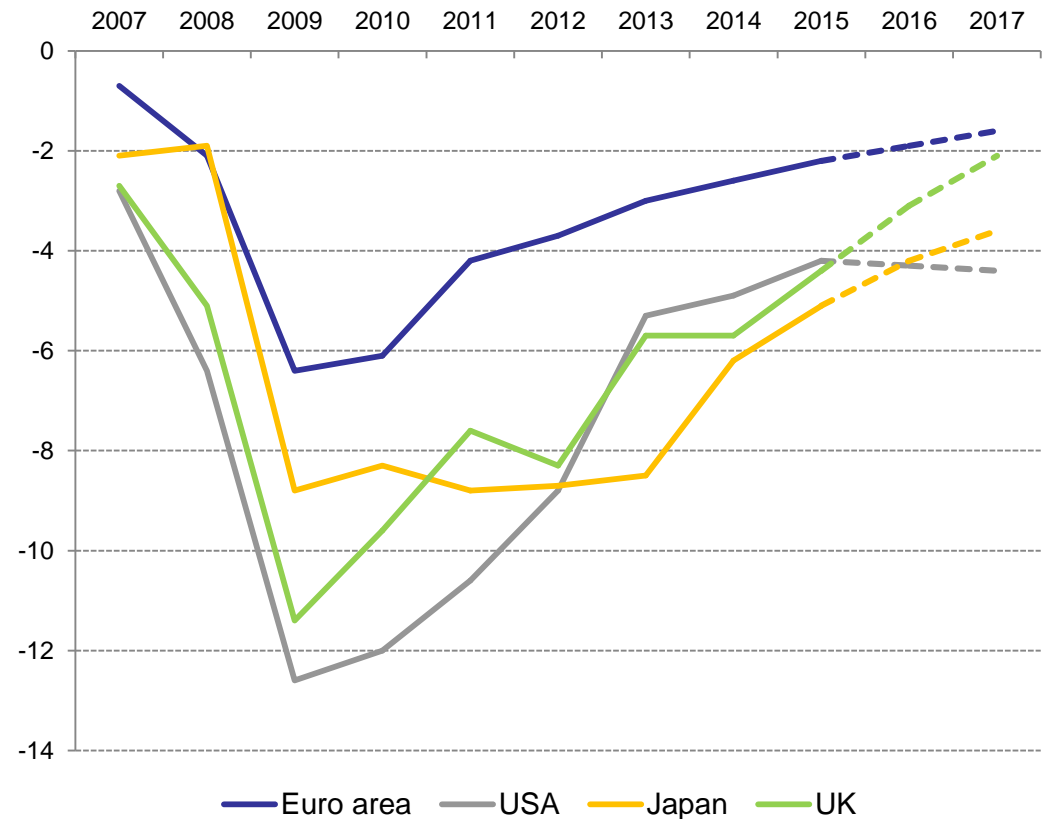
- a) Budget consolidation and structural reform in euro area countries
- b) An active monetary policy
- c) Closer economic policy coordination in the currency union
- d) Strengthening the banking system
- e) Firewalls against the crisis: EFSF and ESM

a) Deficit reduction policies are paying off

Fiscal balance in programme countries (% of GDP)



Selected comparative fiscal balances (% of GDP)



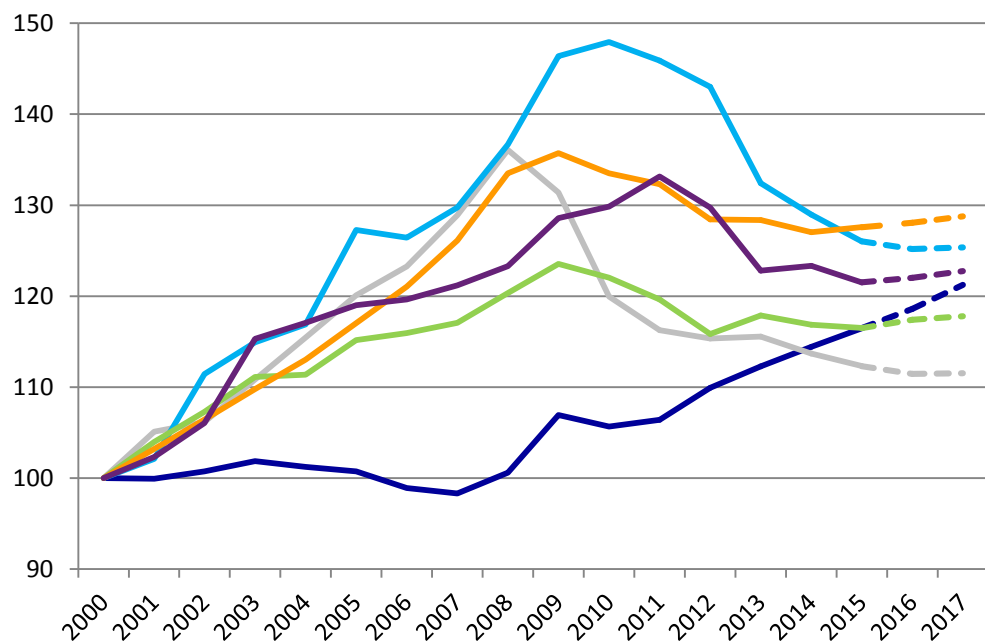
Source: European Commission Economic Forecast – Winter 2016

* Actual figure for Ireland in 2010: -32.4%

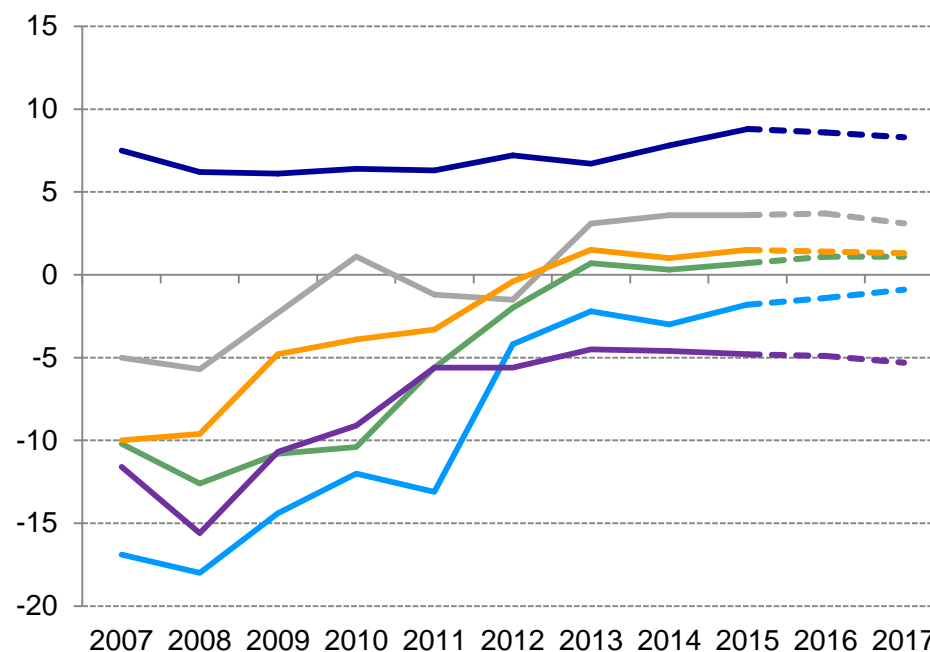
Internal devaluations are restoring competitiveness

- Thanks to the convergence in competitiveness, costly external imbalances in the periphery have disappeared

Nominal unit labour costs (2000=100)



Current account balance (% of GDP)



— Germany — Ireland — Greece
— Portugal — Spain — Cyprus

Source: EC European Economic Forecast – Winter 2016

Programme countries are reform champions

- **Greece, Ireland, Portugal and Spain** are in top five of 34 **OECD countries** with regard to implementation of **structural reforms**.

Ranking in OECD report
1. Greece
2. Ireland
3. Estonia
4. Portugal
5. Spain

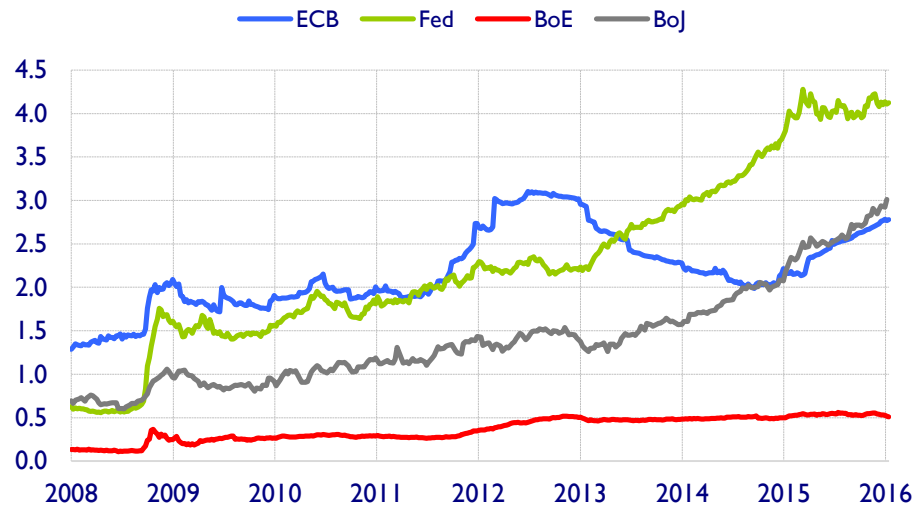
“Euro area countries under financial assistance programmes are among the OECD countries whose responsiveness [to the OECD’s structural reform recommendations] was highest and also where it most increased compared with previous period.”

- *Going for Growth* (OECD Report)

Source: OECD report *Going for Growth* for 2015
Ranking takes into account responsiveness to OECD recommendations on structural reforms in key policy areas

b) An active monetary policy

- The ECB has expanded its balance sheet, like other central banks:



Central bank balance sheets in € trillion

Sources: Central banks named in the chart

- ECB provides long-term liquidity to the banking sector
- Purchases government bonds and other securities
- Low interest rates, negative deposit rates
- Banks incentivised to lend more, aim is to boost investor appetite
- Weaker euro improves the external competitiveness of industries

c) Closer economic policy coordination in the currency union

- The EU has tightened surveillance of fiscal policies
 - Stricter Stability and Growth Pact
 - „Fiscal compact“

- Better coordination at European level („European semester“)
 - Countries submit draft budgets to the Commission
 - Recommendations to remove obstacles to growth in countries

- New Procedure to avoid macroeconomic imbalances
 - Broader macroeconomic surveillance
 - Commission recommendations in case of imbalances
 - Possible sanctions

d) Strengthening the banking system

■ New Institutions

- ESRB to monitor macroprudential risks
- New EU supervisory bodies for banks, securities markets and insurance companies

■ Begin of Banking Union

- Single Supervisory Mechanism is overseeing largest banks and problem banks
- Single Resolution Mechanism and Single Resolution Fund
- From bail-out to bail-in: new rules for resolution of banks (BRRD)

■ More bank capital

- EU banks have raised their capital by more than €600 bn since the beginning of the crisis in 2008

e) Firewalls against the crisis: ESM and EFSF

- Maximum lending capacity of €700 bn
 - Lending always linked to conditionality
 - Disbursed to five countries so far: €254.5 bn
 - Ireland, Portugal, Spain, Cyprus, Greece
- Four success stories:
 - Ireland, Portugal, Spain have exited programmes
 - Cyprus will exit in March
 - Greece is a special case
 - It entered a new programme of up to €86 bn last year

Benefits of EFSF/ESM

- Keeping the euro area together
- Cash for reform: promoting reforms and adjustment
 - Like IMF programmes in Brazil, Turkey, South Korea, Indonesia, etc.
- Debt sustainability
 - EFSF/ESM programmes lead to substantial budgetary savings
- Risk sharing
- Lender of last resort for sovereigns

Benefits of EFSF/ESM lending

Savings as a result of EFSF/ESM financing vs theoretical market cost (for 2014)

	In € billion	As percentage of GDP	As percentage of total primary expenditures
Cyprus	0.26	1.5	4.3
Greece	7.87	4.4	10.86
Ireland	0.09	0.05	0.15
Spain	0.82	0.08	0.21
Portugal	0.49	0.28	0.69

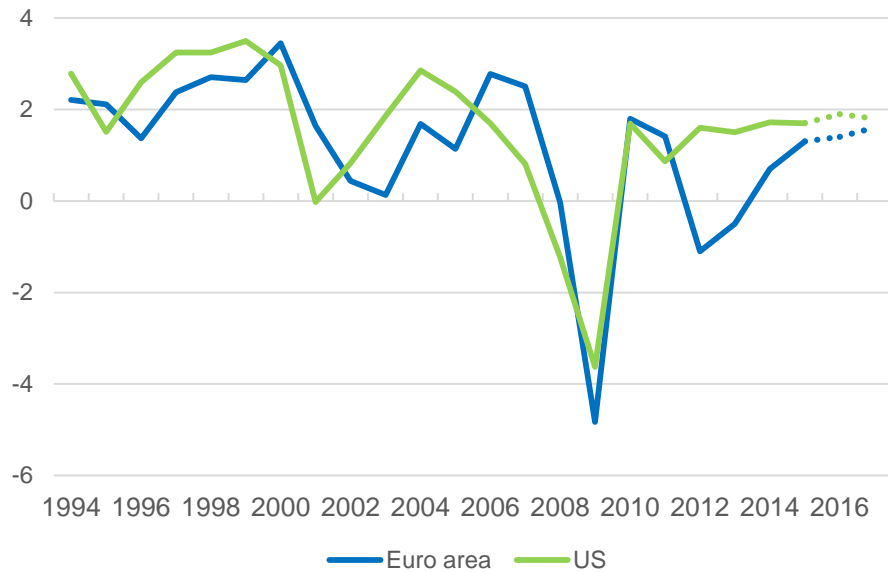
Calculated using the average sovereign market spread of each country matching the EFSF/ESM maturity profile. This is compared with the equivalent EFSF/ESM funding cost.

3. What remains to be done?

- Boost productivity and potential growth
- Manage immigration successfully
- Further integration steps to make EMU more robust

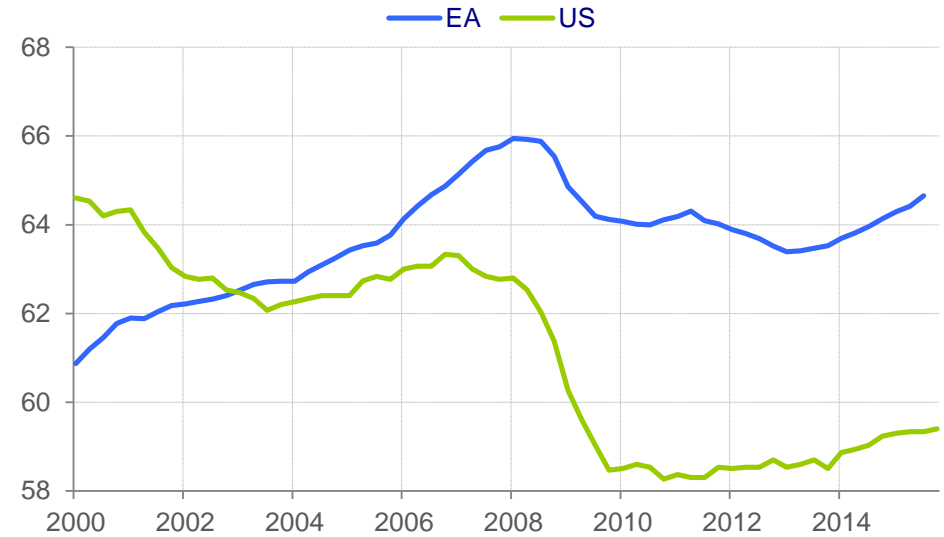
Europe's employment rate has increased significantly

Per capita growth in US and EU is similar



Source: EC European Economic Forecast - Winter 2016

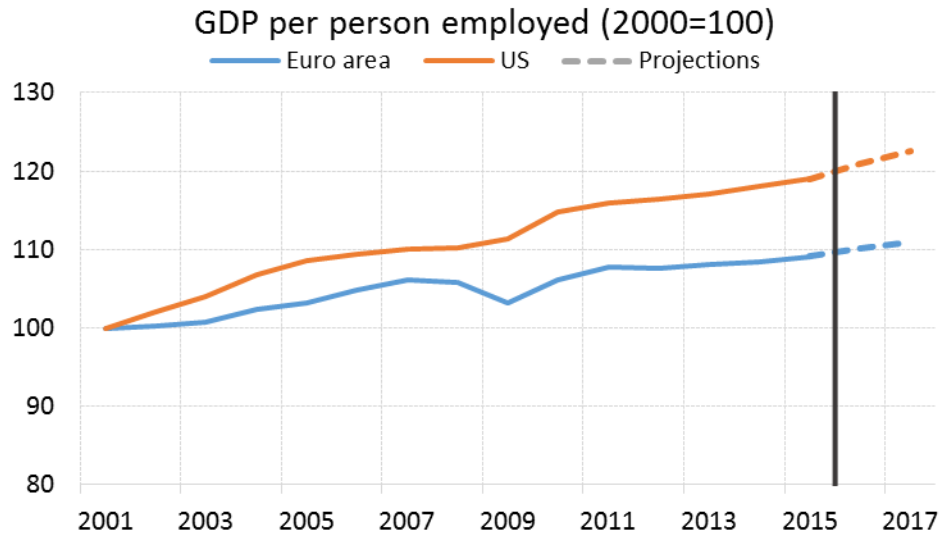
Europe has a higher employment rate



Age group: 15+ for euro area, 16+ for US
 Latest observations: Q3 2015 for euro area, Q4 2015 for US
 Source: Eurostat and BLS

...but Europe needs to strengthen productivity

- Europe is lagging behind the US in productivity



Steps that need to be taken:

- Structural reforms
- More investment: Juncker plan
- Promote research and education
- Clean up banks' balance sheets so they will start lending again

Immigration: short-term burden, long-term blessing?

- Short term: immigration stimulates growth
 - Small but positive impact on EU GDP
 - Estimated spending for Germany alone: €20 to €25 bn in 2016
- Medium to long-term: new labour supply can compensate for poor demographics
- But: possible negative impact on investor and consumer sentiment
 - Rising populism: not just a European problem (U.S., Switzerland)
- Crises tend to strengthen Europe
- Key: successful policies for integration, protection of outside borders

Further integration: towards a more robust EMU

- Five Presidents proposals (Juncker, Tusk, Dijsselbloem, Draghi, Schulz)
- Banking and Capital Markets Union
 - European Deposit Insurance Scheme (EDIS)
 - Address taxation, insolvency and company law issues
 - Financial market integration
 - More capital flows
 - Risk sharing
- Fiscal Union
 - Limited fiscal capacity for the euro area
 - A euro area Finance Minister
- Political Union

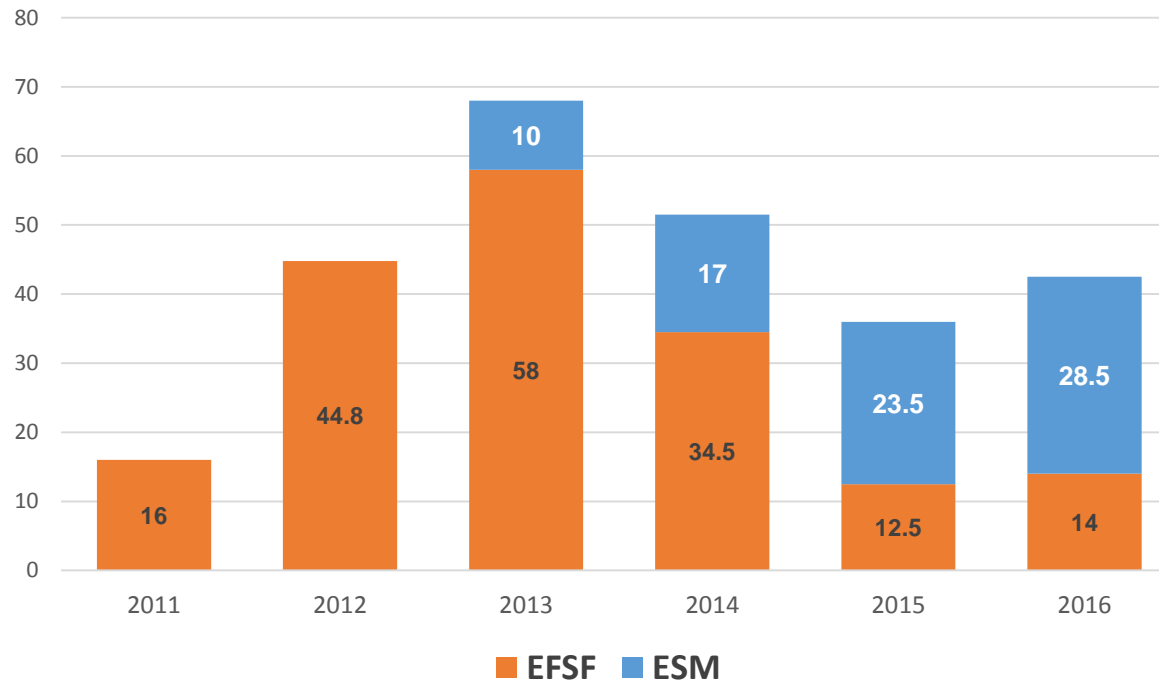
The European economy after the crisis

- A steady recovery
- Economic developments compare well with the United States
- We saved the euro
- The crisis has brought Europe closer together
- The EU provides solidarity to weaker countries
- ‘Cash for reform’ is a success formula
- More homework; reforms need to continue
- Productivity and potential growth need to be pushed up
- Integrating migrants: new challenge and opportunity
- Further integration to make EMU more robust

The issuance programmes of the EFSF and the ESM

EFSF and ESM bond issuance

Annual volume of bonds issued (€ bn)



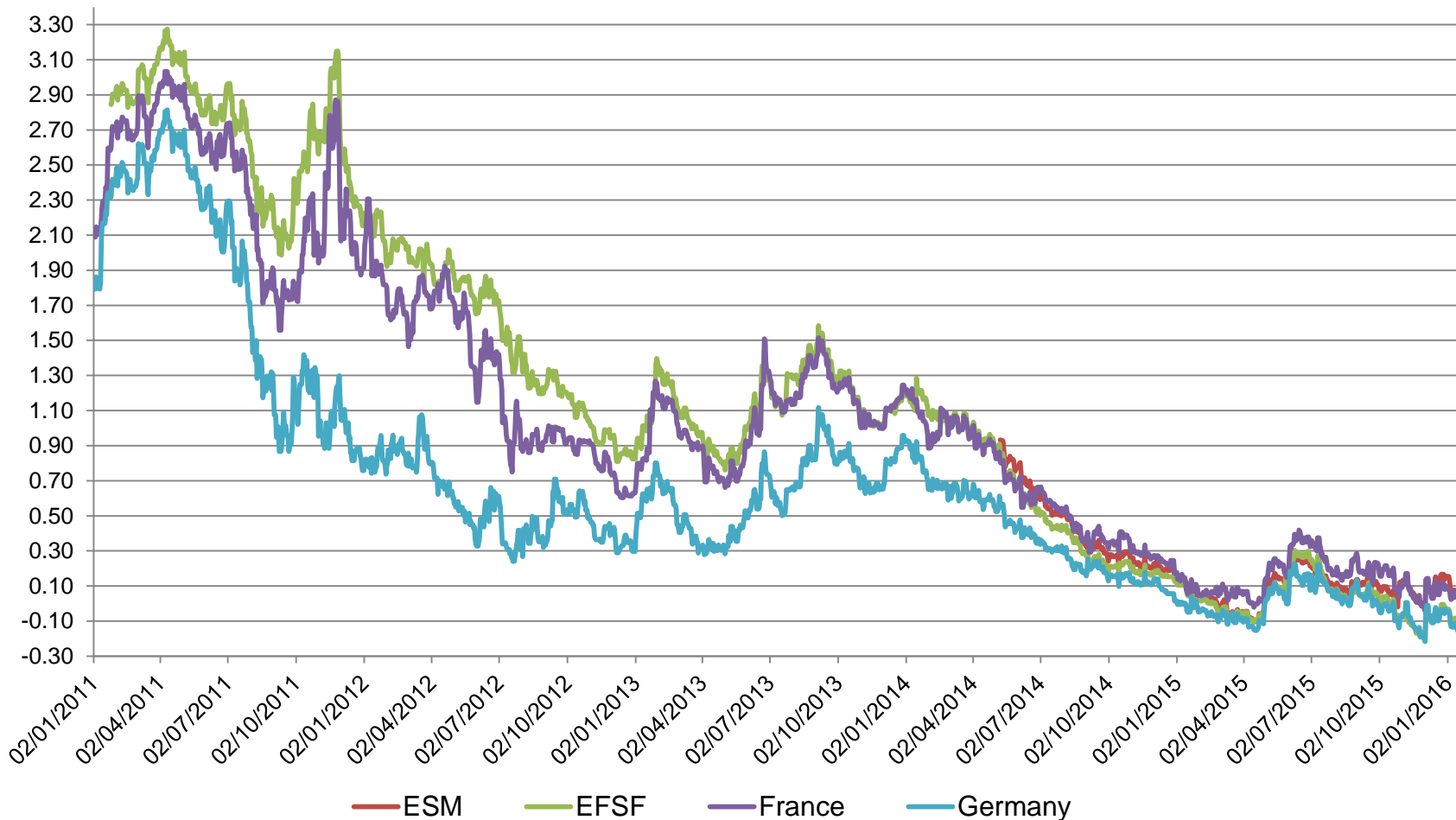
- ESM/EFSF was the 6th biggest SSA issuer in euros in 2015
- Sizeable issuer for years to come – around €40 bn after 2017

Amounts for 2016 are current targets and may change

EFSF & ESM vs Peers Bond Curves

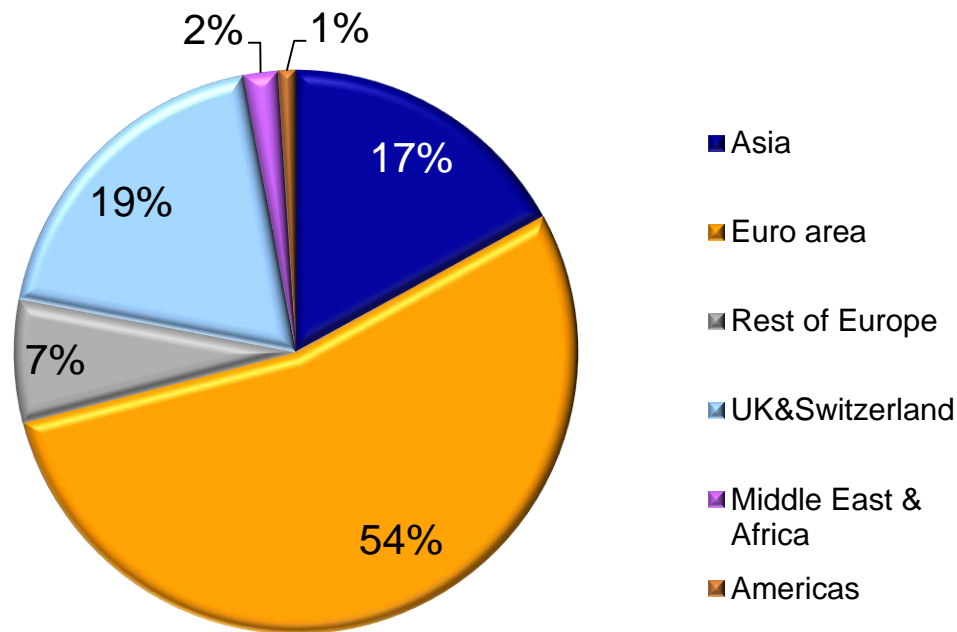
EFSF and ESM bonds are **well-established in the market** and trading **close to other highly-rated issuers**.

ESM, EFSF, France and Germany 5-year yields

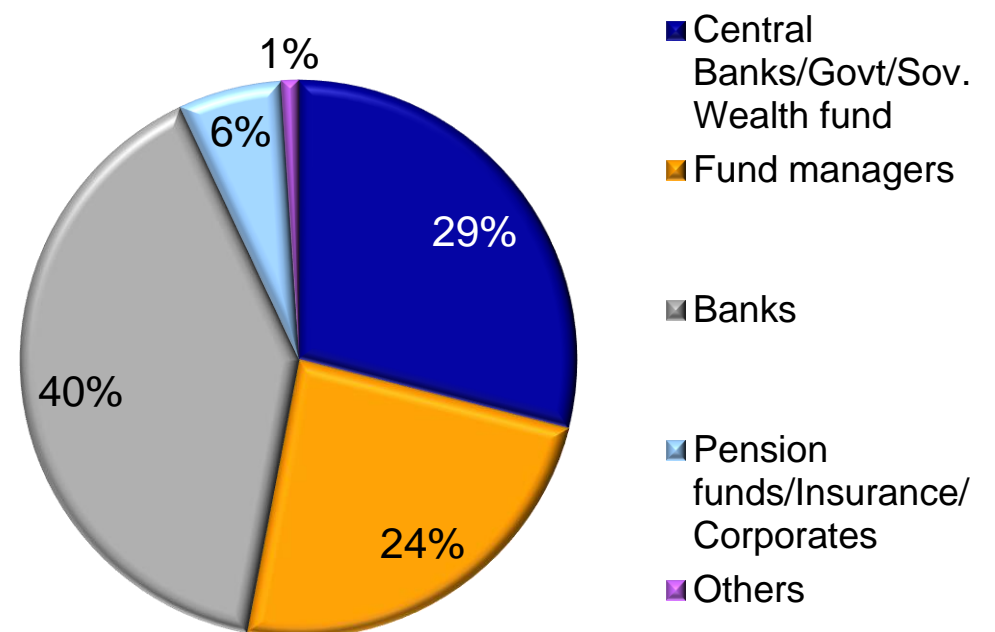


ESM: already a mature investor base

Geographical breakdown



Breakdown by investor type



*Total breakdown includes all ESM syndicated bond issues at time of issue. Placements by auction are not included. As at 13/01/2016

Contacts


Klaus Regling
ESM Managing Director

Investor.relations@esm.europa.eu

www.esm.europa.eu

www.efsf.europa.eu

Bloomberg: ESM <GO> ; EFST<GO>

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