

CRISIS MANAGEMENT IN EUROPE: ACHIEVEMENTS AND NEW CHALLENGES

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Bank of Greece, 14 November 2022



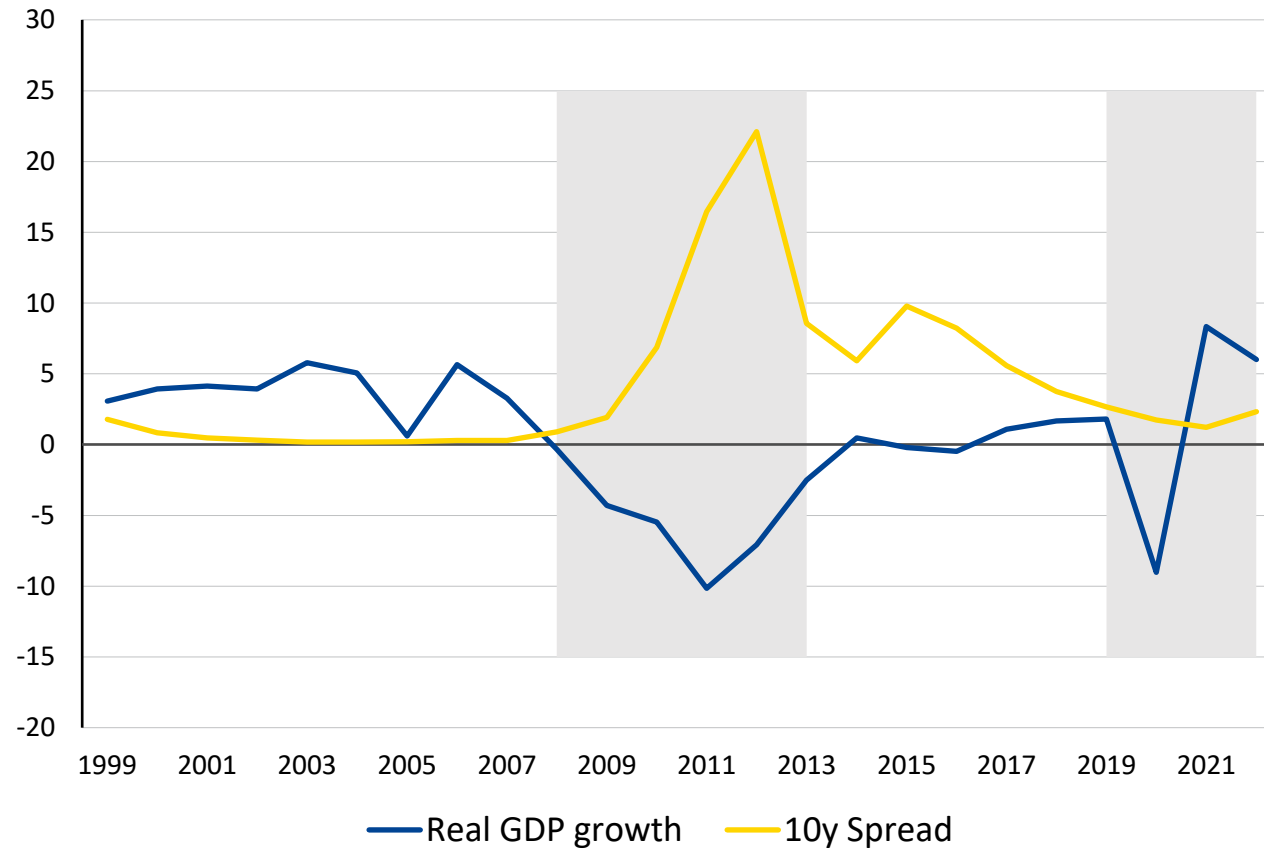
INTRODUCTION: FOUR CRISES

Since the introduction of the euro in 1999, Economic and Monetary Union has experienced four major crises:

- Global financial crisis, 2008-2009
- Euro crisis, 2009-2012
- Covid-19 pandemic crisis, 2020-2021
- Energy crisis (triggered by Russian invasion of Ukraine), 2022

THE GREEK EXPERIENCE

Greece: Real GDP growth and spreads to Bund



Note: Left hand scale (%) applies to both annual real GDP growth and spreads of 10-year Greek bonds vs Bund.
Source: World Bank (for GDP growth until 2021; ESM internal estimates (Greek GDP growth in 2022); Xetra and Athens Stock Exchange (spreads).

LESSONS FROM CRISIS EXPERIENCES AND FUTURE CHALLENGES

The tale of four crises: Global Financial Crisis, Euro Crisis, Pandemic Crisis, Energy Crisis

What was the origin of the crisis?

Did monetary-fiscal interaction work?

Why was European support provided? How did it help?

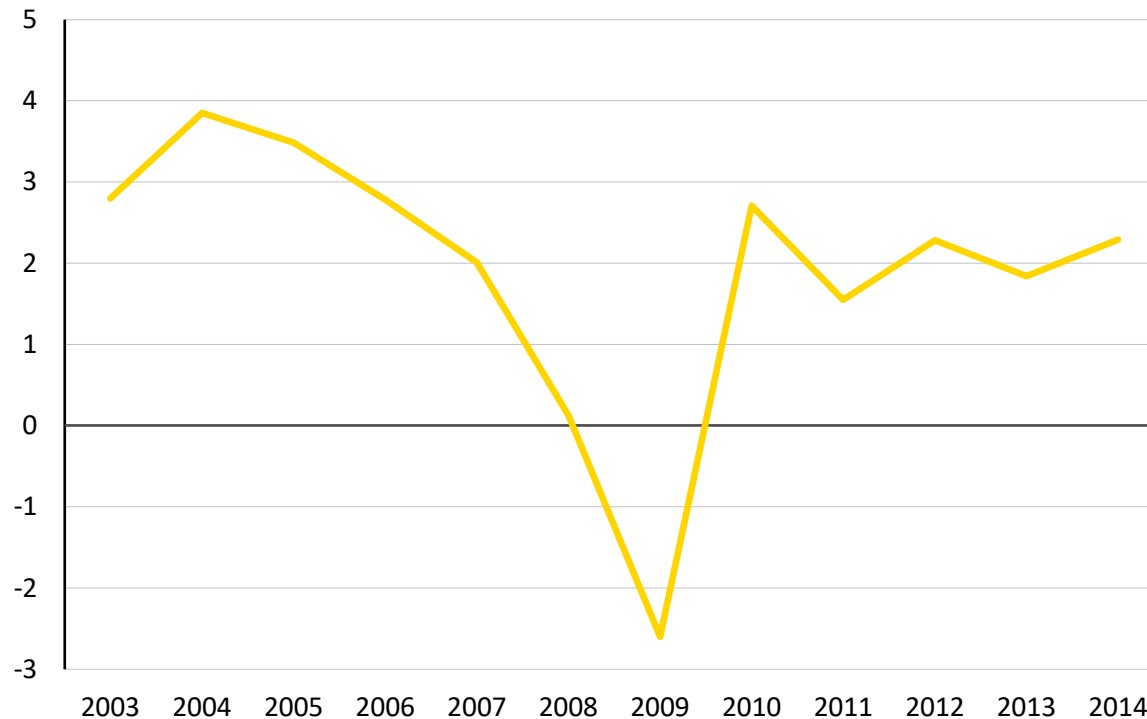
CONCLUSION: Achievements and lessons to address future challenges

II. THE 2008-2012 CRISES – COMMON SHOCK AND HOME-GROWN PROBLEMS



GLOBAL FINANCIAL CRISIS (2008-2009) AND THE GREAT RECESSION IN THE US

US real GDP growth, year-on-year



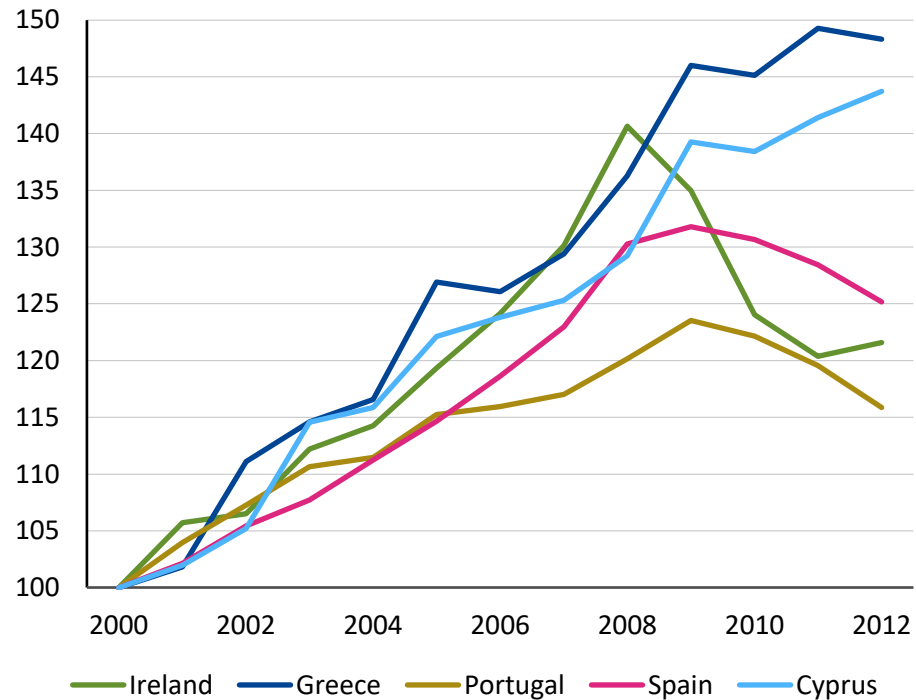
The unfolding of the crisis

- Crisis sparked by downturn in US housing market
- Trust in banking sector declined sharply, leading to 'credit crunch'
- The "Great Recession" unfolded
- Spill-over through linkages in the global financial system and economic impact

EURO CRISIS: LOSS OF COMPETITIVENESS, RISING DEBT

Nominal Unit Labour Costs

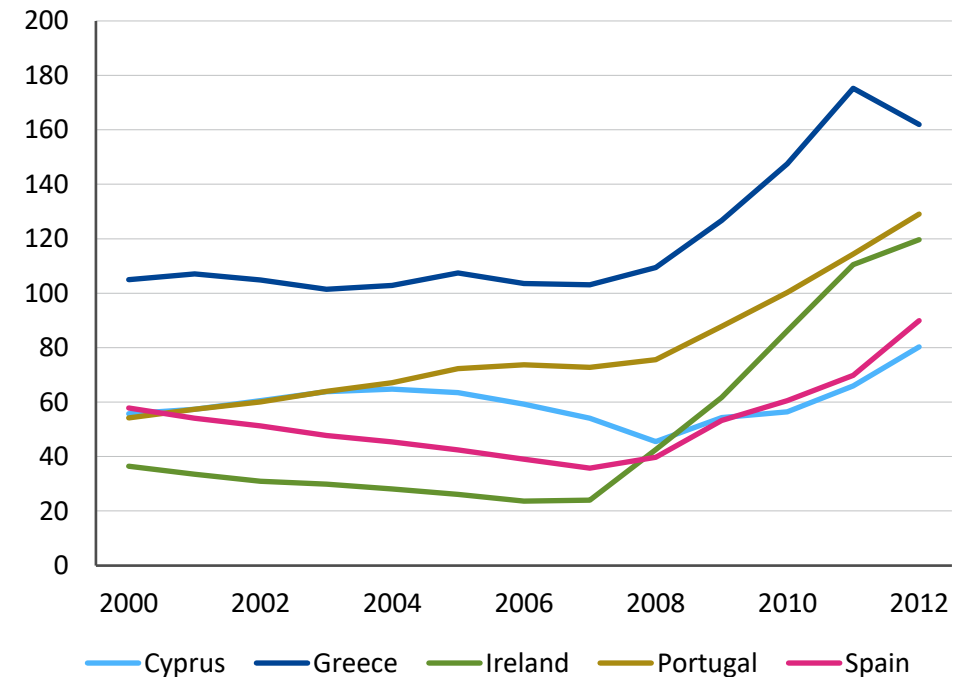
(2000=100)



Source: AMECO

Public sector gross debt

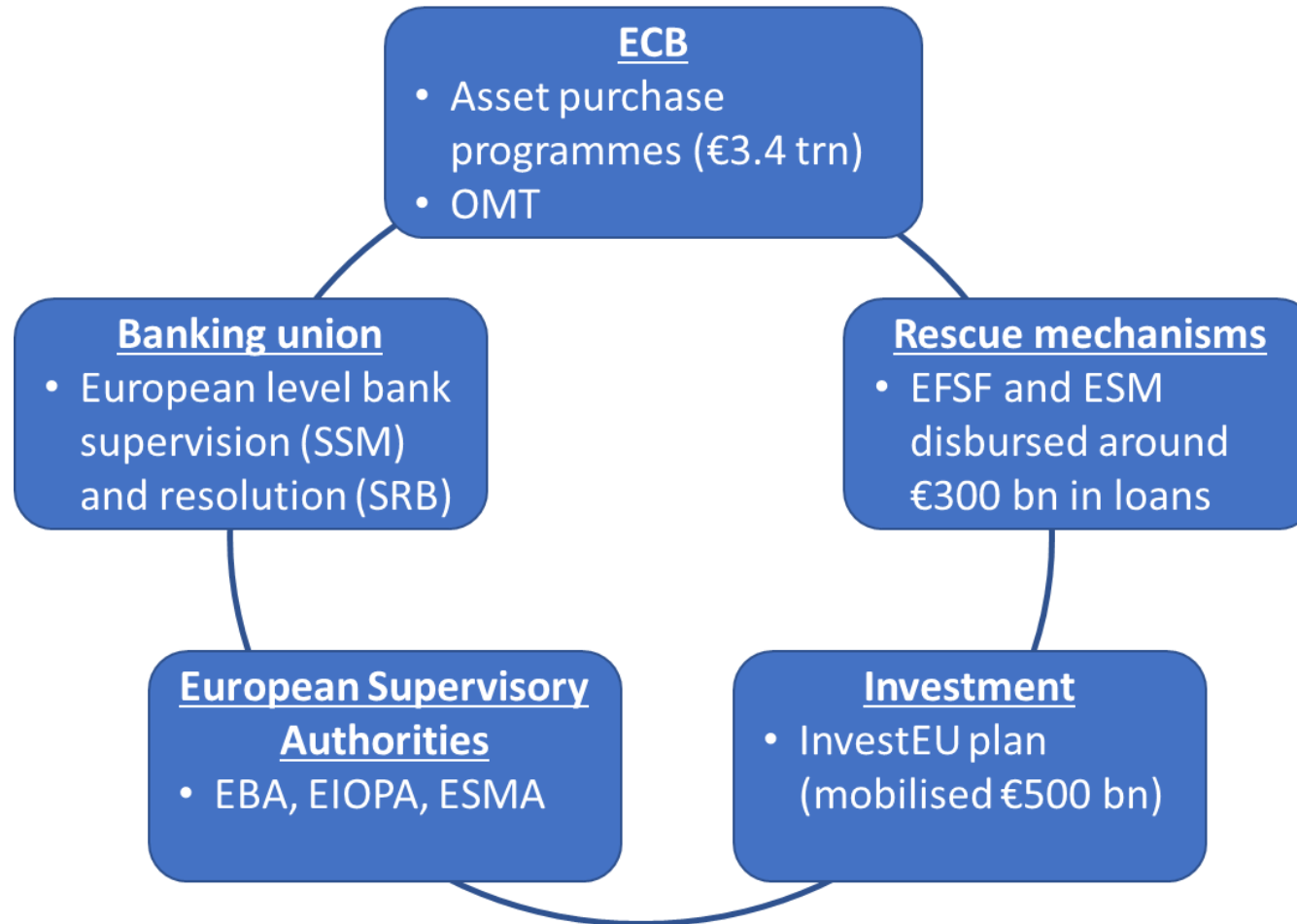
(% GDP)



Source: AMECO

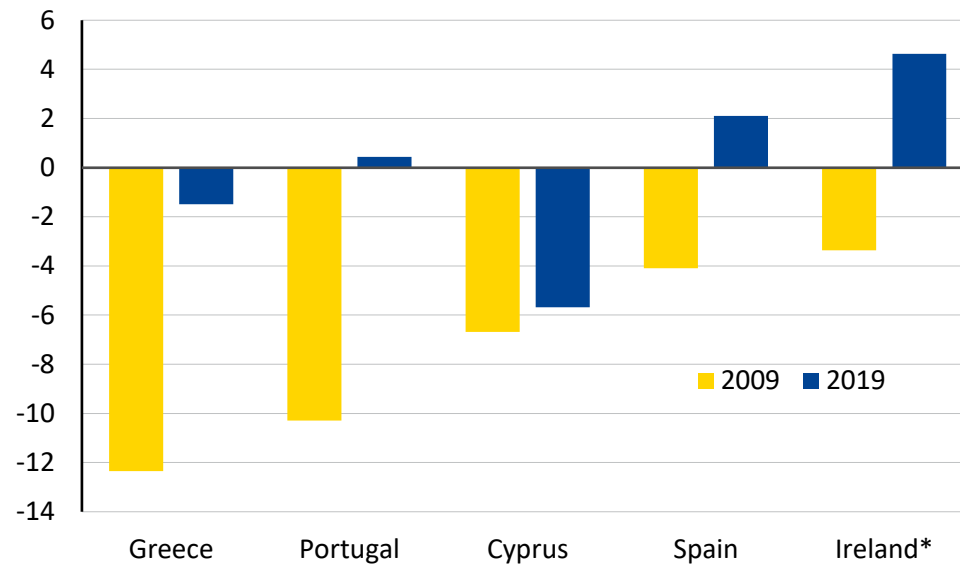
EUROPEAN POLICY MEASURES DURING THE EURO CRISIS – FILLING THE GAPS

Policy response to global financial crisis and euro crisis:



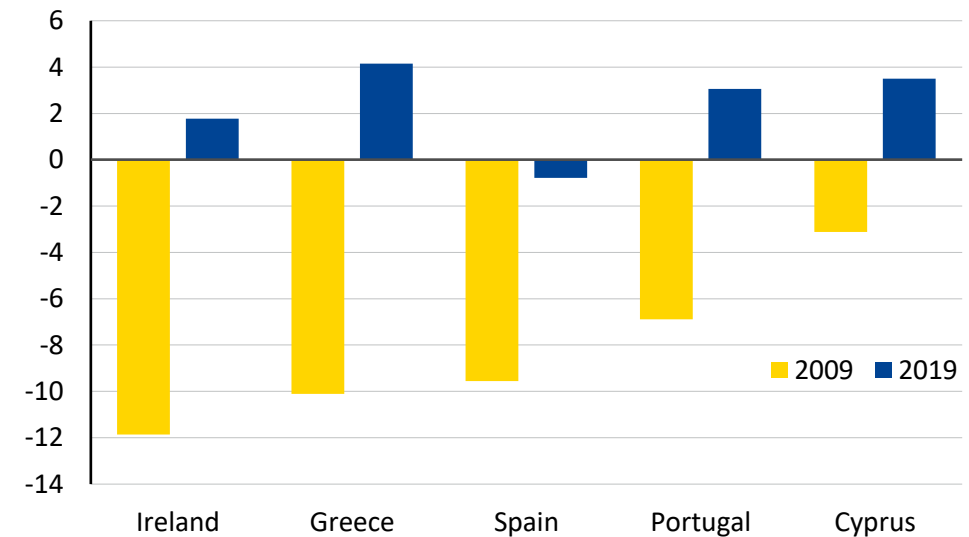
ADJUSTMENT IN EFSF/ESM PROGRAMME COUNTRIES

Current account
(% GDP)



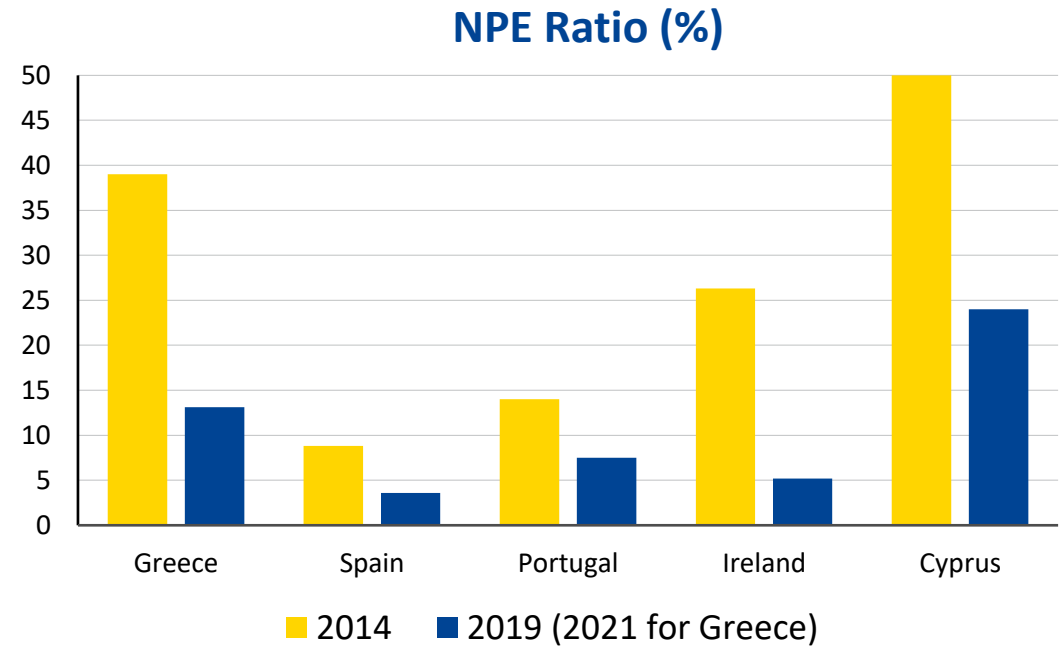
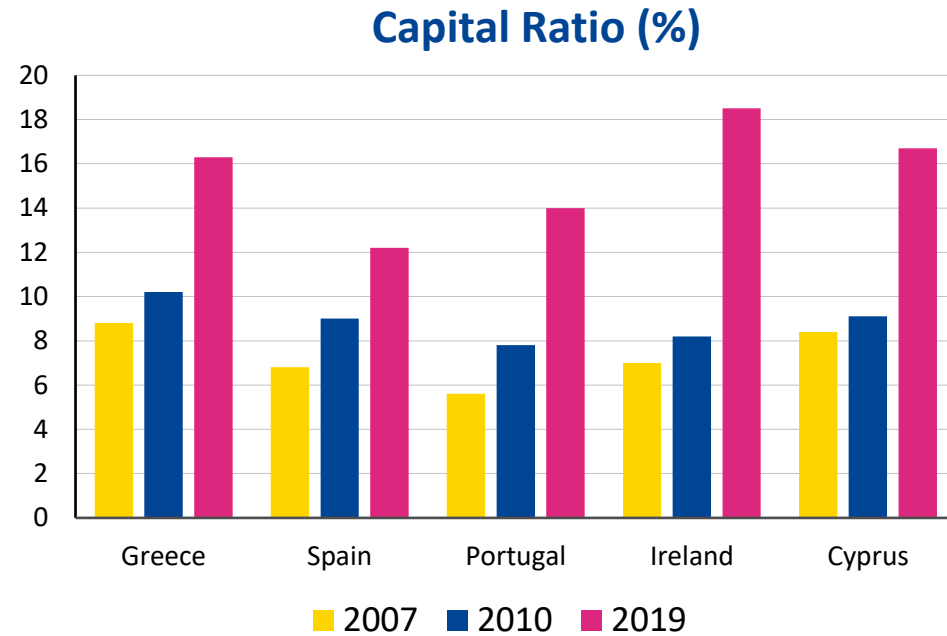
Source: AMECO and Irish Central Statistics Office. Note(*). Data for Ireland represent the “adjusted current account balance” and excludes the depreciation of foreign-owned domestic capital (such as net imports of IP and imports of research and development (R&D) services).

**General Government
Primary Balance**
(% GDP)



Source: AMECO

BANKS ENTERED THE PANDEMIC WITH STRONGER METRICS COMPARED TO PREVIOUS CRISES



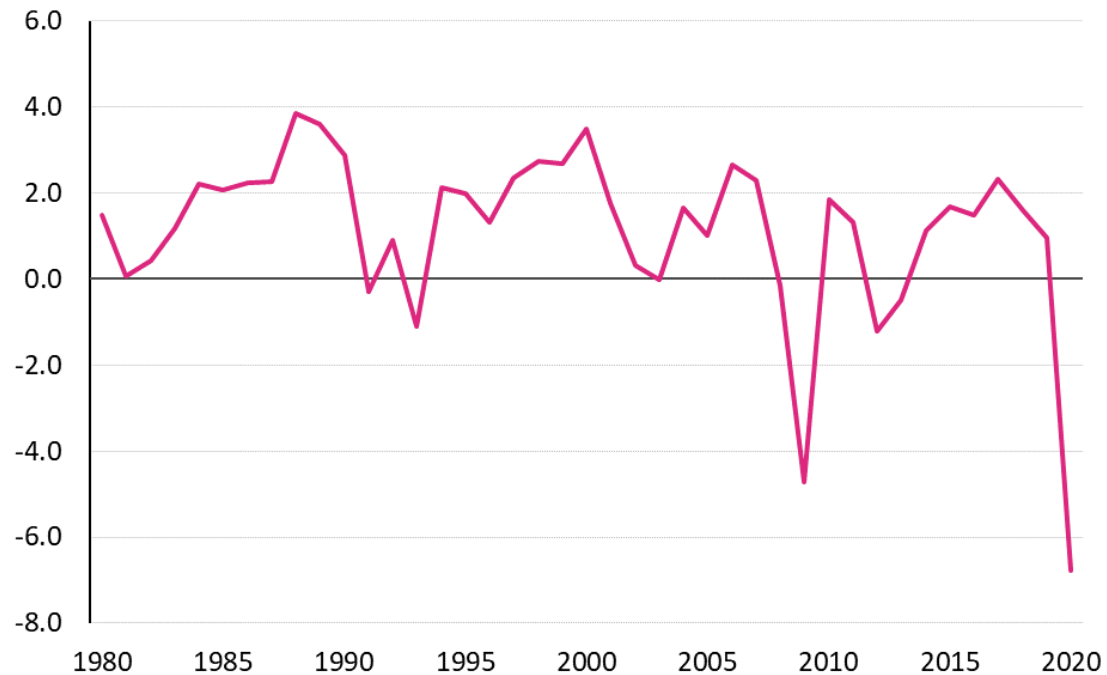
Note: Capital Ratio refers to Common Equity Tier 1

III. THE RECENT CRISES: COMMON SHOCKS, FRAGMENTATION AND POLICY COORDINATION



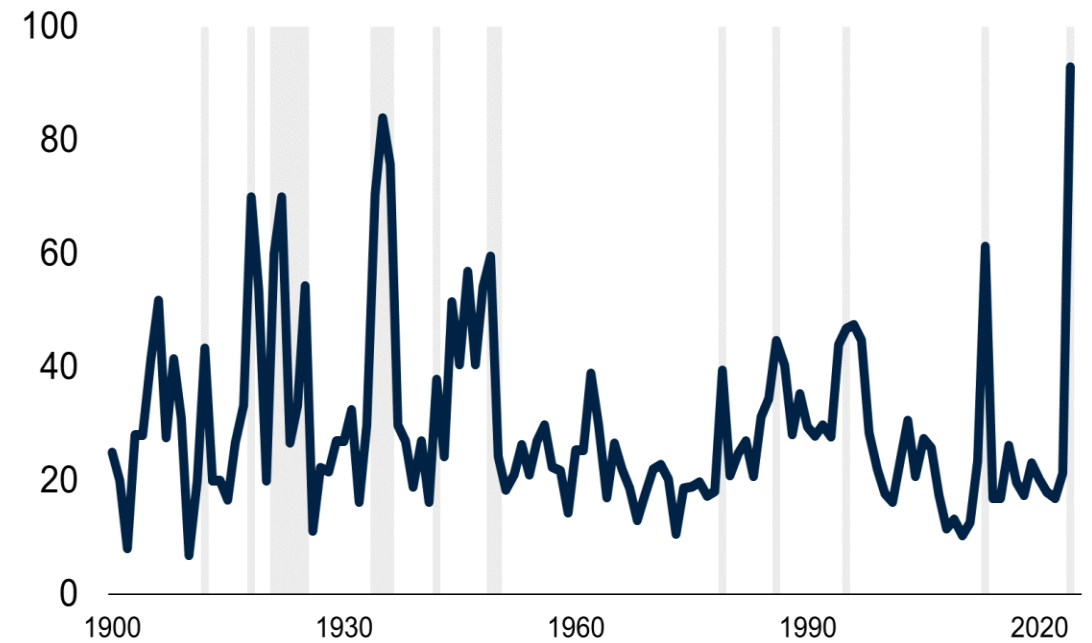
COVID CRISIS: AN UNPRECEDENTED GLOBAL SHOCK

EA-12 real GDP per capita growth
(% annual growth rate)



Source: AMECO. Note: EA12 assumes West Germany before 1991

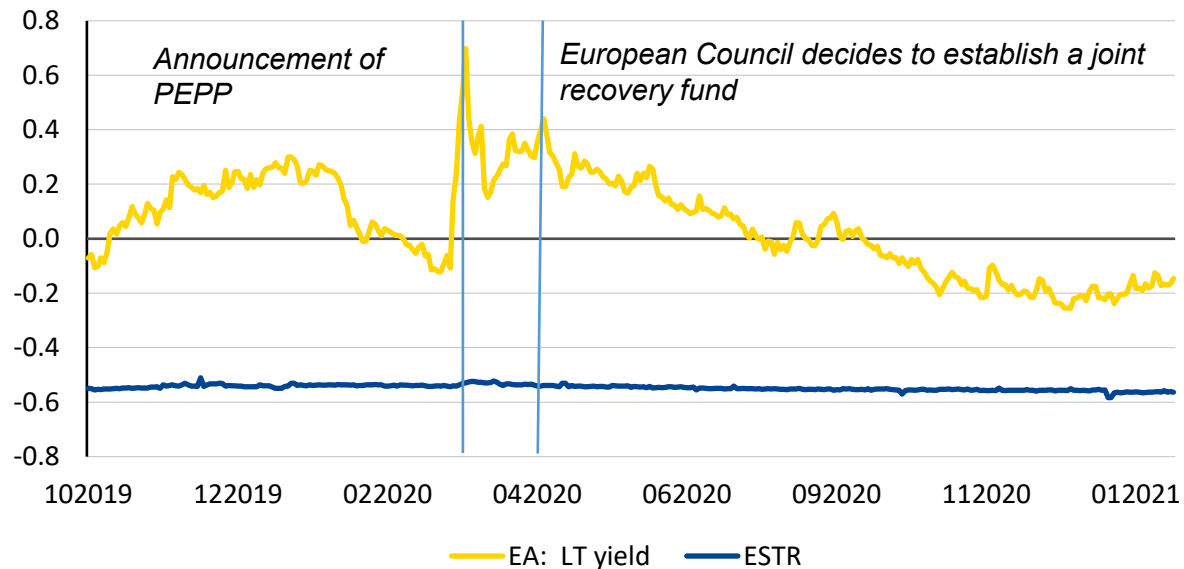
Share of world economies in recession
(%)



Source: World Bank. Note: share of economies in recession defined as an annual contraction in per capita GDP

Euro area GDP-weighted sovereign bond yields and ESTR rates

(in %)



Source: Haver and ECB, chart based on the ECB

Note: ESTR refers to Euro Short Term Rate (ESTR, % p.a.) and EA: LT yield refers to the EA GDP weighted sovereign bond yields on 10-year government bonds of selected euro area countries (AT, BE, FI, FR, DE, EL, IE, IT, PT, SI, ES).

ECB took swift policy action

March 2020:

- Existing TLTRO: lowered interest rates
- Additional longer-term refinancing operations
- Additional asset purchases of €120 billion combined with the existing asset purchase
- PEPP programme of €750 billion: private and government sector securities
- Relaxed collateral standards to provide easier access to liquidity

April + June 2020:

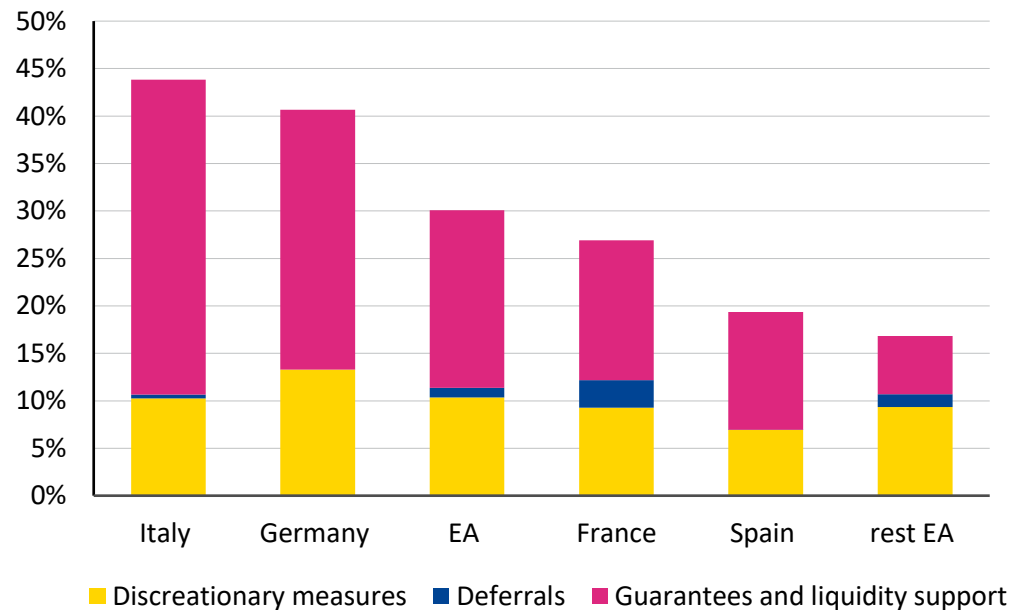
- Further collateral easing
- More flexible and extended PEPP
- Creation of a series of non-targeted pandemic emergency longer-term operations (PELTROs)

Source: EFB, 2020.

STRONG NATIONAL POLICY RESPONSE TO THE PANDEMIC

National fiscal response to Covid-19

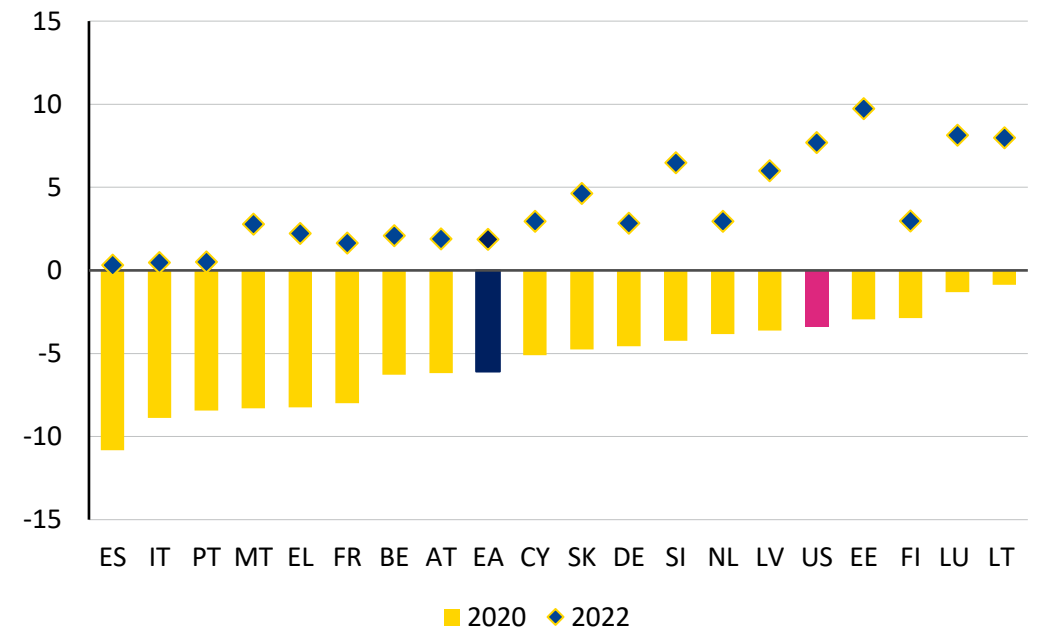
(% of 2019 GDP, measures announced since March 2020)



Note: ESM calculations based on the IMF, July 2021 WEO. The chart summarises key fiscal measures governments have announced or taken in selected economies in response to the COVID-19 pandemic as of 5 June, 2021 for selected economies. It includes COVID-19 related measures since January 2020 and covers measures for implementation in 2020, 2021, and beyond. The actual take-up rate of guarantees varies across the member states.

EA countries and the US: Real GDP compared with pre-crisis level

(% of 2019 GDP)



Source: IMF October 2022 WEO.
Note: Ireland was omitted as an outlier.

IMMEDIATE EU RESPONSE TO THE CORONAVIRUS PANDEMIC (2020)

In May 2020, the EU Heads of State committed € 540 billion to fight the Covid-19 crisis



Support for workers

Up to €100bn in loans to EU member states under the **European Commission's SURE** programme in support of national unemployment schemes.



Support for companies

A pan-European **guarantee fund** by the European Investment Bank (EIB) of €25bn, which could provide around €200bn of financing for companies, especially SMEs.



Support for countries

The **ESM's Pandemic Crisis Support**, a precautionary credit line with a total volume of up to €240bn, is available to all euro area countries until the end of 2022 to support healthcare-related costs of up to 2% of GDP.

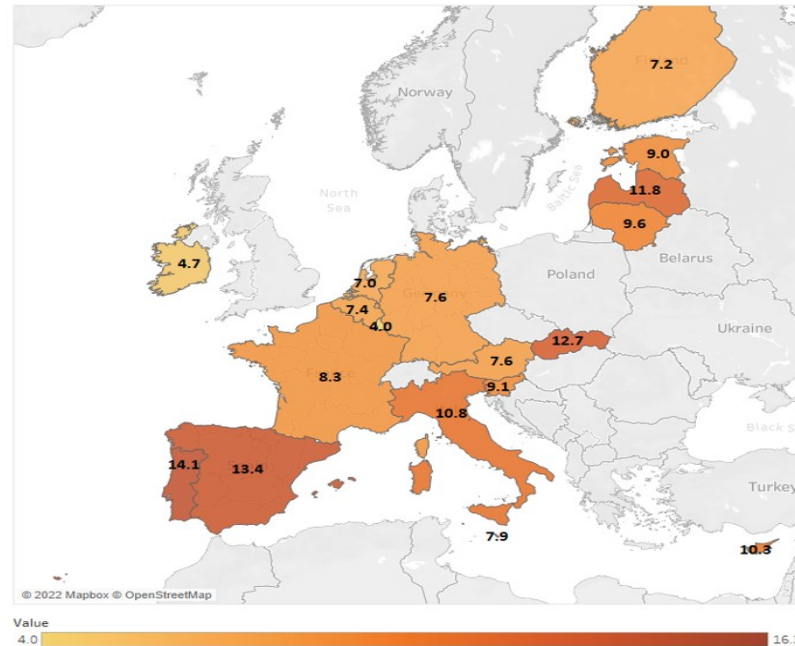
CORE EU ACTION: TARGETED THE MOST VULNERABLE MEMBERS AND STRUCTURAL CHALLENGES

Next Generation EU package, total amount: €750 billion

Recovery and Resilience Facility: grants and loans: maximum allocations
(In % of 2021 GDP)

Contribution key:

- Skewed towards countries most hit by the pandemic
- Redistribution towards **most vulnerable members**



Recovery and Resilience Facility

- 37% green, 20% digital transitions
- Grants (€312.5 bn) and loans (€360 bn)
- High degree of solidarity
- National Resilience and Recovery Plans

Contribution to other EU programs

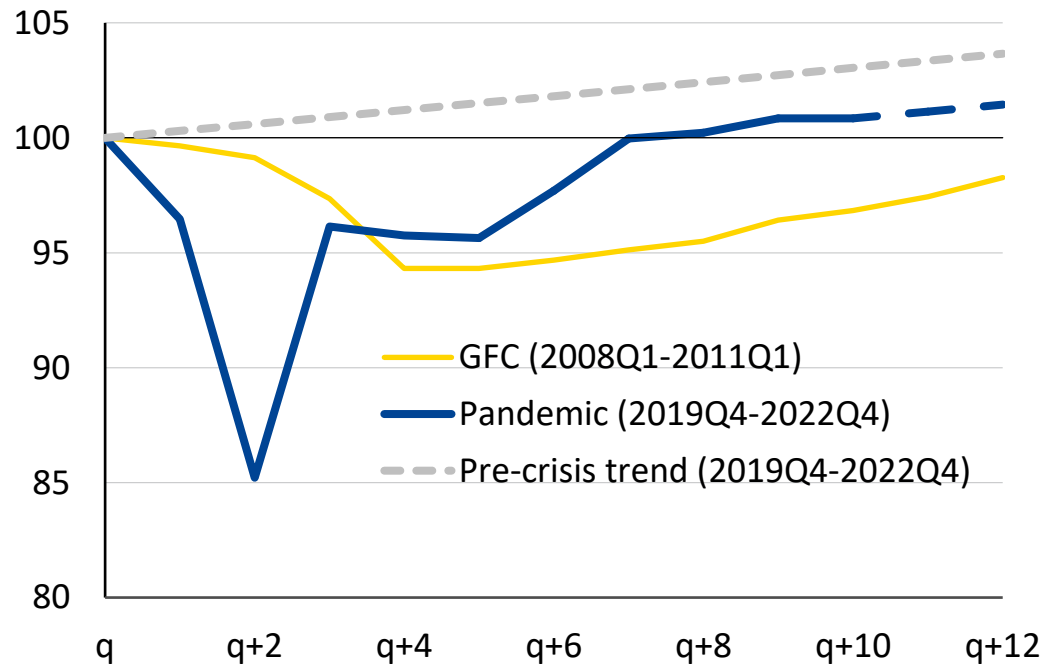
- Regional and rural development;
- climate neutrality;
- research and innovation

Source: European Commission, European Parliament

Note: Grants distribution as computed based on European Commission June 2022 updates. The maximum volume of the loan support for each Member State corresponds to 6.8 % of its 2019 gross national income (article 14 (5) of the RRF Regulation).

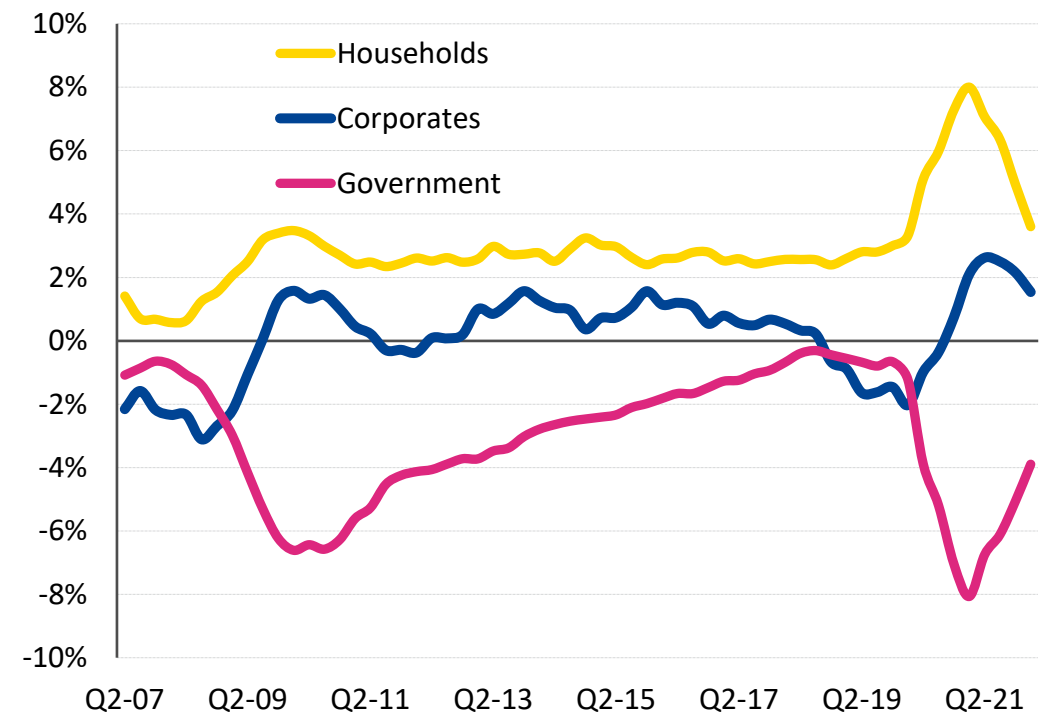
THE ECONOMY RECOVERED FAST, FISCAL VULNERABILITIES INCREASED

**EA real GDP level since the pandemic:
comparison with global financial crisis**
(Index pre-crisis quarter = 100)



Sources: ESM calculations based on EC 2022 Summer forecast and Eurostat. Note: 2022Q2 data point is based on latest Eurostat flash estimates.

Non-financial sector: net lending/borrowing
(% GDP, cum 4Q)

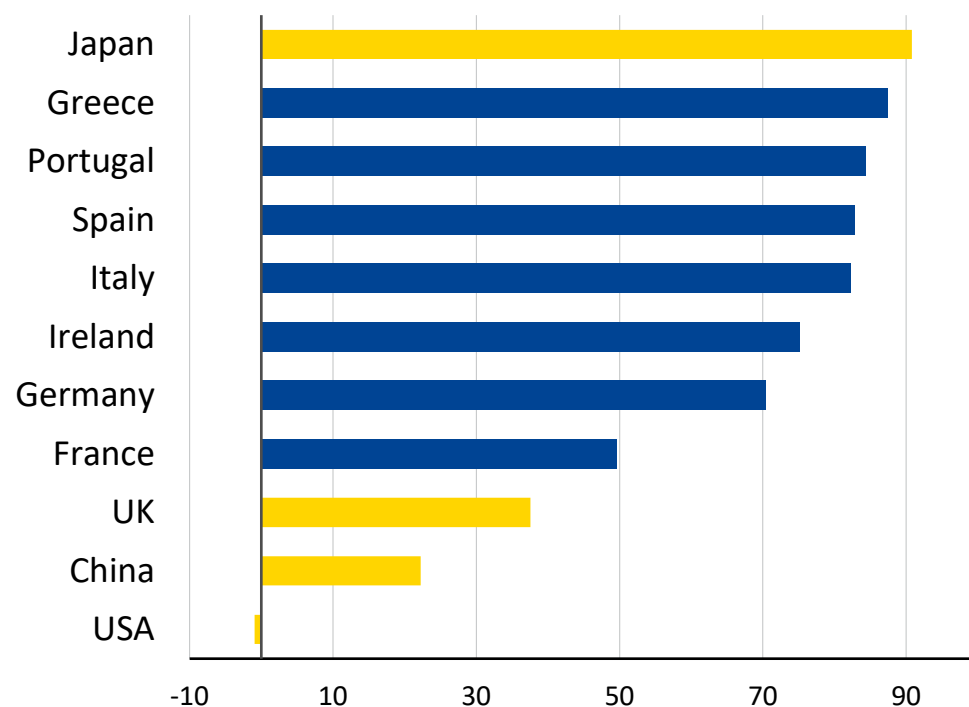


Source: Eurostat.

ENERGY CRISIS AND WAR AGAINST UKRAINE- EUROPEAN ECONOMIES PARTICULARLY EXPOSED

Energy dependency

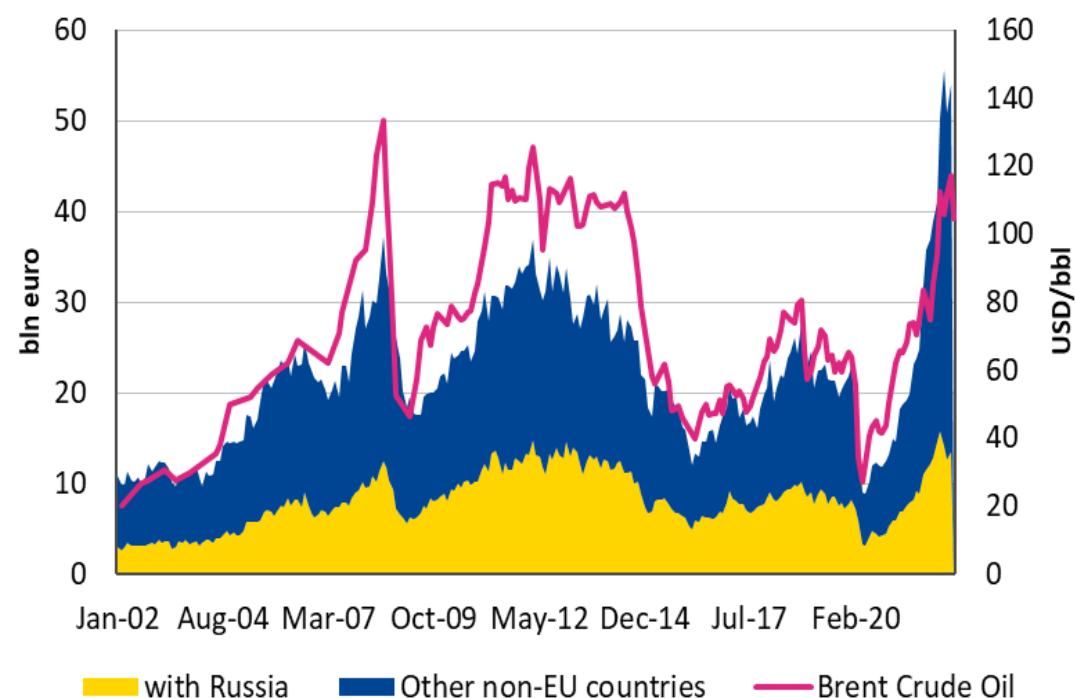
(net imports of energy goods/ total supply,%)



Source: International Energy Agency (IEA). Note: Latest available data from 2019.

Increase in energy prices results in transfers of income abroad

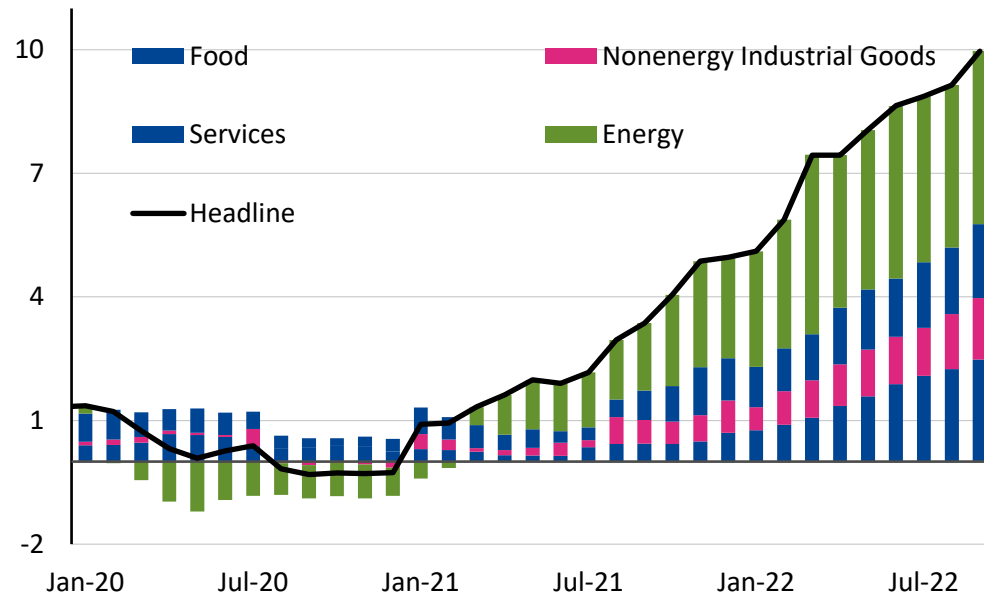
(EU energy trade deficit and oil prices on rhs)



Source: Eurostat and Haver Analytics.

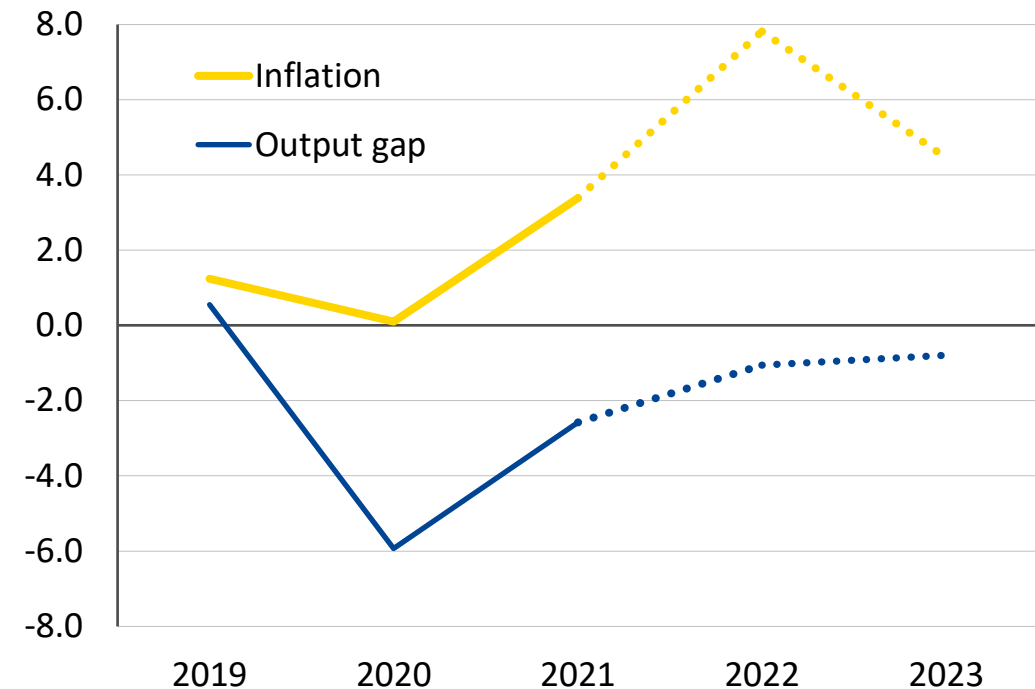
MONETARY POLICY IS FOCUSED ON PRICE STABILITY

HICP inflation and components (yoy growth rates in %)



Source: Eurostat.

EA inflation vs output gap: average estimates of EC, IMF and OECD (in % yoy and % of potential GDP)

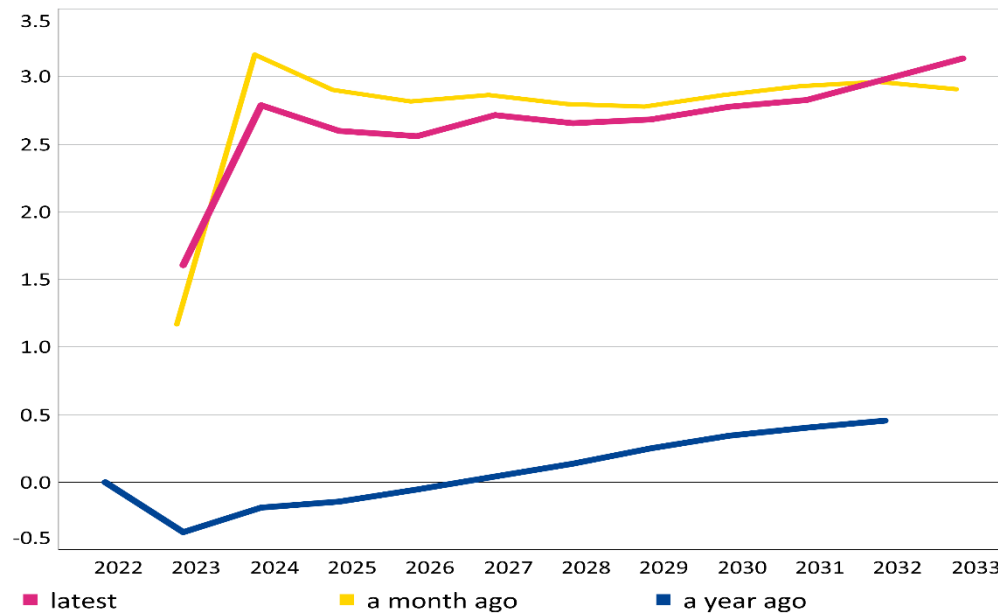


Source: ESM based on Bloomberg

Source: EC May and July 2022, OECD June 2022, IMF October 2022.

ASSET PURCHASES CONTINUE TO CONTAIN FRAGMENTATION RISKS

Market-implied path of short-term rates (ESTR 3m, %)



Source: ESM based on Bloomberg

Note: The latest refers to the latest data point available – 26 October 2022.

PEPP reinvestment flexibility:

- Reinvestments skewed towards Italy, Spain, Greece, Finland, and Portugal.

ECB's Transmission Protection Instrument:

- TPI designed to ensure smooth monetary policy transmission if spreads widen beyond fundamentals
- The purchases subject to eligibility criteria, including **fiscal sustainability**
- When assessing public debt sustainability, the ECB to take into account analyses conducted by the institutions incl. ESM

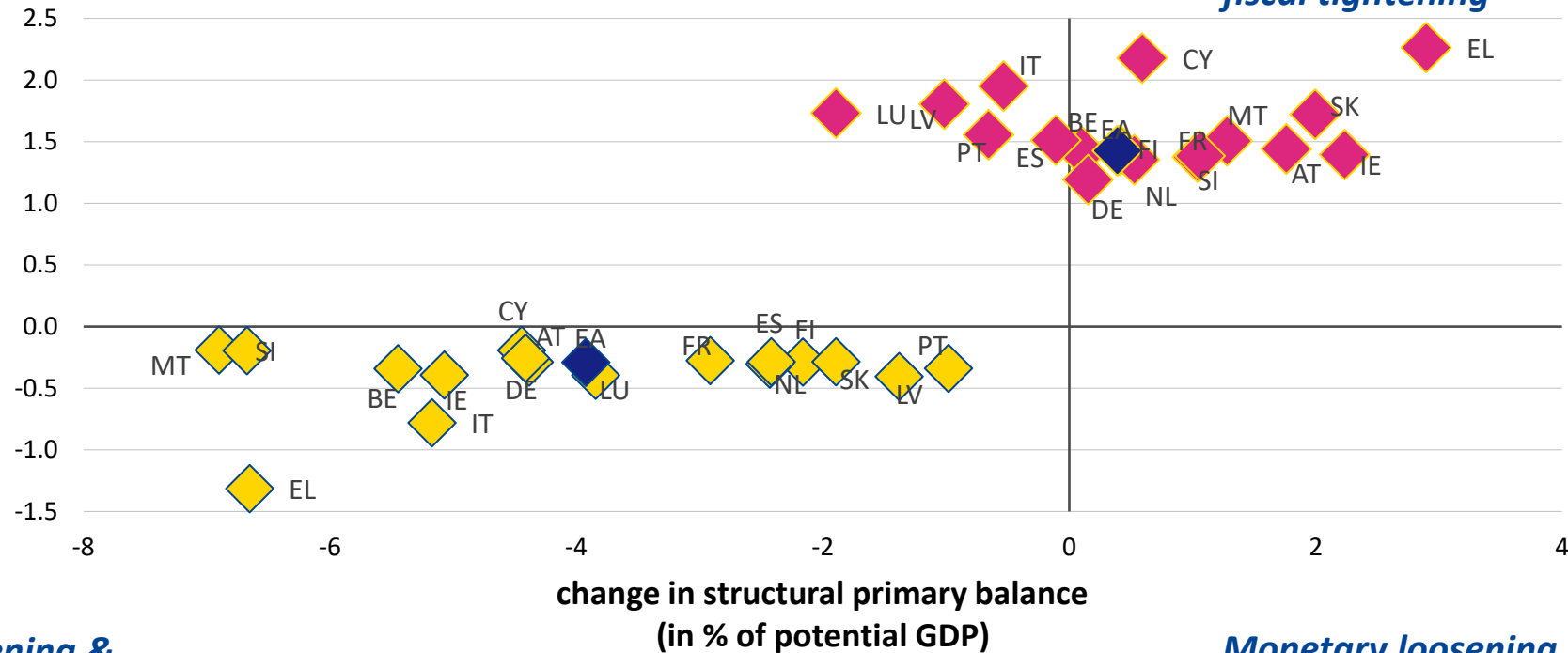
Outright Monetary Transactions:

- Contingent on “strict conditionality” attached to an ESM credit line or adjustment programme.

ASSET PURCHASES CONTINUE TO CONTAIN FRAGMENTATION RISKS

Monetary tightening & fiscal loosening

change in long-term government bond yields (in %)



Monetary tightening & fiscal tightening

Monetary loosening & fiscal loosening

◇ change 2020 vs 2019

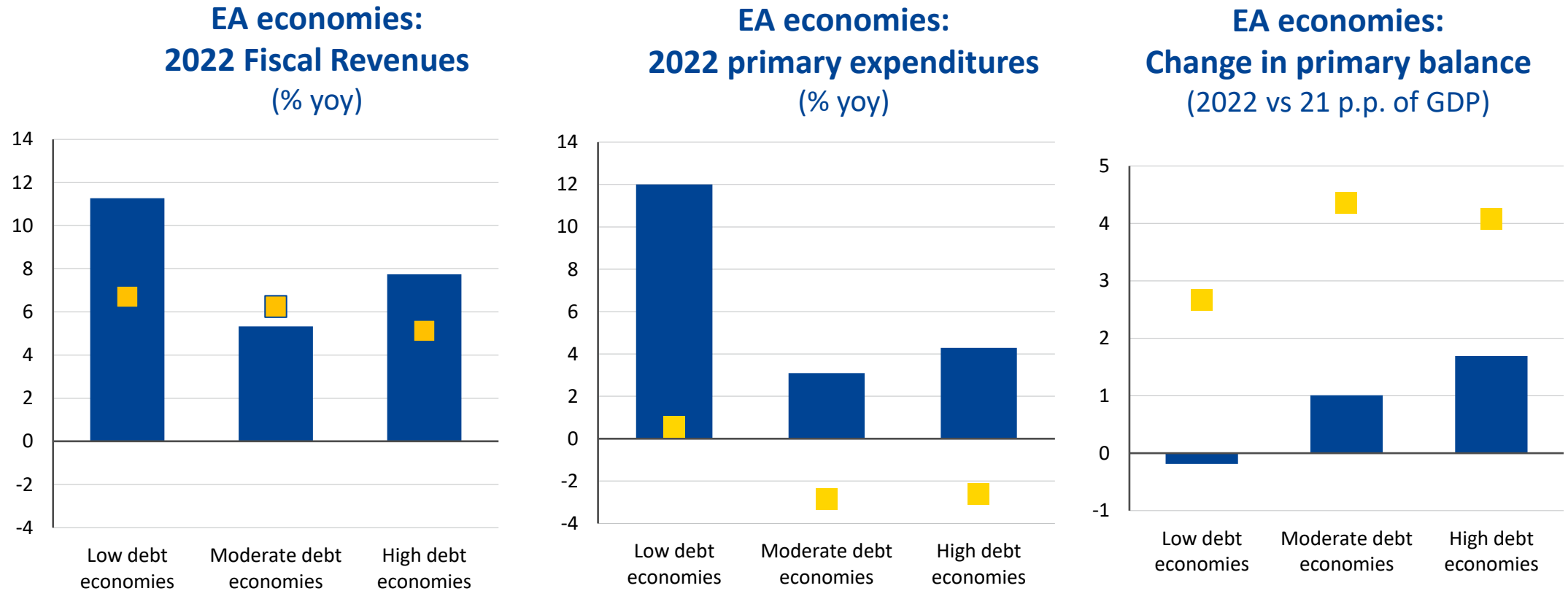
◇ change 2022 vs 2021

Monetary loosening & fiscal tightening

Source: IMF WEO and Fiscal Monitor database, ECB and Haver.

Note: The change in primary structural balance was computed by subtracting the 2019 from 2020 and similarly 2021 from 2022. Estonia and Lithuania are not depicted due to the missing data.

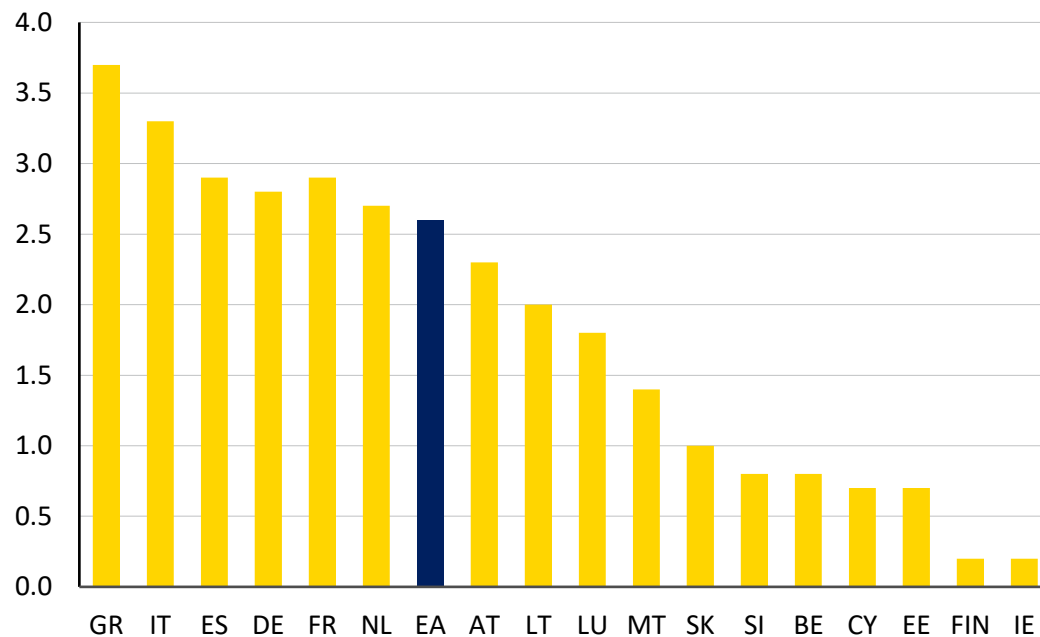
FISCAL PERFORMANCE IN 2022



Source: Own calculations based on IMF WEO database. Note: Countries grouped based on their average public debt to GDP ratio in 2012-20. Low debt countries (debt ratio below 60%) = EE, LU, LT, LV, MT, SK; Moderate debt countries (debt ratio between 60% and 90%) = NL, IE, FI, DE, SI, AT; high debt countries (debt ratio above 90%) = CY, FR, BE, ES, PT, IT, EL. Variables calculated as 2021 GDP-weighted average of each group

EMERGENCY SUPPORT AND LONG-TERM RESILIENCE

EA: National fiscal support vs energy crisis (Sep 2021-Sep 22, % GDP)



Source: Bruegel database and ESM calculations, last update: 21 September 2022. Note: The chart refers to governments allocated funding to shield households and businesses from the energy crisis. Estimated numbers also include measures that have been announced by governments but not converted into law yet. The EA weighted average is only an approximation based on the available data.

EU green transition and phasing out Russian fossil fuels: NGEU and RePowerEU

NGEU

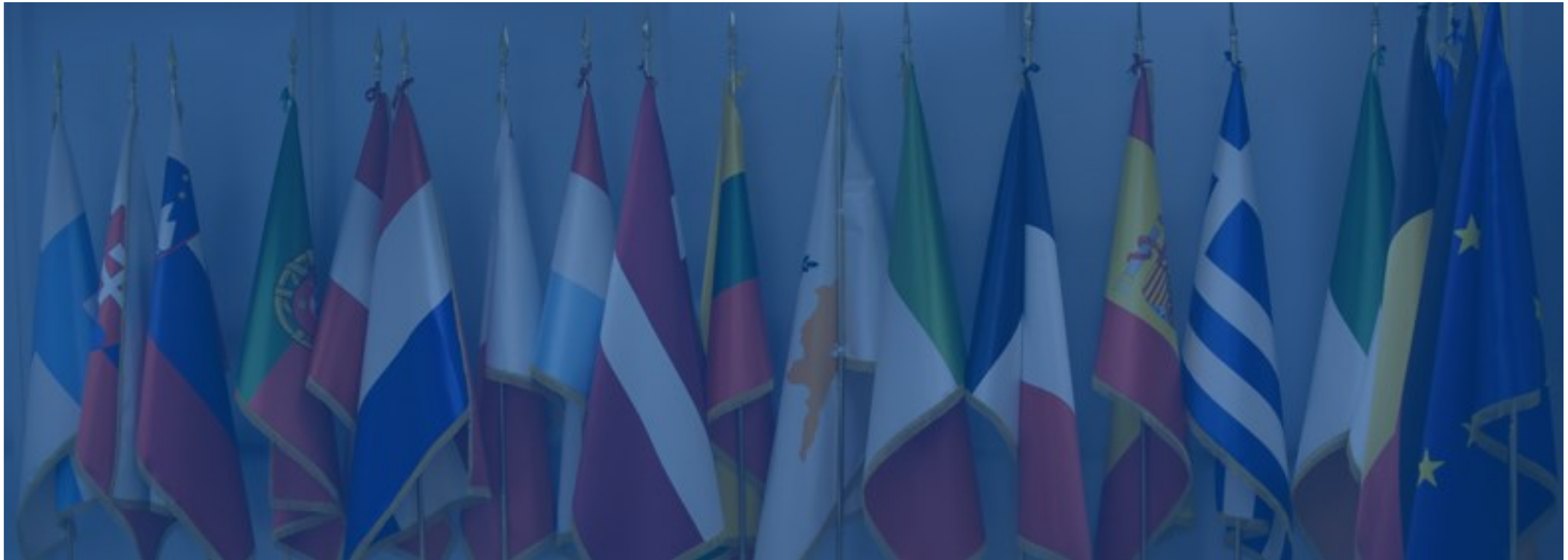
- 40% of RRP's total allocation supports climate objectives
- More than EUR 200bn of loans available to be allocated

Repower EU

- Demand: energy saving
- Supply: diversifying away from Russia
- Investment in renewables

EC toolbox to tackle rising energy prices

Source: European Commission



EU AND EURO AREA CRISIS MANAGEMENT

Purpose of common crisis management

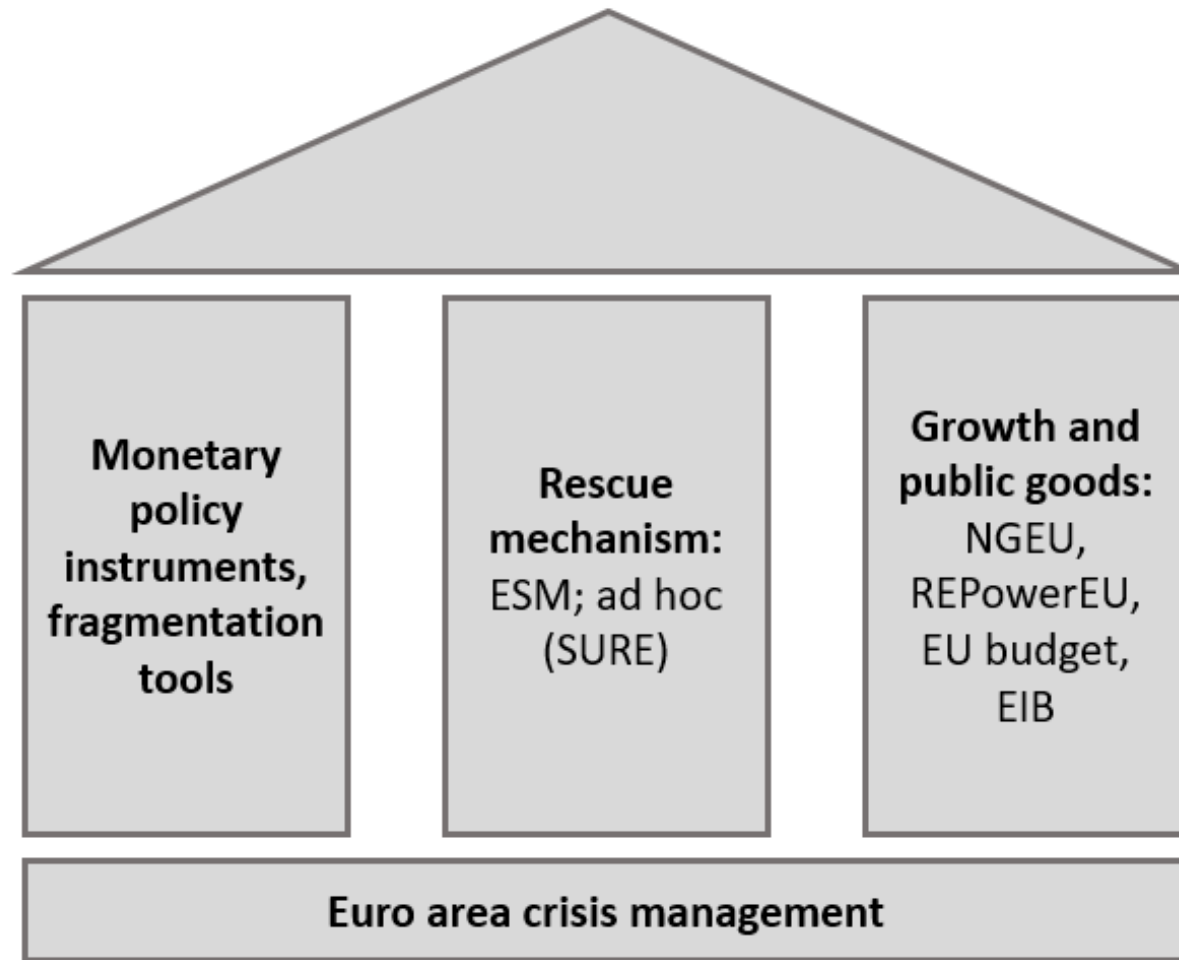
EU:

- Protect the common market
- Ensure economic convergence

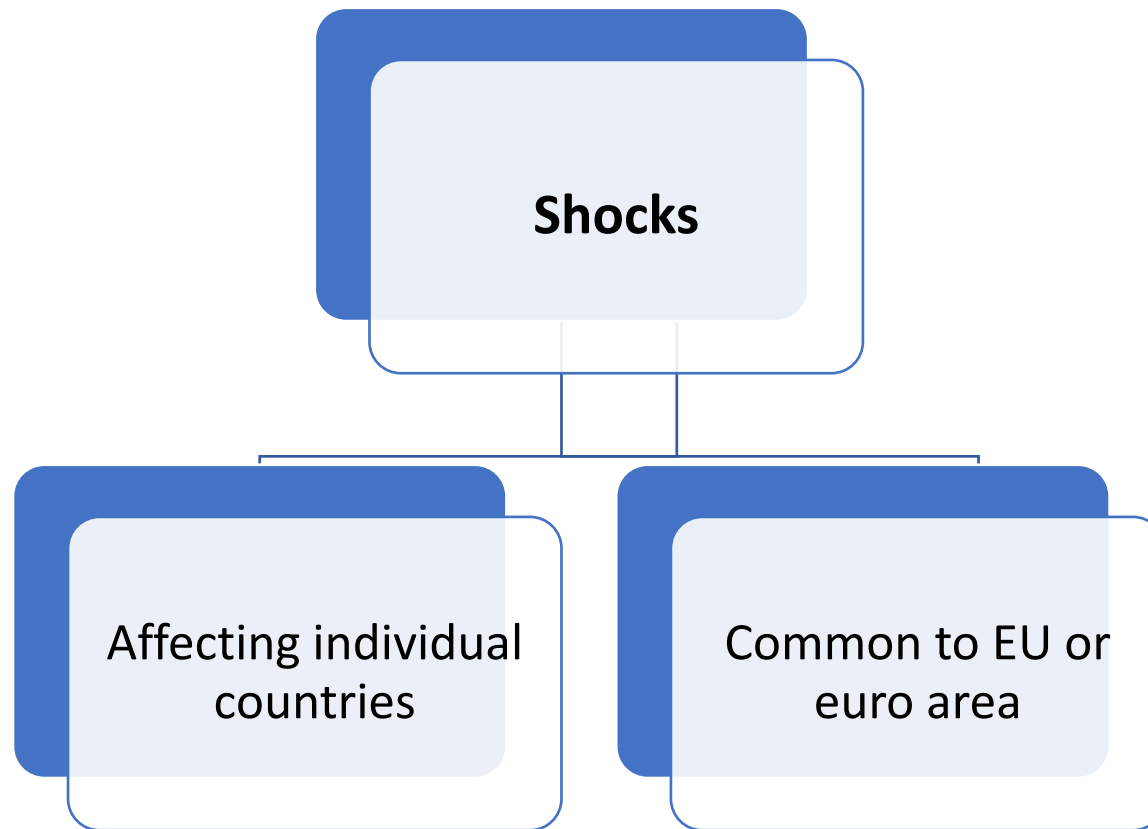
Euro area:

- Defend the integrity of the euro area
- Control spill-over effects
- Effective monetary policy transmission and business cycle synchronisation

THREE PILLARS OF CRISIS MANAGEMENT IN EUROPE



FUTURE SHOCKS/CRISIS SCENARIOS



Types of shocks:

- Economic
- Financial
- Disease
- Climate (transition & physical effect)
- Geopolitical conflict (war & access to goods and markets)
- Cyber (software & hardware)

WHAT IS NEEDED TO STRENGTHEN CRISIS MANAGEMENT

- Crisis management – **Conditionality 2.0**
- Policy coordination: revised **Stability and Growth Pact** & incentives for reforms
- **Fiscal stabilisation facility** to mitigate fragmentation
- **European backing of financial service union**
- **European public goods** - climate change - strategic independence - common infrastructure