THE EUROZONE CRISIS AND BEYOND

Presentation for
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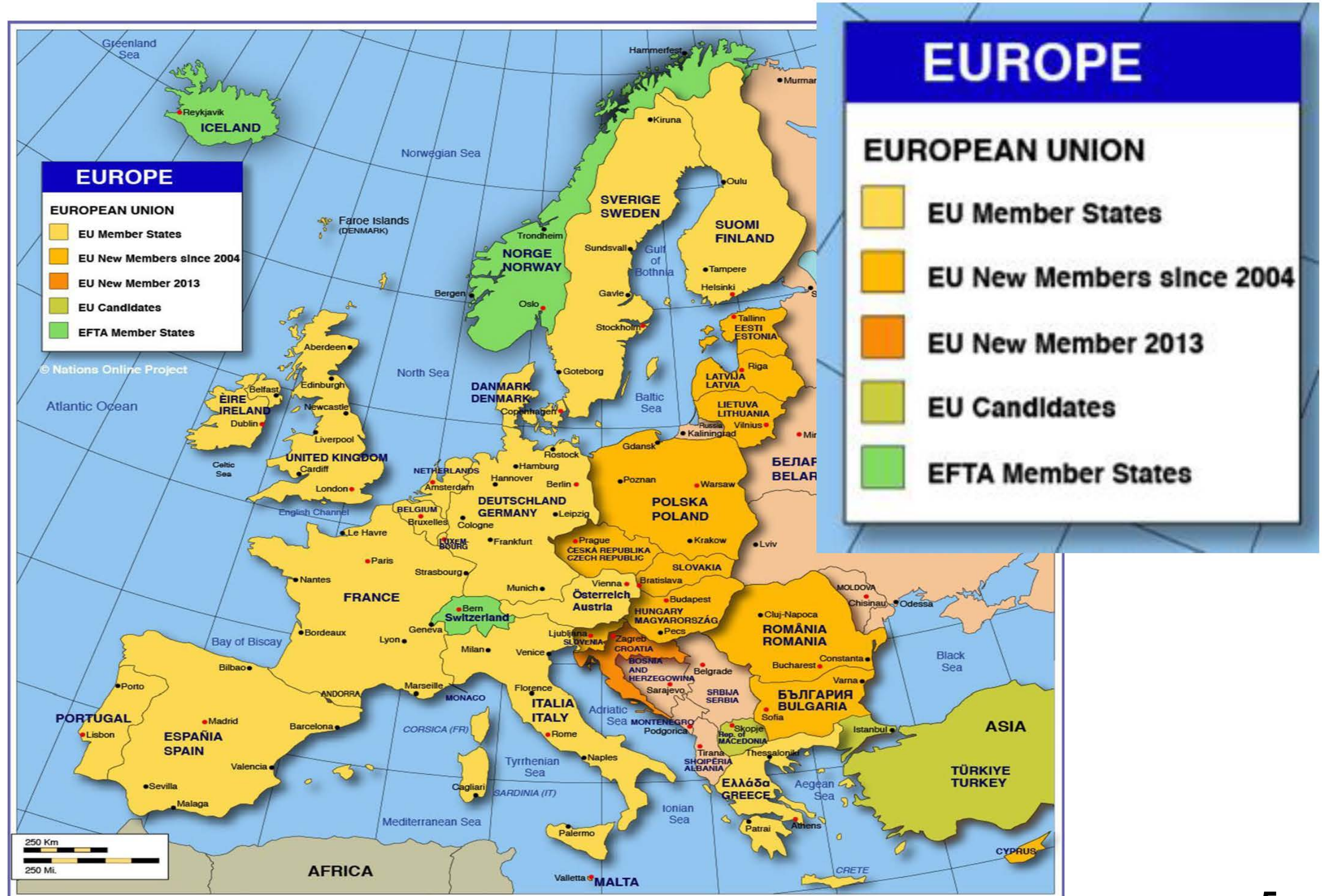
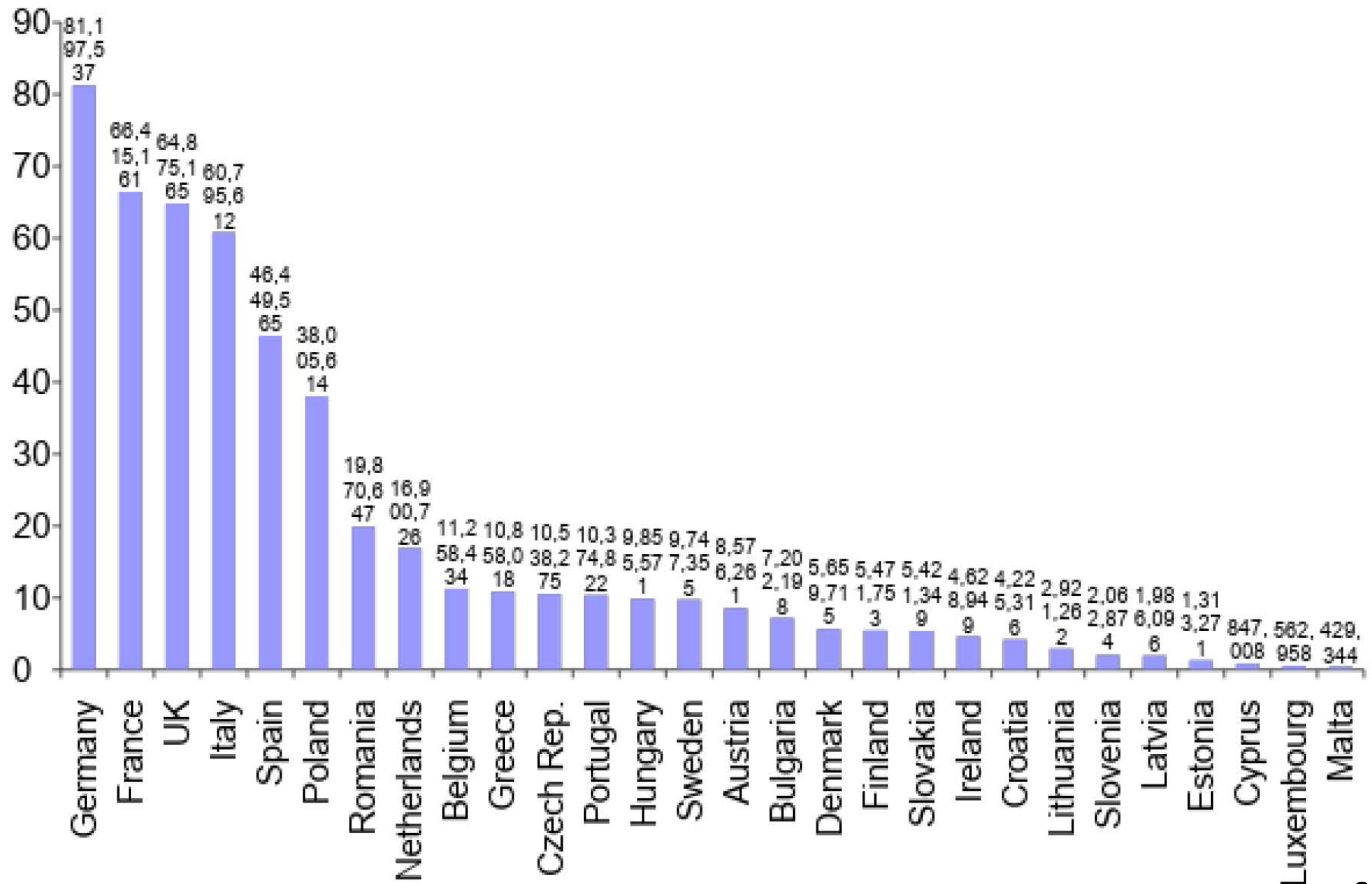
The EU – Brief Information

The European Union dwarfed by Asia and Africa

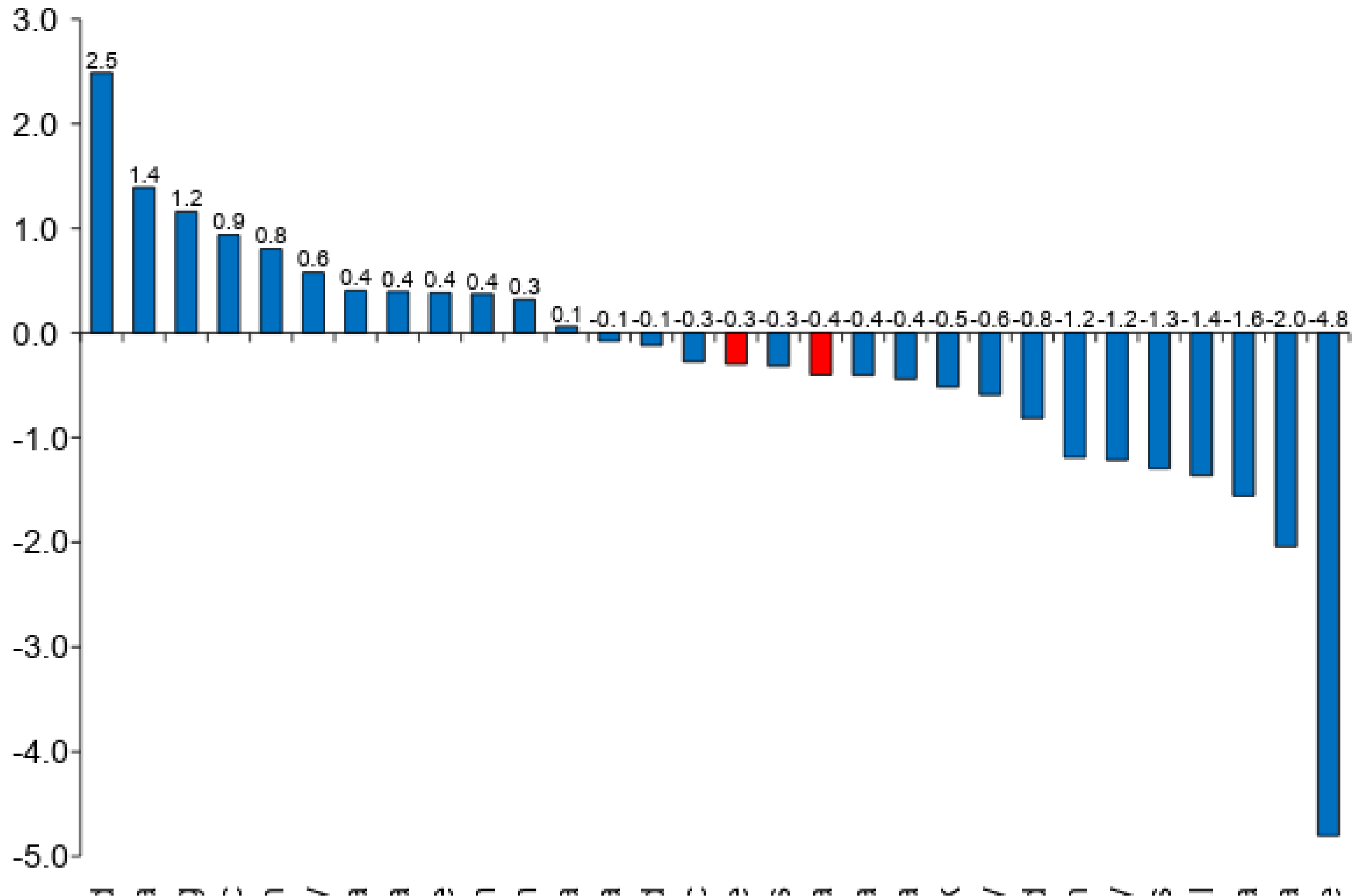
Map of the European Union



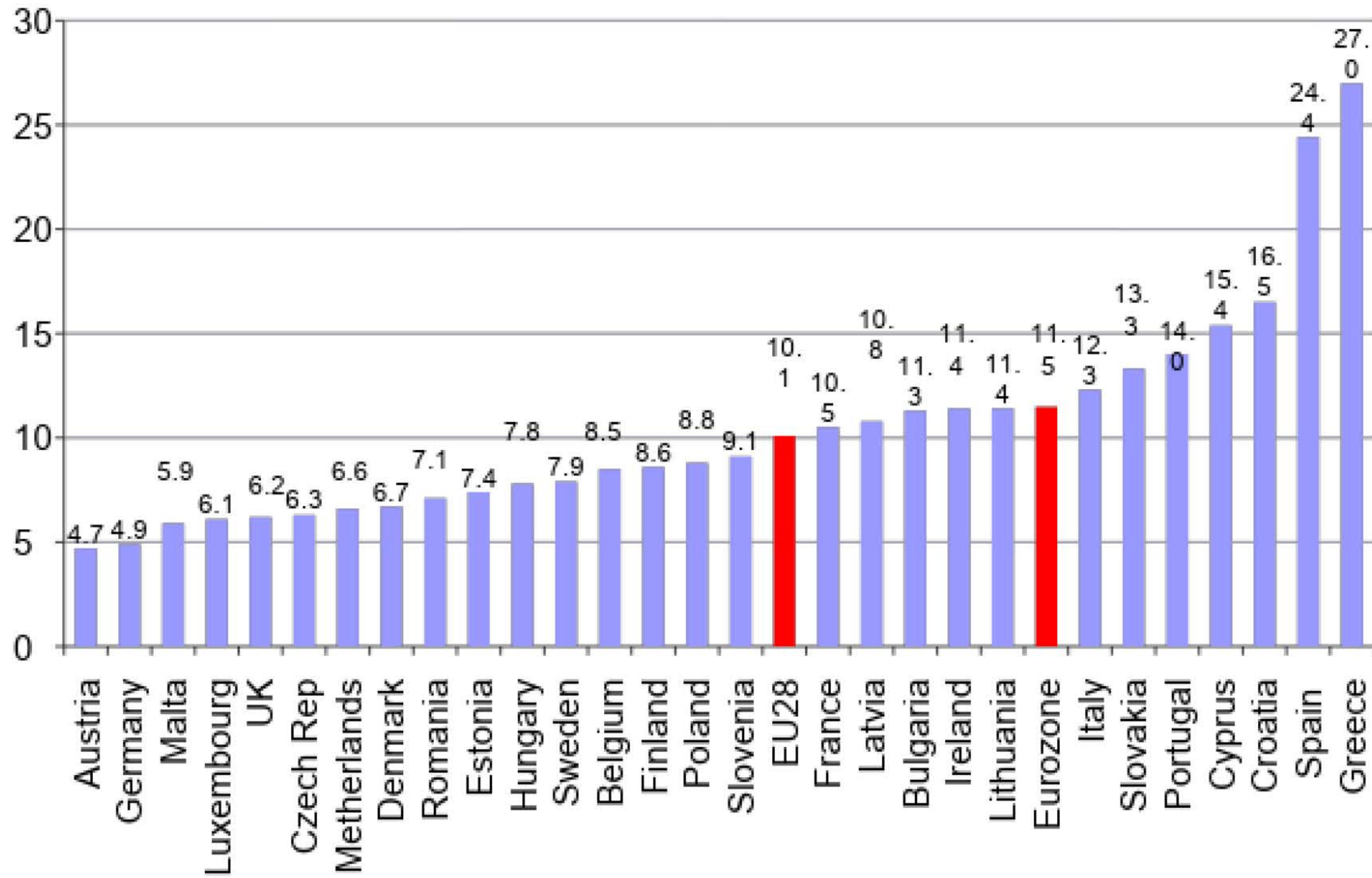
EU Population in 2014 totaling 508.5 Million



Real GDP Growth Rate (%) Average 2009-2014



Unemployment Rates (%) 2014



1957 to 2010 – From the EC to the EU

1957: Germany, France, Italy, Belgium, Netherlands and Luxembourg signed the Treaty of Rome.
1973: Denmark, Ireland and the UK joined the EC
1980s: Greece joins in 1981; Spain and Portugal in 1986
1995: Austria, Finland and Sweden join
2004: Ten Countries join of which eight were central and eastern European countries — the Czech Republic, Estonia, Latvia, Lithuania, Hungary, Poland, Slovenia and Slovakia and two were Mediterranean island states, Cyprus and Malta.
2007: Bulgaria and Romania join
2013: Croatia joins

Candidate countries: Macedonia FYR, Montenegro, Serbia and Turkey.
Potential candidate countries: Albania, Bosnia and Herzegovina and Kosovo

The Main EU Institutions

The European Parliament members are elected directly by the people in each member state. The EP shares legislative and budgetary power with the EU Council

The European Council are meetings of the Heads of State (summits)**. The Council of the European Union** is the EU's main decision-taking body attended by Ministers from all member states.

The European Commission is the executive body of the EU. Amongst other things, it takes steps to ensure that EU policies are properly implemented in the member states.

The Court of Justice, located in Luxembourg, ensures that EU law is upheld.

The European Central Bank, located in Frankfurt, with the remit to manages the EU monetary policy and the euro.

Directives and Regulations

A regulation has general application and is binding in all Member States. As such, regulations are powerful forms of European Union law. When a regulation comes into force it overrides all national laws dealing with the same subject.

A directive is also binding on all Member States regarding the results to be achieved, but leaves it to the national authorities as to the choice of form and methods. Directives are only binding on the member states to whom they are addressed, which can be just one member state or a group of them. In practice however directives are addressed to all member states.

These regulations and directive imply that member states forego some aspects of national sovereignty

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European Monetary Union

What is Economic and Monetary Union (EMU)?

Economic and Monetary Union (EMU) is part of EU law and is aimed at coordinating economic policy among EU member states, achievement of economic convergence among same states and ultimately adoption of a single currency (the euro).

All member states of the European Union are expected to participate in the EMU, although eligibility to adopt the Euro (the third stage of the EMU) is conditional on satisfying the so called Maastricht criteria. Two countries namely Britain and Denmark, have legal opt-outs and are not legally obliged to adopt the euro. The other seven members are obliged to adopt the europ when they are in line with the Maastrich criteria.

Origins: European Monetary System (EMS)

The system of fixed exchange rates, under the Bretton Woods arrangement, ended in 1971. The member states of the European Community decided to take steps to reduce exchange fluctuations between their currencies by means of an intervention in currency markets. This led to the creation of the European Monetary System (EMS) in March 1979.

The EMS involved, amongst other things, the creation of a reference currency called the **European Currency Unit** (ECU) composed of a basket of the currencies of the member states. Each currency had an exchange rate linked to the ECU; bilateral exchange rates were allowed to fluctuate with the ECU within a band of 2.25 %.

EMU: Three Stages during the 1990s

The EMU's first stage (which began 1 July 1990) involved the abolition of exchange controls.

The second stage (which began on 1 January 1994) provided for establishing the European Monetary Institute (EMI) in Frankfurt, with representatives of the governors of the central banks of the EU countries

The third stage was the introduction of the euro (which began in January 1999). Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain adopted the Euro for non-cash transactions. Greece joined them on 1 January 2001.

The European Central Bank

The European Central Bank took over from the EMI in 1998 and became responsible for the monetary policy of the EU as a collegial system with the Governors of the Central Banks of EU member states. Euro notes and coins were issued on January 2002 in 12 euro-area countries. National currencies were eventually withdrawn from circulation. Sweden, Denmark and the UK did not adopt the euro.

Following the 2004 enlargement, Slovenia (2007) Malta, Cyprus (2008), Slovakia (2009), Estonia (2011) Latvia (2014) and Lithuania (2015) also adopted the euro. Bulgaria, Croatia, Czech Republic, Hungary, Romania and Poland will adopt the euro when they are ready to do so in line with the Maastricht criteria.

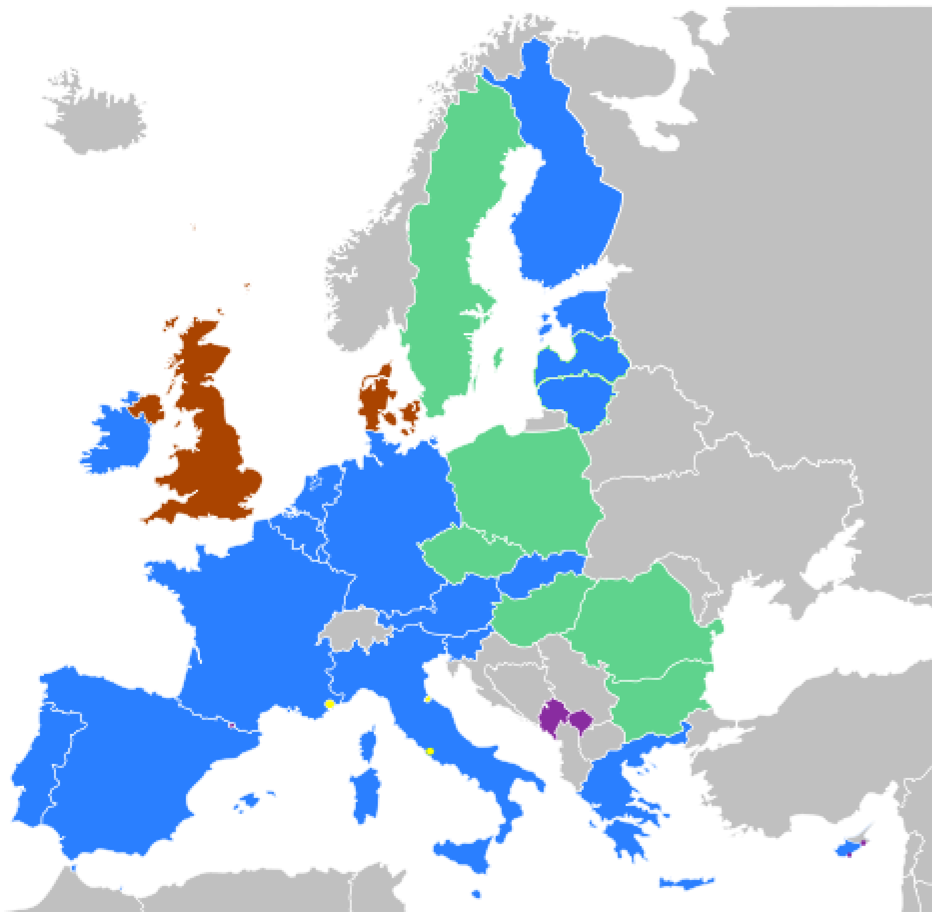
Adoption of the euro

Nineteen member states of the European Union have adopted the euro as their currency, and thus have moved to the third stage of the EMU. The other nine EU members use their own currencies, and are also members of the EMU, but have remained at the second stage.

Of the 10 non-adopters:
(a) Denmark and the UK obtained opt-outs and are legally exempt from joining the eurozone.*
(b) Sweden must convert to the euro at some point but has not yet joined the ERM II.
(c) Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania are yet to converge.

* (Denmark however is participant in the Exchange Rate Mechanism - ERM II - tying its currency to the Euro within a 2.25% band).

The eurozone



Blue shaded countries: 19 Participants in the Eurozone: Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Portugal, Slovak Republic, Slovenia, Spain

Green shaded countries: 7 countries obliged to eventually join the Eurozone (Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania and Sweden).

Brown shaded countries:
2 EU states with an opt-out on Eurozone participation (UK and Denmark).

Purple: Non-EU members that use the euro Andorra, Kosovo, Montenegro, Monaco, San Marino, and the Vatican City.

The convergence (Maastricht) criteria

An EU country must meet the five convergence criteria in order to adopt the euro. These criteria are:

Price stability: the rate of inflation not to exceed the average rates of inflation of the three member states with the lowest inflation by more than 1.5 %;

Inflation: long-term interest rates not to vary by more than 2 % in relation to the average interest rates of the three member states with the lowest inflation;

Deficits: national budget deficits to be below 3 % of GDP;

Public debt: not to exceed 60 % of GDP;

Exchange rate stability: exchange rates must have remained within the authorised margin of fluctuation with the euro for the previous two years.

Euro notes and coins

Coins have one common face, indicating their value, while the other side carries a national emblem. Coins circulate freely. Maltese coins, for example, can be used in other euro area country.

Notes are the same throughout the Euro area. There are denominations of 5, 10, 20, 50, 100, 200 and 500 euro and the notes increase in size as the denomination rises.

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The Stability and Growth Pact

What is the SGP?

The Stability and Growth Pact is a political agreement reached at the European Council in December 1996, aimed **at imposing discipline in the government finances** of member states.

It built on the Maastricht criteria and binds all euro area members to implement the so-called excessive deficit procedure if they do not meet the provisions of the pact, particularly that the budget deficit should be below 3% of GDP and government debt should be below 60% of GDP.

Following the euro-crisis the SGP has been reformed with

New Developments in the SGP

The new rules include more automatic procedures to issue warnings and sanctions against debt offenders, an annual national budget assessment procedure by the European Commission, empowerment of the Commission to conduct spot checks at national level and a find for fraudulent statistics on government finances and greater independence of statistical bodies.

The objective of the changes is that fiscal and macro-economic imbalances of Member States could be identified and tackled at an early stage. The rules of the Stability and Growth Pact have not been changed but there is increased monitoring of national budgetary policies.

Compliance reports as part of the SGP

All EU member states are each year obliged to submit a Stability and Growth Pact (SGP) compliance report for the scrutiny and evaluation of the European Commission and the Council of Ministers, with the country's expected fiscal development for the current and subsequent three years and a the Medium-Term budgetary Objective (MTO).

These reports are called "stability programmes" for eurozone member states and "convergence programmes" for non-eurozone member states, but they are essentially the same. If the EU Member State does not comply with both the deficit limit and the debt limit,

The European Stability Mechanism

The European Stability Mechanism (ESM) is a permanent structure as an intergovernmental organisation under public international law and is located in Luxembourg.

It has the function of a "financial firewall‟ so as to limit financial contagion by one member state.

As from 2014 the ESM had up to €500bn euros to help countries in difficulty.

The rescue fund is available to the 17 eurozone countries - but loans will only be granted under strict conditions, demanding that countries in trouble undertake budget reforms.

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The European Central Bank

The Role of the European Central Bank

As the overseer of monetary policy in the EU, the ECB has taken steps to stimulate the economy.

The ECB has place growth as a priority as against the tradition inflation targeting.

In multiple steps during 2012–2015, the ECB lowered its bank rate to historical lows.

The most recent drive by the ECB to stimulate growth in the EU, was the introduction on the US style quantitative easing (QE) which is essentially a bond-buying scheme.

Single Supervisory Mechanism

As a result of the euro crisis, in mid-December 2012, EU finance ministers agreed on a single euro-area bank supervisor thereby expanding the European Central Bank oversight role. The idea was to break the connection between banking problems and sovereign-debt crises. The institution is called Single Supervisory Mechanism (SSM).

The main aims of the SSM will be to ensure the safety and soundness of the European banking system and to increase financial integration and stability in Europe.

The reassurance by the ECB may have helped

In a 2012 statement, the ECB president, Mario Draghi, said that governments should not overdo austerity measures and if they are to cut expenditure this should be done on operations and not on investment, particularly in the infrastructure.

He also vowed during a 2012 speech in London, to do "whatever it takes" within the central bank's mandate to preserve the euro.

Mario Draghi

Mario Draghi, the president of the European Central Bank, considered by many as a possible saviour of the euro.

Quantitative Easing (QE)

In March 2015 the ECB ushered in a Quantitative Easing (QE) scheme (buying government bonds) worth about €1.1 trillion euros (even though there was German opposition to this). This resulted in a drastic depreciation of the euro (making EU exports cheaper and imports more expensive) and in reduced Bond yields. The asset purchases are intended to continue until the end of Sept 2016 but could be extended. The idea is to restore inflation to the ECB's target of just below 2% and lower borrowing costs.

In December it extended QE by six months until March 2017, raising the programme’s total size from €1.14 trillion to €1.5 trillion. Interest rates, which first fell below zero in

Quantitative Easing (QE)

The bond-buying programme is not yet having a major effect on unemployment as this is still high and deflation is still a threat, although it is expected that eventually the QE will bring about a turnaround in the EU economies.

In addition, the stimulus and the negative interest rates did not weaken the euro as expected.

It would seem therefore that Mario Draghi's magic touch is not working.

However he asserted that "Without ECB action over the last three years, the eurozone would have descended into "disastrous deflation".

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Greece and the Euro Crisis

The meaning of the crisis

The European debt crisis was essentially a major financial problem, leading to a situation where some euro area member states could not repay or re-finance their government debt.

When a particular country defaults on its sovereign debt the creditor nations also experience difficulties and hence the contagion effect.

The meaning of the crisis

There are various explanations for the crisis. One explanation is that countries with weak economic fundamentals were able to free-ride on the euro area high creditworthiness.

When n 1992, the EU member states signed the Maastricht Treaty, they undertook to limit their debt levels. However, some member states failed to abide by these rules, often hiding their malpractice through various methods including false data and inconsistent accounting. When joining the euro area, countries like Italy and Greece were able to enjoy high credit worthiness and favourable credit terms, leading to high private and government spending and housing bubbles , based on weak economic fundamentals

Origins of the crisis …2

Apart from the explanation just put forward, there were a combination of factors that may have led to the euro crisis, including:

- Lack of fiscal prudence and lax regulatory frameworks in some countries.
- Slow growth in major eurozone countries;
- Lack of competitiveness, which could not be corrected by devaluation of the domestic currency in the euro area;
- Housing bubbles in some countries, threatening the financial market;
- Loose banking regulations, which fuelled the housing bubbles.

Origins of the crisis …1

Fears that the global financial system, including the euro system could be on shaky grounds started in 2008, much before the Greek problem emerged in its fullest.

In February 2009 European members of the G20 group, which represents the world's largest economies, met in Berlin and agreed on the need for a common approach to combat the financial crisis.

Within the euro area, it was obvious that economic governance differed markedly between member states. Even before 2010, it was already known that the Greek government did not say the whole truth regarding its public finances when it applied to join the euro area.

The Greek Problem

In 2010, when the possibility of a Greek default started to be taken more seriously, the crises started to unfold in an alarming manner.

Although Greece is a small country and its share of the euro area economy is less than 3%, many banks are exposed to the Greek sovereign debt.

In addition, it was feared that a Greek exit from the Euro area could have a domino effect, as other countries could feel the pressure to exit, aided and abetted by the growing Eurosceptic political movement.

The Greek economic needs reforming ...1

Greece was in dire need for economic reform and a high debt ratio was not the only major problem. The were various barriers to entry, open and hidden, which mostly benefit and protect vested interests.

Public sector unions were very strong and a considerable proportion of the economy was, directly or indirectly, in government hands.

In addition the tax system was very inefficient, leading to tax evasion and corruption.

To complicate matters there is the ticking bomb in an

Rescuing Greece

In March 2010 Euro members (together with the IMF and the European Central Bank – called the Troika) agreed to help Greece combat its financial problems to allow a €110 billion loan for Greece, conditional on the implementation of severe austerity measures.

A second bailout of €140 billion was agreed upon in July 2011. The second bailout carried a lower interest rate than the first, but had more complicated elements.

Greece also managed to negotiate a 53.5% reduction in its debt burden to private creditors, while any profits made by eurozone central banks on their holdings of Greek debt will be returned to Greece.

Harsh austerity measures for Greece

- Public sector limit of annual bonuses.
- Cut in wages for public sector utilities employees.
- Limitations on payments to high earning pensioners.
- A special tax on high pensions.
- Limitations on overtime pay.
- Special taxes on company profits.
- Increases in VAT and increases in on alcohol, cigarettes, and fuel.
- Scaling of pension age to life expectancy changes.
- retirement age for public sector workers has increased
- Public-owned companies to be reduced.
- In the second bailout, the European Commission, the ECB and the IMF also requested Greece to take measures to render its economy more competitive.

Economic and social implications of austerity

The austerity measures have the desirable aim of reigning in fiscal imbalances and generating confidence in government finances and in the euro area.

However there are drawbacks associated with these measures. They may have a negative effects on economic growth and therefore may be counter-productive in that the tax base will be reduced

They also generate hardship among families leading to social unrest, resulting in the government diverting its attention from solving the economic problems.

The patient needs more cuts

Political implications of the austerity measures

The austerity programme, as expected, was considered to harsh and unfair by the Greeks as this led to heavy spending cuts and enormous tax increases to pay off Greek debts. This resulted in the electoral victory of the radical left (ironically in alliance with the populist right).

Greece now has a government , which is ruro-sceptic and anti-reform, compounding the Greek problem.

But solving Greece's deeper financial problems is very difficult and although the Greek governance still enjoys popularity, the support is dwindling as the government is finding it difficult to keep its promises.

Greece debt repayment timetable

Protesters take part in an anti-austerity pro-government demonstration in Athens.

Souring Greek/German relations ...1

The Greek debacle soured relationships between Germany and Greece, and unbecoming accusations by Greece could have a major negative effect on the euro zone. The former Greek Finance Minister Yanis Varoufakis, had, in 2013 made a rude gesture at Germany suggesting that the Greeks should simply refuse to pay the debt.

The relationship between Germany and Greece are still acrimonious but have healed somewhat as a result of Germany's willingness to help Greece in the migration crisis.

Germany as seen by many Greeks

Germany as seen by many Germans

The PIIGS

Portugal, Ireland, Italy, Spain and Cyprus (euro area members in Southern Europe) also faced debt problems in recent years. Italy and Spain are large economies and this puts them in a relatively strong position and could both be potentially solvent.

The Southern Europe countries that faced problems (other than Cyprus) labelled PIIGS (Portugal, Ireland, Italy, Greece and Spain).

At the moment, Greece and Italy would seem to be still facing series problems relating to economic reform.

Worrying situation in Greece and Italy

Greece and Italy would seem to pose the most worrying prospects in the euro area.

Ireland, Portugal and Spain

Ireland and Portugal to exited their bailout programmes in 2014 while Greece and Cyprus both managed to partly regain market access in 2015. Their bailout programme is scheduled to end in 2016.

Spain never officially received a bailout programme. Its rescue package from the ESM was earmarked for a bank recapitalization fund and did not include financial support for the government itself.

Ireland, Portugal and Spain

The euroarea difficulties may no longer be called a crisis but it has been followed by what seems to be chronic slow growth and high unemployment rates.

Some authors argue that the euroarea crisis was not a sovereign-debt crisis, but one of massive capital flows across borders, which led to private sector debt which eventually got banks into serious trouble.

That trouble than led to economic downturns and bank failures, both of which led to growth in sovereign debt burdens.

Recent developments re Greece

Greece has benefitted from three bailouts so far, and has undertaken a major debt restructuring, but the problem is not yet solved. Greek unemployment remains the highest in Europe at about 25%. Many companies have left the country and relocating in Bulgaria, Albania, Romania and Cyprus as a result of over-taxation.

To make matters worse, tourism has been negatively affected because of immigration problem. As a result Greece is experiencing another recession.

And to make matters even worse, it appears that the IMF wants to wash its hands from the bailout programme and to leave Greece's €86 billion rescue package to the European

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Slow Growth in the Euro Area

The current eurozone problem: Slow growth …1

The original euro crises was mostly financial brought about by fiscal imprudence of some member states. The Euro market actually calmed down during 2014 and 2015. The interest spread on government bonds in Italy and other countries in trouble have narrowed. Many EU banks that were experienced liquidity problems had healthier balances, as evidenced by early repayment of the 3-year loans they took from the ECB. Also the European Central Bank, erstwhile focusing exclusively on price stability would seem to be also considering promoting economic growth in its remit But a new crisis was ushered in 2014 and 2015 – relating to slow economic growth rates and high unemployment rates.

The current eurozone problem: Slow growth ...2

The current eurozone problem: Slow growth …3

The slow-growth crisis is not exclusively based on high public debt ratios, but on lack of competitiveness. It has led to high rates of unemployment and a Japan-type deflation.

Currently even the German economy, the European powerhouse, is experiencing relatively slow growth.

Difficult uphill climb

The prolonged slow-down in the EU

While the US, UK, Canada, Australia, New Zealand and Japan registered positive growth rates between 2012 and 2014, the eurozone economies as a whole contracted during the same period. But there were divergences within the eurozone, with positive growth rates for Germany and France, and negative growth rates for Spain, Portugal, Italy, Greece and Cyprus.

The Greek economy contracting by about 10% during the same period of 3 years, generating an unemployment of about 25%.

EUROZONE CRISIS
So, we're all agreed. We don't know what to do

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Impact on the Philippines

Impact on the Philippines and South-East Asia

In a recent study, a paper by the Asian Development Bank (ADB) stated that the Philippines and other developing countries in Asia have the capacity to remain stable in the event that the prolonged crisis in the eurozone should evolve into another global economic meltdown.

Paper available at:
http://www.adb.org/publications/economic-impact-eurozone-sovereign-debt-crisis-developing-asia

Impact on the Philippines and South-East Asia

Although further deterioration in the eurozone condition would negatively effect growth of Asian economies, the ADB paper argued that this would be to a manageable extent. In the Philippines this could mean a few percentage points lower in the growth rate attributed to the euro crisis.

The ADB further stated the impact of the slow growth of the EU was not expected to cause a recession in South-east Asia because countries in the eastern part of the globe have flexibility to implement measures to boost growth.

Impact on the Philippines and South-East Asia

One factor that renders the South-east Asian economies resilient is that their debt/GDP ratios are not high. The ADB paper states that this would give governments in Asia the flexibility to spend on stimulus programmes in the case of a downturn in trade and FDI.

In the case of the Philippines, the national government's debt to GDP ratio has fallen over the years to about 35 percent in 2014, with a GDP growth rate exceeding 6%.

Conclusion

It is not easy to exactly determine the effect of conditions in the EU on the Philippine economy, because there are many factors involved, including the Philippine Banks balance sheets and their exposure to the eurozone, which factors do not seem to have posed major problems.

However, although it appears that the Philippines was able to absorb the shocks that arose from the Euro crisis, as evidenced by its solid economic growth rates and its relatively low debt ratio, economic conditions in the EU are likely to have an effect on the Philippine economy, given that the EU is an important trade partner and a major FDI contributor.

THANK YOU FOR YOUR ATTENTION!