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**THE CURRENT ECONOMIC
CRISIS AND FINANCIAL
UPROAR IN THE EU**

He who blames his failure to a crisis neglects his own
talent and is more interested in problems than in
solutions
A. Einstein

Dr. Maria Lorca-Susino
Dept of Economics and Dept of International Studies


OUTLINE

- The euro: A quick overview
- The euro as a common currency
- The euro and an international and global currency
- The new monetary order
- The EU and the Eurozone:
 - The 1st economic crisis
- The current economic crisis and financial turmoil
 - Greece and the “bail-out plan”
- Final thoughts



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INTRODUCTION

The euro: an overview


The most dramatic change in the international monetary system since President Nixon took the dollar off gold in 1971.

Robert Mundell

The euro: a common currency area

- The adoption of the euro
 - The only other successful monetary union:
 - The US and the greenback after the Civil War of 1961-65
- Path to the euro:
 - Many trials from 1865 to 1971
 - An alternative in Europe:
 - The Union of Soviet Socialist Republics (USSR): from 1922-1991
 - The Werner Report → the Delors report and its 3 steps to adopt the euro:
 - Nominally on January 1999
 - Physically on January 2002

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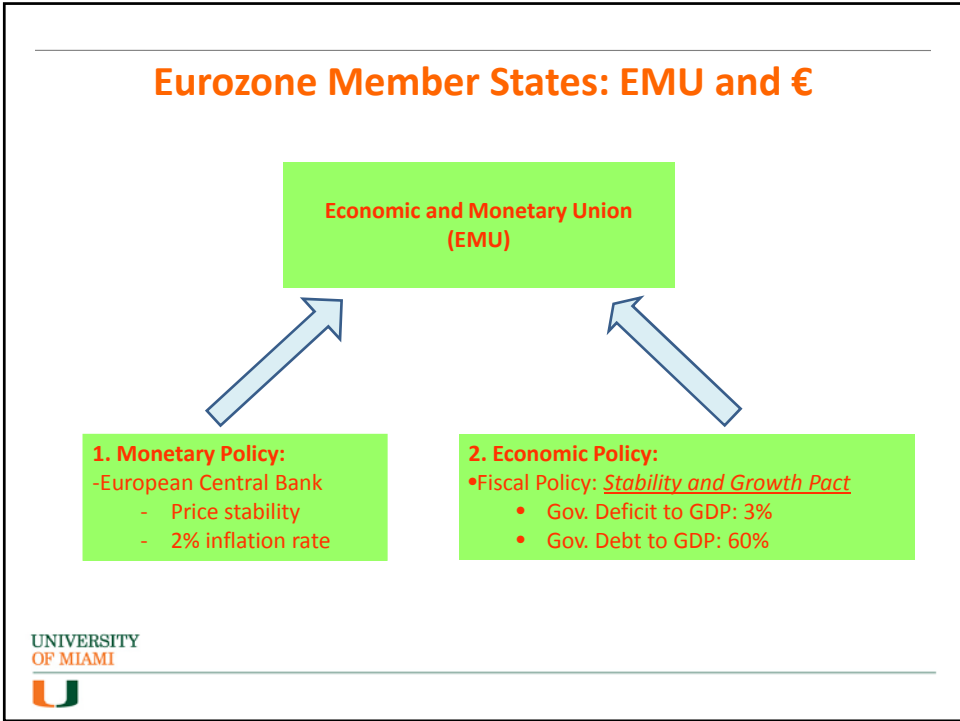
The Maastricht Treaty

- The set of requirements that must be met to join the euro:

Target	Requirement
Inflation Rate	No more than 1.5 percentage points higher than the 3 best-performing Member States of the EU.
Public finances	The ratio of the annual government deficit to gross domestic product must not exceed 3% at the end of the preceding fiscal year.
Interest rates	The nominal long-term interest rate must not be more than 2 percentage points higher than the 3 best-performing Member States.
Exchange rate stability	Applicant countries should have joined the exchange rate mechanism under the European Monetary System for 2 consecutive years and should not have devaluated its currency during the period.

Denmark, Sweden, and the U.K.

- Denmark's** national currency, the KROEN linked to the euro through
 - The government has met the economic convergence criteria for participating in the third phase of the (EMU), but a **September 2000 referendum rejected joining the EMU**
 - New Referendum: ?
- Sweden: rejected the euro in a popular vote** maintains its own currency, the Swedish Krona
 - The Swedish Riksbank founded in 1668 is the oldest central bank in the world
 - Convergence problems – **Working on inflation**
- The U.K.** The currency is the pound sterling.
 - The Bank of England is the Central Bank
 - The UK chose not to join the euro at the currency's launch.**
 - British Prime Minister, Gordon Brown MP, has ruled out membership for the foreseeable future.
 - Former Prime Minister Tony Blair promised to hold a public referendum based on a number (five) points.
 - In 2005, more than half (55%) of the UK were against adopting the currency, while 30% were in favour.



Enlargements: 2004 & 2007

Country	EMU entry date	Expected
Cyprus	January 1, 2008	
C.Republic		2013
Estonia	January 1, 2011	
Hungary		2012
Latvia		2013
Lithuania		2013
Malta	January 1, 2008	
Poland		2012
Slovenia	January 1, 2007	
Slovakia	January 1, 2009	
Bulgaria		2012
Romania		2014

Due to economic turmoil these countries will not be making this deadlines since they are far from complying with the Maastricht requirements

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Non-EU countries and the euro

Country	Pegged to	Adopted Euro	Agreement signed	Seeking
Monaco	French franc	January 1, 1999	December 31, 1998	
San Marino	Italian lira	January 1, 1999	December 31, 1998	
Vatican City	Italian lira	January 1, 1999	December 31, 1998	
Andorra	French franc Spanish peseta	January 1, 1999	December 31, 1998	Agreement but not membership to EU
Montenegro	German mark	January 1, 2002	Never	Membership to EU
Kosovo	German mark	January 1, 2002	Never	Membership to EU



Existing (struggling) Monetary Union

The East Caribbean dollar: in Anguilla, Antigua and Barbuda, Dominica, Grenada, Montserrat, Saint Kitts and Nevis, Saint Lucia, Saint Vincent, and the Grenadines.



The Central and West CFA franc used by currency used in 12 formerly French ruled African countries plus Guinea-Bissau (Portuguese) and Equatorial Guinea (Spanish)



The East African Shilling used in the East African Community (EAC) between the Republics of Kenya, Uganda, the United Republic of Tanzania, Republic of Burundi, and Republic of Rwanda




The Facto Monetary Union

The euro	is legal tender in Andorra, Kosovo, and Montenegro.
The Hong Kong Dollar	is used in Macau
The Russian rubble	is used in Russia and the Georgian Autonomous republics of Abkhazia and South.
The Swiss franc	in Liechtenstein
The U.S. dollar	is used in Palau, Micronesia, the Marshall Islands, Panama, Ecuador, El Salvador, Timor-Lester, the British Virgin Islands, and the Turks and Caicos Islands.

Planned Monetary Union

Name	Currency	Date
West African Monetary Zone – as part of the Economic Community of West African States (ECOWAS)	Eco	December 2009
Gulf Cooperation Council (GCC)	Khaleeji	2010
Caribbean Single Market and Economy (CSME) as part of the CARICOM	Unknown	Due between 2010-2015
Southern African Development Community	Unknown	2016
Alternativa Bolivarianas para los Pueblos de América (ALBA) - Bolivarian Alternative for the Americas → Bolivia, Nicaragua, Honduras, Cuba, Venezuela, Dominica, and San Vicente-Granadinas (which have the East Caribbean Dollar) and Ecuador is not sure bc it has the US dollar	SUCRE (Sistema Unificado de Compensación Regional)	4 th quarter of 2009 (Oct/Nov/Dec)



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Greece and market instability

The stability of the international monetary system can't hinge on the currency of one single country, even though that is the largest economy in the world

Zhou Ziaochuan

Introduction

- The past two years have been very dramatic for the EU, particularly for the Eurozone.
- In 2010 a sovereign debt problem unfolded in Greece.
 - solving this problem and avoiding contagion: a challenge.
- March 2011 was a decisive month: two dramatic but necessary financial and economic agreements:
 - reinforce the Stability and Growth Pact by automatically implementing harsher financial sanctions for rule breakers.
 - agree, after two years of debate, on establishing the European Stability Mechanism (ESM).



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- On Nov , 2010 → European Finance Ministers → approve a detailed agreement establishing a permanent crisis mechanism: EMS
 - The purpose → safeguard financial stability in the euro area by expanding the mandate of the European Financial Stability Facility (EFSF).
 - Why? after Greece received the rescue package in May 2010, however, the situation in Greece has not improved, and other countries have shown the need for economic support.
 - The EMS is ready to lend around €500bn, or about \$710bn
 - Supposed to operate in 2013 to replace the current EFSF.

Structure

- 1. Summary Greek situation by analyzing the two rescue plans
- 2. reviews and compares default cases such as Asia and Argentina
- 3. actions that have been taken to save the rest of the euro area countries
- 4. pinpoints the measures taken are not enough to settle the financial markets.

Understanding the Greek Conundrum: Two Rescue Plans and One Mission

- In May 2010 → bankruptcy with a country debt expected to reach about €350bn by 2014.
- Greece has not respected the Stability and Growth Pact
- Greece used “creative accounting” to work out the numbers on its national accounts in 2009, which led to the budget crisis in 2010.
 - in 2008 Greece presented budget deficit estimates for 2009, which stood at about 6.7% of GDP
 - in October 2008 the newly elected Greek government revised the estimate: from 6.7% of the gross domestic product (GDP) to 12.7% of GDP
 - It was then explained that Goldman Sachs helped Greece → obscure billions in debt from the budget overseers in Brussels.



The First Bail-Out

- The FIRST lending facility, or bailout, of €110bn (\$146.2Bn) on May 2, 2010
 - €30bn in standby agreement with the IMF and €80bn from euro area member states in the form of bilateral loans
- The terms of the bail-out : three year bailout plan that Greece would have to repay with an interest of 7.5%.
- The first loan, worth €30bn, was given before May 19, 2010 → the date by which Greece had to make debt repayment and avoid defaulting on its massive debt.
- IN RETURN: Greece was sked to take some extreme austerity measures: cut €30bn over the next three years → reduce public debt from 13.6% in May 2010 to less than 3% by 2014.
 - Some of these austerity measures:
 - scraping bonus payments for public sector workers,
 - capping annual holiday bonuses,
 - increasing the Value Added Tax from 21% to 23%,
 - raising taxes on fuel, alcohol, and tobacco by 10%
 - and taxing illegal construction



Results: General Strikes

One year later....

- In July 2011 → Greece asked for more money
 - Important: Greece was still entitled to the last payment of the first bail-out plan
 - €12bn payment due on June 29, 2011
 - The IMF asked for even more austerity
 - Greece promised: €14.32bn of public spending cuts and €14.09bn of tax increases for 5 years
- The second bail out: €109bn in new loans
- In return: Greece agreed to about €78bn in additional austerity measures and asset sales through 2015.
 - €6.4 billion spending cut from June 2011 to December 2011,
 - another €22 billion up to 2015,
 - and €50 billion in sales of assets.
 - This time some sacrifice on the bondholders' side.

Greece is NOT alone

- Default??: Greece should be left to default and self-organize: Argentina.
- “Default” :
 - Mexico first country which had difficulties.
 - the US provided funding with about \$50bn in loans.
 - The East Asian crisis was different.
 - Those countries helped either by the IMF, the World Bank, G7 countries, or a combination.
 - Thailand—the first country in the area which ran into financial difficulties → the US did not rush to save it → this country was regarded as insignificant → The 1997 East
 - This lack of response on the part of the US has been blamed and used to explain the spillover effect to the rest of the area.
 - Years later, Russia ran into sovereign debt difficulties and defaulted selectively after receiving some help.
- Alternatives to Greece:
 - No restructuring
 - Voluntary restructuring
 - Forced restructuring

What Happened in Greece: Agreed Default

- On March 2012 → Agreement
- Greece pushed through the bond swap offer which is key to its 130 billion (\$172 billion) bailout deal with bondholders representing 83.5 percent of the value of its bonds taking part.
- The country will now activate Collective Action Clauses on those who held out, raising participation to 95.7 percent.
- The International Swaps and Derivatives Association met to determine whether a credit event has occurred - which could trigger payouts on **credit default swaps** on Greek debt.
- After just 69 percent of those holding bonds governed by international law and issued by public companies accepted the deal, the deadline for them to accept has been extended to March 23.
- Greece's private investors — mostly banks and investment funds — have been asked to take a face value loss of 53.5 percent on their bonds."

Not alone in Europe

Country	Amount in euros
Greece	110bn in May 2010
Ireland	85bn in November 2010
Portugal	78bn in April 2011
Greece 2 nd bail out still under debate	102bn in July 2011


The EFSF has already committed about €256 billion out of the €440bn available to help Greece, Portugal and Ireland.

Summer 2012: Spain

- June 25, 2012. The Minister of Economy and Competitiveness, Luis de Guindos, sent the president of the Eurogroup, Jean-Claude Juncker, the letter requests on behalf of the Government of Spain, financial assistance for the recapitalization of financial institutions so require.
- The Fund for Bank Restructuring (FROB), acting on behalf of the Government of Spain, will be the institution receiving the funds channeled to financial institutions.
- This line of credit of up to € 100,000 million
- Conditions of the credit line → interest from 3%- 4%, with a cadence period of 5 to 10 years
- Bring in a group of auditors to study the state of banks

- Following the logic of the study of stress on the banking sector
- The study was released on Friday Sept 28 by the auditors → Oliver Wyman
- the need of Spanish banks would total @ €60.000 mill

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A SOUP OF LETTER

Churchill once said:

you can always count on the Americas to do the right things---after they have tried everything else.

ESM and EFSF: the No Bailout rule

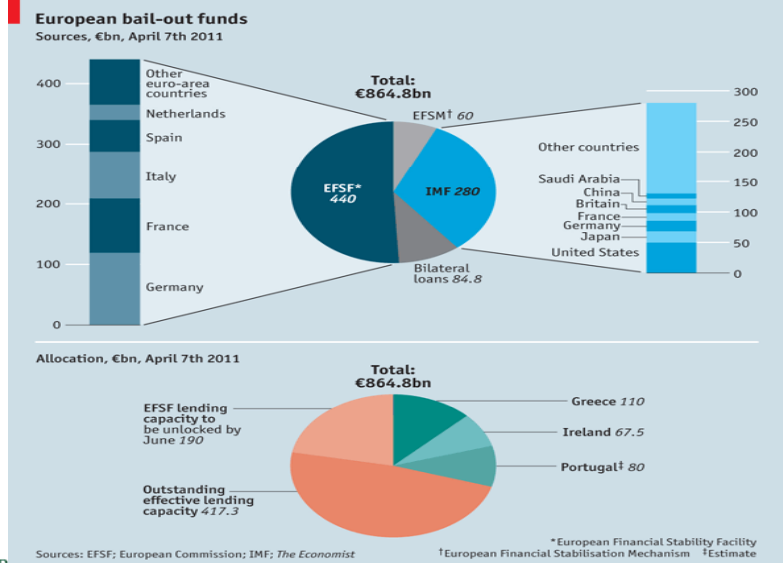
- EU approved 3 lending facilities in May 2010 to deal with Greek sovereign debt crisis and stop it might spread to other countries.
 - Deal with the no bail-out rule and art 125:
 - Article 12531 (ex Article 103 TEC) states that neither the EU nor a member state should be liable or assume the commitment of any public body or entity of any member state.
 - This article directly bans any direct fiscal transfers from one member state to another and also seems to ban purchases of sovereign debt in the primary market
- On May 11, 2010: the Council of the European Union approved the Council Regulation (EU) No 407/2010, which established the European financial stabilization mechanism
 - the No-Bail out rule of Article 125 was bypassed using Article 122(2) of the Treaty.

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EFSM

- On May 9, 2010, the EU's finance ministers adopted a regulation establishing a European Financial Stabilization Mechanism (EFSM)
 - 2nd Facility: maximum total lending capacity of €60bn from the EU budget and administered by the European Commission
 - 3rd Facility: the capacity to issue bonds guaranteed by EAMS for up to €440 billion for on-lending to euro area member states (EAMS) in difficulty, subject to conditions negotiated with the European Commission, and in liaison with the European Central Bank and International Monetary Fund, and to be approved by the Eurogroup.
 - International Monetary Fund: €250bn



Where is this money coming from?

Country	Amount
Germany	119,390.07 (27%)
France	89,657.45 (20%)
PIIGS	161,562.71 (36%)
Portugal	11,035.38
Ireland	7,002.40
Italy	78,784.72
Greece	12,387.70
Spain	52,352.51

THE BAILOUTS

- Two vehicles to save the Eurozone:
 - 1) The European Financial Stability Facility (EFSF) → €440 bn in loans from plus the IMF, the European Commission and other → \$622 bn
 - 2) The European Stability Mechanism (ESM) → will take effect in 2013 → \$996bn
- Bailouts so far:
 - Greece → 110bn
 - Ireland → 67.5bn
 - Portugal → 80bn

The ESM

The temporary fund EFSF is set to expire on June 30, 2013, and has around 140 billion euros of bailout fund left available.

The ESM, which was originally scheduled to come into force in July 2012, has been expected to help increase the "firewall" and calm market.

Sept 10, 2012 → Federal Constitutional Court of Germany approved the ratification of the European Stability Mechanism (ESM) paving the way for the permanent bailout fund and other crisis-battling instruments to go into operation.

- But the court said the German parliament should "receive comprehensive information" over future decisions made by the ESM and Germany's financial burden in the fund should be limited to its share of the capital stock or about 190 billion euros (245 billion U.S. dollars).
- Any increase of the burden should not happen "without agreement of German representatives," said Court President Andreas Vosskuhle in a statement.

- The court has been considering more than 1,000 petitions against the ESM and the fiscal pact filed by German lawmakers, economists, professors and ordinary people since July. Around 37,000 plaintiffs were involved.
- The opponents argue that the ESM, as well as the fiscal pact to enforce budget discipline, strips the parliament of the power to decide how taxpayers' money should be used, thus infringing German constitution.
- They fear that Germany's contribution to the fund could be increased when the debt crisis spreads further in Europe.
- Once coming into force, the ESM will have a capacity of 500 billion euros for lending and purchasing bonds of indebted countries, such as Greece and Portugal.



Final Thoughts

That which does not 'kill' us makes us
stronger

Friedrich Nietzsche

- The EU and the Eurozone are in serious danger
 - Lack of supervision (see no evil, hear no evil, speak no evil)
 - This shows negligence → EU politicians should be held accountable
- Common fiscal policy → not viable
 - Budget will be imposed → fiscal sovereignty
 - Politicians are not longer needed...
- If PIIGS are asked to leave:
 - Currency devaluation with lack of comp → immediate bankruptcy
- What about Germany leaving the EU?
 - Best economy in the area and record high export rate despite euro
 - FX vendors still maintain the DEM as a currency
- Solution is not:
 - The European Monetary Fund
 - Institution to supervise financial activity

Thank you

