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Measures Implemented by "The Troika" for overcoming Great Financial Crisis in European Union

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Abstract- The latest financial crisis had strong impact on global economy. In European market exists specific situation conditioned with special institutional agreements that deteriorate consequences of financial crisis, and created a doubt about future of European Union. The crisis has deepened the problem of indebtedness within the European Monetary Union, increased unemployment. In these circumstances European Central Bank (ECB) banking had to implement measures to mitigate financial shocks in European countries, and made itself work between its monetary policy and liquidity policy. It is clear that there must be changes implemented to ECB liquidity operations. In this work we will show joint activities of International Monetary Fund (IMF) and European Central Bank in Euro zone crisis made to repair the damage that crisis made and to save the most affected countries from bankruptcy and social unrests. Governments that are most affected by the crisis have coordinated their responses with a committee formed by the European Commission, the European Central Bank and the International Monetary Fund named "the Troika", formed for enhance cooperation between them for overcoming impact of crisis.

Index Terms- The Troika, Great Financial Crises, European Union, IMF, European Central Bank, depth crises, monetary policy, liquidity.

I. INTRODUCTION

The world economy is still under the burden of Great Financial Crisis. Crisis began on July 2007 with the liquidity crisis due to the loss of confidence in the mortgage credit markets in the United States. The financial crisis brought about changes in the operation of central banks, it became necessary to think over of central banking in terms of both functions and instruments. The crisis has even raised the question of how central bank independence, can be reconciled with the new position of heightened influence.[1]

The European debt crisis culminated 2009, and it's characteristics was high government with structural deficits and accelerating debt levels. Vulnerable banking sector suffered large capital losses, most states in Europe had to bail out several of their most affected banks with some supporting recapitalization loans, because of the strong linkage between their survival and the financial stability of the economy.

Responding to the global financial crisis, in which then had brought upon the sovereign debt crisis in Eurozone; EU has been taking concrete steps through fiscal consolidation and a much stronger integration within the EMU. Hence most of the policies produced and introduced by EC and ECB are initially compose from the EMU. This means that the policies itself has the common initial purpose to not only curbing and preventing the crisis to get worse, but also to maintain economic stability in the unique system of EMU for longer term. The policies in this term are referred to kind of rules, agreements, or programs.[2]

Since the start of the global financial crisis, a number of emerging European countries have requested financial support from the IMF to help them overcome their fiscal and external imbalances. Four members of the euro area—Greece, Portugal, Ireland, and Cyprus—also accessed IMF resources. Access to IMF resources for Europe is being provided through Stand-By Arrangements (SBA), the Flexible Credit Line (FCL), the Precautionary and Liquidity Line (PLL), and the Extended Fund Facility (EFF). Ireland's and Portugal's EFFs concluded in December 2013 and June 2014, respectively, and they then entered into Post-Program Monitoring (PPM).[3]

Most of the first wave of IMF-supported programs in 2008-09 was for countries in emerging Europe. The IMF provided front-loaded, flexible, and high levels of financing for many emerging European countries. In most EU countries—including in Hungary, Latvia, and Romania—this financing was provided in conjunction with the EU, while Poland has a Flexible Credit Line arrangement with the Fund. The IMF also provided financing to Iceland when its banking system collapsed in late 2008[4]

II. THE "TROIKA"

In purpose to fight the great financial crisis International Monetary Fund (IMF) was included in the rescue actions of the European Union (EU). The IMF provided in the financial assistance and economic adjustment programs for Greece, Ireland and Portugal by contributing around one third to the emergency funds.[5] Together with the EC and the ECB, IMF formed the IMF/ECB/EC-Troika responsible for negotiating and monitoring the economic adjustment programs for Greece, Ireland and Portugal. EU could not solve the problem by itself

[1] Liikanen Erkki: The economic crisis and the evolving role of central banks, Speech by Mr. Erkki Liikanen, Governor of the Bank of Finland and Chairman of the High level Expert Group on the structure of the EU banking sector, to the Paasikivi Society, Helsinki, 25 November 2013.

[2] http://www.imf.org/external/np/exr/facts/europe.htm
[3] http://www.imf.org/external/np/exr/facts/europe.htm
[4] Ibid
[5] Jost T. and Seitz F., The Role of the IMF in the European Debt Crisis, Weidener Diskussionspapier, nr.32,2012

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that is why it was necessary to create competent institutional body to deal with it.

International Monetary Fund (IMF) was involved in the rescue actions of the European Union (EU) to fight the sovereign debt crisis that emerged end of 2009 in several European Monetary Union (EMU) countries. The IMF participated in the financial assistance and economic adjustment programs for Greece, Ireland and Portugal by contributing around one third to the emergency funds. In a “Troika”, the IMF elaborated the economic adjustment programs for these economies and closely monitored their progress through quarterly reviews based on economic missions. The Troika can be seen as a new institutional body hat was formed on an ad hoc basis as the EU was not able to manage its problems alone and as politicians of the donor countries did not trust the European institutions and tried to reduce the moral hazard problem that was connected with the bail-outs.

Cooperation through the Troika is aimed at ensuring maximum coherence and efficiency in staff-level program discussions with governments on the policies that are needed to put their economies back on the path of sustainable economic growth. [6]

Decision to lend to above mentioned countries without having agreed on a convincing path back to a manageable level of debt was a exception from agreed principles for the IMF. It turns out it was very expensive decision for Europe and, now as a precedent for the future, it will be costly for crises to come in other parts of the world.[7]

Efficient financial planning assures protection for business investment. Measures for overcoming the financial crisis in EU must be joint activities in financial planning of IMF and ECB. Its main objective repair the damage that crisis made and that it will safe the most affected countries from bankruptcy and social unrests.

Troika determine six main policies in effort on helping troubled countries in Eurozone crisis.

- European Financial Stabilization Mechanism (EFSM) and European Financial Stability Facility (EFSF)/European Stability Mechanism (ESM)
- Stability and Growth Pact (SGP) and the “Six Pack”
- Macroeconomic Imbalance Procedure (MIP)
- European Semester
- New Supervisory Authorities
- Article IV Consultation[8]

Cooperation through the Troika is aimed at ensuring maximum coherence and efficiency in staff-level program discussions with governments on the policies that are needed to put their economies back on the path of sustainable economic growth. [9]
While the IMF coordinates closely with the other members of the Troika, Fund decisions on financing and policy advice are ultimately taken independently of the Troika process by the IMF’s 24-member Executive Board.

[6] http://www.imf.org/external/np/exr/facts/europe.htm
[7] Schadler, S., “Unsustainable Debt and the Political Economy of Lending: Constraining the IMF’s role in Sovereign Debt Crises”, CIGI Papers, No 19, 2013
[8] European Commission Directorate-General for Economic and Financial Affairs, The two-pack on economic governance: Establishing an EU framework for dealing with threats to financial stability in euro area member states, 2013, available at http://ec.europa.eu
[9] http://www.imf.org/external/np/exr/facts/pdf/europe.pdf

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IMF-Supported Programs in Europe

As of March 23, 2015, the IMF had arrangements with 8 countries in Europe, totaling about € 71 billion or $ 78 billion.

			Amount Agreed (billions)			Undrawn Balance (billions)		
Member[1]	Effective Date	Expiration Date	Euros (billions[2])	Dollars (billions[2])	As percent of Quota	Euros (billions[2])	Dollars (billions[2])	As percent of Quota
Stand-By Arrangements								
Bosnia	9/26/12	6/30/15	0.71	0.77	330	0.17	0.19	80
Romania	9/27/13	9/26/15	2.2	2.4	170	2.2	2.4	170
Serbia	2/23/15	2/22/18	1.19	1.30	200	1.19	1.30	200
Extended Fund Facility								
Albania	2/28/14	2/27/17	0.38	0.41	492	0.26	0.28	335
Cyprus	5/15/13	5/14/16	1.1	1.2	563	0.7	0.7	329
Greece	3/15/12	3/14/16	30.24	33.00	2,159	17.24	18.81	1,231
Ukraine	3/11/15	3/10/19	15.7	17.1	900	11.2	12.2	642
Flexible Credit Line								
Poland	1/14/15	1/13/17	19.7	21.5	918	19.7	21.5	918
Total			71.3	77.8		52.6	57.4	

Source: IMF Staff calculations.

[1] Poland, Romania and Serbia's arrangements are treated as precautionary by the authorities.

[2] Calculated using the prevailing exchange rate on March 23, 2015.

Table 1: IMF-Supported Programs in Europe[10]

[10] http://www.imf.org/external/np/exr/facts/pdf/europe.pdf

Cooperation through the Troika is aimed at ensuring maximum coherence and efficiency in staff-level program discussions with governments on the policies that are needed to put their economies back on the path of sustainable economic growth and job creation. [11]

While the IMF coordinates closely with the other members of the Troika, Fund decisions on financing and policy advice are ultimately taken independently of the Troika process by the IMF's 24-member Executive Board.

The European Bank Coordination Initiative The Vienna Initiative was launched at the height of the financial crisis in 2008/09 to help avoid a rush-to-the-exit of Western European cross-border banking groups whose subsidiaries dominate the banking systems of CESEE. Banks entered into explicit exposure maintenance agreements in the case of five program countries. This Initiative brings together key International Financial Institutions (EBRD, WB, and IMF), the European Commission and relevant EU institutions, the main cross-border banking groups, and home and host country authorities. [12]

III. Troika's financial plan for overcoming crisis

As a response to the global financial crisis which affected Eurozone, European Union taken steps through fiscal consolidation and a much stronger integration within the EMU, with purpose preventing the crisis to make unreperable damage, and to keep economic stability in the unique system of EMU for longer term.[13]

The cooperation with the other Troika-members has been essential as the IMF alone would not have been able to raise the emergency funds due to the sheer size of the rescue packages. By contributing around 33% to the rescue funds the IMF got a maximum 100% influence in the program design and surveillance procedure as the programs are IMF-style and the disbursement of each tranche of the funds ultimately depends on the decisions of the IMF executive board – indeed a good leverage.[14]

The plan for rescuing Eurozone from greater damage included financial assistance for Greece, Ireland, Portugal and Cyprus. Program considered very large funding because of macroeconomic imbalances and the because of loss of price competition. Programs were very optimistic about adjustment and recovery in Greece and Portugal. In all four countries, unemployment increased much more significantly than expected. The GDP deterioration happened because, large fiscal multipliers, poor external environment, including an open discussion about euro area break-up, an underestimation of the initial challenge and the weakness of administrative systems and of political ownership.

[11] Ibid
[12] http://www.imf.org/external/np/exr/facts/pdf/europe.pdf
[13] Ibid
[14] Jost T. and Seitz F., The Role of the IMF in the European Debt Crisis, Weidener Diskussionspapier, nr.32,2012

In Greece, a first program was initiated in May 2010, and superseded in March 2012 by a second program that was planned to runs till the end of 2014. In Ireland, the program was started in December 2010 and ended in December 2013. Ireland was the first country to exit a Troika program. The exit was 'clean' or 'full' in the sense that Ireland did not request any further financial assistance from its official creditors in the form of a precautionary credit line.

In Portugal, the program started in May 2011 and is due to end in May 2014. With less than four months before the end of the program, the big question at this stage is whether Portugal will be able to emulate Ireland and make a clean exit from its program, or if it will need a precautionary credit line or even a second program.

In Cyprus, the program only started in May 2013 and runs until May 2016. It is too early, therefore, at this stage to assess the implementation of this program, let alone to evaluate the prospect of Cyprus exiting the program when it ends. What can be done now, however, is an assessment of the circumstances that led to the program and the quality of its design.

The documents show that the IMF's baseline estimate – the most likely outcome – is that Greece's debt would still be 118% of GDP in 2030, even if it signs up to the package of tax and spending reforms demanded. That is well above the 110% the IMF regards as sustainable given Greece's debt profile, a level set in 2012. The country's debt level is currently 175% and likely to go higher because of its recent slide back into recession.

The documents admit that under the baseline scenario "significant concessions" are necessary to improve Greece's chances of ridding itself permanently of its debt financing woes.[15]

Even under the best case scenario, which includes growth of 4% a year for the next five years, Greece's debt levels will drop to only 124%, by 2022. The best case also anticipates €15bn (£10bn) in proceeds from privatizations, five times the estimate in the most likely scenario.

In the Annual Growth Survey 2011, the Commission highlighted three main areas of actions.[16]

- First is action in fundamental prerequisite for growth which requires on implementing a rigorous fiscal consolidation, correcting macroeconomic imbalances, and ensuring stability of the financial sector.
- Second is mobilizing labor markets and thus creating job opportunities by making work more attractive, reforming pension systems, getting the unemployed back to work, and balancing security and flexibility.
- Third action is frontloading growth which is done by tapping the potential of the Single Market, attracting private capital to finance growth, and creating cost-effective access to energy. The following 2012 Annual

[15] Nardelli A., IMF: austerity measures would still leave Greece with unsustainable debt, 2015, available at, http://www.theguardian.com/business/2015/jun/30/greek-debt-troika-analysis-says-significant-concessions-still-needed

[16] ec.europa.eu/europe2020

Growth Survey was presented on 23 November 2011 by the Commission, embodied with focus on five priorities.[17] The survey calls for the EU and member states to focus on pursuing differentiated, growth-friendly fiscal consolidation, restoring normal lending to the economy, promoting growth and competitiveness, tackling unemployment and the social consequences of the crisis, and modernizing public administration.

In terms of pensions, which have been the stickiest point in the negotiations, the plan demands reforms to:

- Create strong disincentives to early retirement, including changes to early retirement penalties.
- Adopt legislation so that withdrawals from the social insurance fund will incur an annual penalty, for those affected by the extension of the retirement age period, equivalent to 10% on top of the current penalty of 6%.
- Ensure that all supplementary pension funds are only financed by own contributions.
- Gradually phase out the solidarity grant (EKAS) for all pensioners by end-December 2019. This shall start immediately for the top 20% of beneficiaries with the details of the phase-out to be agreed with the institutions.[18]
- Freeze monthly guaranteed contributory pension limits in nominal terms until 2021.
- Provide to people retiring after 30 June 2015 the basic, guaranteed contributory, and means-tested pensions only at statutory normal retirement age, currently 67 years.
- Increase the relatively low health contributions for pensioners from 4% to 6% on average and extend it to supplementary pensions.[19]

IV. SUCCESS OF IMPLEMENTED MEASURES

If we consider the conditions for regaining market access we can make conclusion that the Irish program can surely be labeled as fully successful since the country was able to make a full exit from the program at the scheduled time, in December 2013, and issue debt at favorable rates. The Portuguese program forecasts the shortfall will drop below the EU's 3 percent limit in 2015, when he aims for a 2.5 percent gap. Portugal will follow Ireland in leaving its rescue program without seeking a precautionary credit line, the third nation to exit its bailout as the euro region rebounds from a four-year crisis. The Greek program cannot be judged as successful at this stage. The first program was discontinued and replaced by a second program after a haircut on privately-held government debt, but there is widespread doubt that the country will be able to regain market access without some form of write-down of its publicly-held debt. Greek prime minister, Alexis Tsipras, rejected the plans and called a referendum on whether to accept the creditors' demands. Result of referendum were dismission of creditors plans and procedures. After a turbulent month in Greece the agreement about debt repayment with creditors. For Cyprus is too early to judge if and how it will be able to regain market access at the end of the program, in May 2016.

If we consider success of programs if countries have adhered to their conditionality, all four countries have adopted the fiscal consolidation measures prescribed by the Troika. They had no alternative because official lenders were loath to offer more financing or to accept debt relief. It is a matter of complex judgment as to whether earlier and bigger debt restructuring for Greece, the bail-in of senior unsecured bondholders of Irish banks and further debt relief in Greece, Ireland, Portugal and Cyprus would have been (and perhaps still are) desirable. The judgment depends on considerations of moral hazard, signaling effects to other indebted countries and financial stability considerations. The four programmed countries have also implemented the measures that aimed to restore the health of their financial sectors, but the process is not over yet, including in Ireland. [20]

Greece and Portugal, accumulated further problems thereafter as the euro and access to cheap credit allowed them to retain antiquated models rather than forcing them to make the required structural changes that a modern economy, in particular one belonging to a monetary union, needs.

In Greece, Ireland and Portugal (we leave Cyprus aside since it is too early to look at outcomes), the fall in domestic demand was bigger than anticipated and, as result, unemployment increased by much more than anticipated. Imports also fell by more than expected in Greece and Portugal, though they actually increased in Ireland. At the same time, the current account deficit improved more than originally forecast. By contrast, export performance was better than anticipated. Altogether, therefore, the trade balance and the current account improved more and faster than expected. [21]

In these countries unemployment rates and debt levels are still very high. Growth prospects are still unsatisfactory and far too weak to address the unemployment challenge. Greece is in the worst situation with unemployment at more than 25 percent and public debt at 175 percent of GDP, but the other three countries, with unemployment at about 15 percent and public debt at about 120 percent of GDP, are also not faring well. High debt levels and generally weak growth determinants in program countries, a fragile global economy, disinflationary tendencies in the EU and the remaining banking problems, suggest that caution should be exercised when considering future exits.

In the case of Greece, it is hard to see how the country could exit from its program at the end of this year without some form of

[17] Ibid

[18] Nardelli A., IMF: austerity measures would still leave Greece with unsustainable debt, 2015, available at, http://www.theguardian.com/business/2015/jun/30/greek-debt-troika-analysis-says-significant-concessions-still-needed

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[20] European Parliament's Economic and Monetary Affairs Committee the Troika and financial assistance in the euro area: successes and failures, European Union, 2014

[21] Ibid

further debt relief and an accompanying framework to improve the structural drivers of growth. [22]

V. Conclusion

As the European Union and EU politicians lacked the necessary credibility, the involvement of the IMF in the EMU debt crisis makes sense as it can mitigate the moral hazard problems that are connected with the bailouts - at least as long as the IMF is able to closely monitor the economic adjustment programs and enforce reform progress. Strict conditionality is crucial for the success of the programs and the credibility of the whole process.

We must believe that joint activities in financial planning of IMF and ECB in Euro zone crisis can repair the damage that crisis made and that it will safe the most affected countries from bankruptcy and social unrests. There are different ways to assess programs. With the improvement of the economic climate in the euro area and Ireland's successful program exit, both market and political sentiment has become more optimistic about the possibility that the other program countries, and certainly Portugal and Cyprus, will be able to exit assistance when their turn comes. The current mood, which tends to focus on exit as a measure of success, is understandable, but should be partly resisted. In the case of Greece, it is hard to see how the country could exit from its program at the end of this year without some form of further debt relief and an accompanying framework to improve the structural drivers of growth.

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