Exiting the Troika Program: An Overview

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EXIT 03
THE FUTURE
NEXT EXIT

Overview

- What is the Program Strategy?
- What are the Remaining Challenges?
- How can Europe Help?

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- **What is the Program Strategy?**
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Externally-supported adjustment program

- **Background:** financial sector crisis results in loss of market access for sovereign

- **Program:**
  - EU and bilateral lenders: €45 billion
  - IMF: € 22.5 billion
  - Irish Authorities: € 17.5 billion
  - ECB continues to provide liquidity to banks

Ultimate Objective	**Sovereign Regains Market Access & Exits Offl. Financing**	
Proximate Policy Design Goals	Public debt sustainability	Restore health of financial system
	Revive Growth **Cut Unemployment** **Limit Loan Arrears**	Resolve private debt issues
	Enhance Competitiveness	Limit structural unemployment

Program Policy—Financial Sector

- Reorganization → universal full-service banks
  - Two pillar banks: BOI and AIB/EBS
  - Failed banks: IBRC
  - PTSB restructuring
- Recapitalization → 10½% core tier 1 (6% stress)
  - Independent loan loss forecast, PCAR
  - €24 bn recap completed 6/’12, public cost €17.8 bn
- Deleveraging → market funding
  - Core vs. non-core assets
  - Banks delevered more than half of €70 bn in identified assets

Program Policies—Fiscal

- Credible medium-term consolidation (3% deficit by 2015)
  - Wage bill cut within Croke Park agreement
  - Welfare rates cut
  - Non-pay current and capital budget
  - Personal income tax base broadening
  - Universal charge, elimination of PRSI reliefs
  - VAT increase

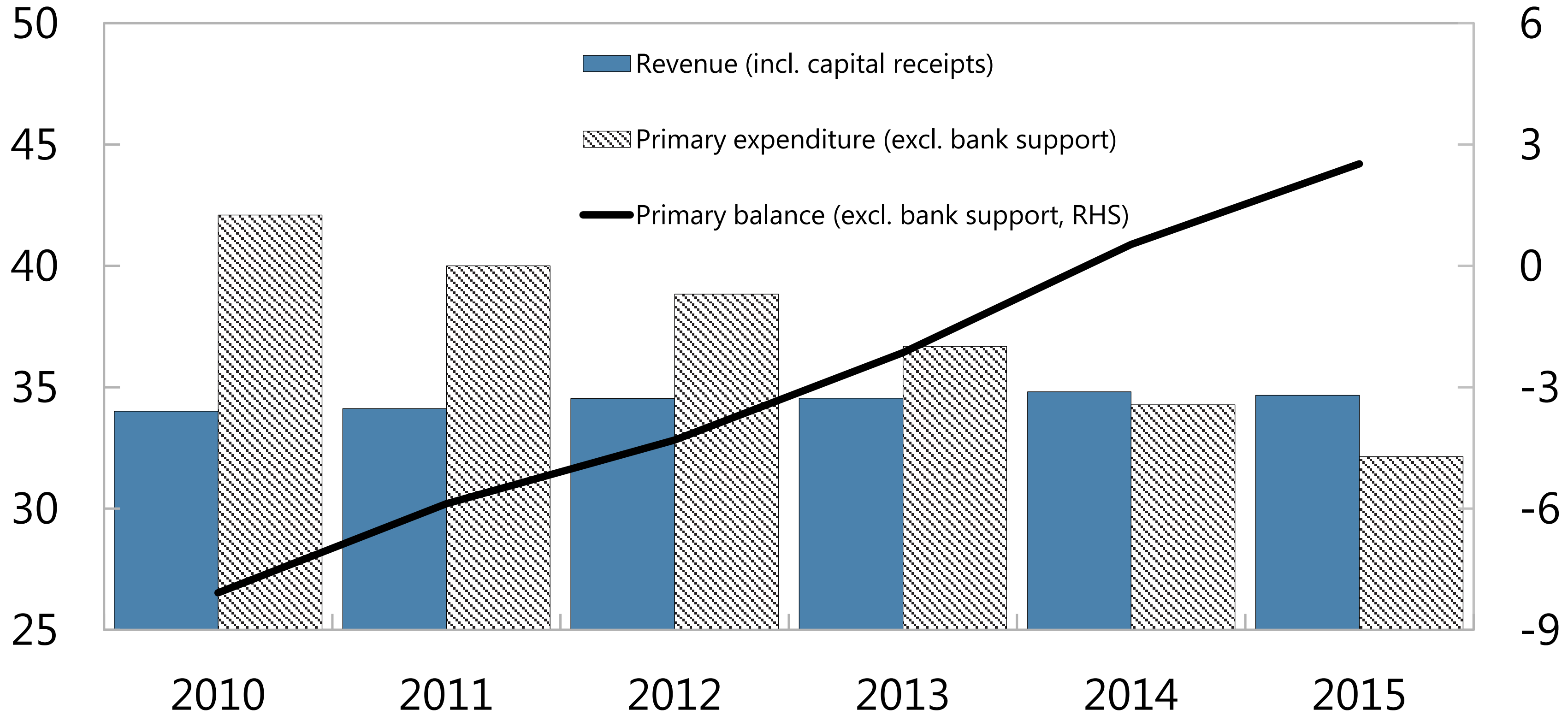
Measures	2011	2012	2013
(% of GDP)	3.5%	2.7%	2.1%

- Emphasis on ownership, quality, social cohesion
- Reforms: Fiscal Council, Fiscal Responsibility Law

Expenditure is brought in line with revenue gradually

Revenues, Primary Expenditure and Balance

(Percent of GDP)



Source: Department of Finance; and IMF staff estimates

Program Policies—Structural

- Mortgage Arrears Resolution Strategies (MARS)
- Personal Insolvency Reform
- Services and Goods markets
  - Reform of sheltered sectors (legal, medical)
  - Improving competition enforcement
- Labour market
  - Strengthening labor activation and training
  - Reforms of sectoral wage agreements
- Sale of state assets (about 2% of GDP from 2013)

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Financial:
Create conditions for robust credit flow

Arrest deterioration in bank asset quality	• Accelerate workout capacity & engagement • Implement personal insolvency reform • Strengthen framework for legal remedies
Regain bank profitability to sustain new lending	• Reduce deposit rates • Phase out costly government guarantee • Reduce operational expenses
Expand bank access to market financing	• Improve liquidity through deleveraging • Expand collateral -- Loan restructuring • **But:** Euro area problems, bank-sovereign linkages

Fiscal:
Complete consolidation in durable manner

- Full implementation of Budget 2013, but no additional measures if growth disappoints
- Full implementation of health sector savings
- Careful preparation for introduction of property tax
- Agreement with public sector unions

Alternatives to Consolidation?

- “Austerity is not working”
- Debt ≈122% of GDP, Deficit ≈8% of GDP

  ⇒ Sustainability needed for market access
- Additional fiscal expansion would imply:
  - slower debt reduction
  - official financing for longer
- Share of senior debt rises → market access?
- Use EU presidency to advance active growth strategy in Europe

Structural: Increase potential for employment-rich recovery

- Economic growth is pre-requisite for job creation
- Align education and training with market needs
- Increased engagement with long-term unemployed

Market access on sustained basis

June 29 statement
and
OMT introduction

- Irish bond spreads declined
- Government issued 5 and 8-year bonds
- Tapped international bond market Jan 8

Substantial risk remains

- Debt rising to 122% of GDP in 2013
- Economic recovery needed to put debt on declining path

→ **Avoid prolonged official financing**

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Break Sovereign-Bank linkage

- Government has high debt—not a strong owner of the banks
  - Bank access to market funding is limited and costly
- Temporary bank ownership by ESM
  - eliminate need for guarantees
  - increase other funding options (reduce deposit rates)
- Improved bank profitability
  - Restore capacity for sound lending
  - Support recovery
- Govt can reduce debt with proceeds from sale

Improve sustainability and prospect for durable market financing

- Debt-equity swap with ESM reduces government debt, breaks bank-sovereign loop, and improves growth prospects
- Refinancing of promissory note reduces financing needs in near- and medium-term
- OMT access reduces tail risks

Improve prospects for durable market access & avoid prolonged dependence on official financing

Conclusion

- **Key Program Objective**:
  - Exit from Official Financing
- **Need**:
  - Re-gain Market Confidence
- **Means**:
  - Debt sustainability $\longrightarrow$ need consolidation
  - Credit flows $\longrightarrow$ need financial sector
  - Growth $\longrightarrow$ structural reforms
- **And:**
  - Break Bank-Sovereign Link

Thank You