The IMF, CESEE and Banking

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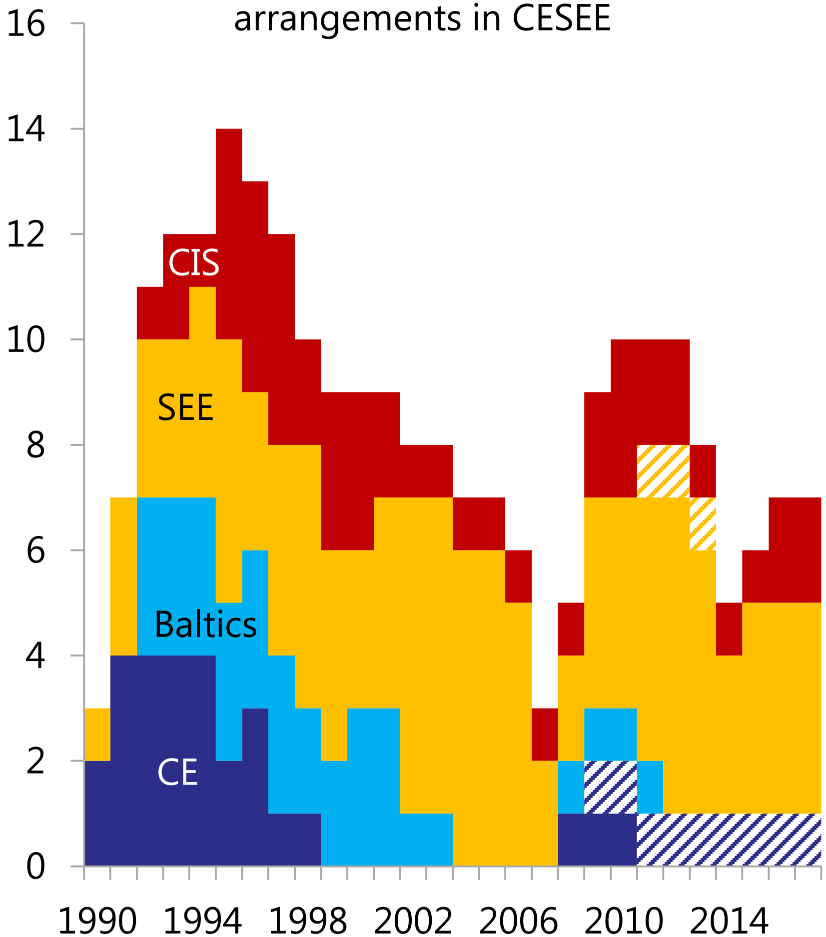
The IMF has had close involvement with CESEE since early transition

- It supported the transition to market economies with
  - Financing
  - Technical Assistance
  - Training
- It provide financial help and TA during the 2008/09 crisis and beyond

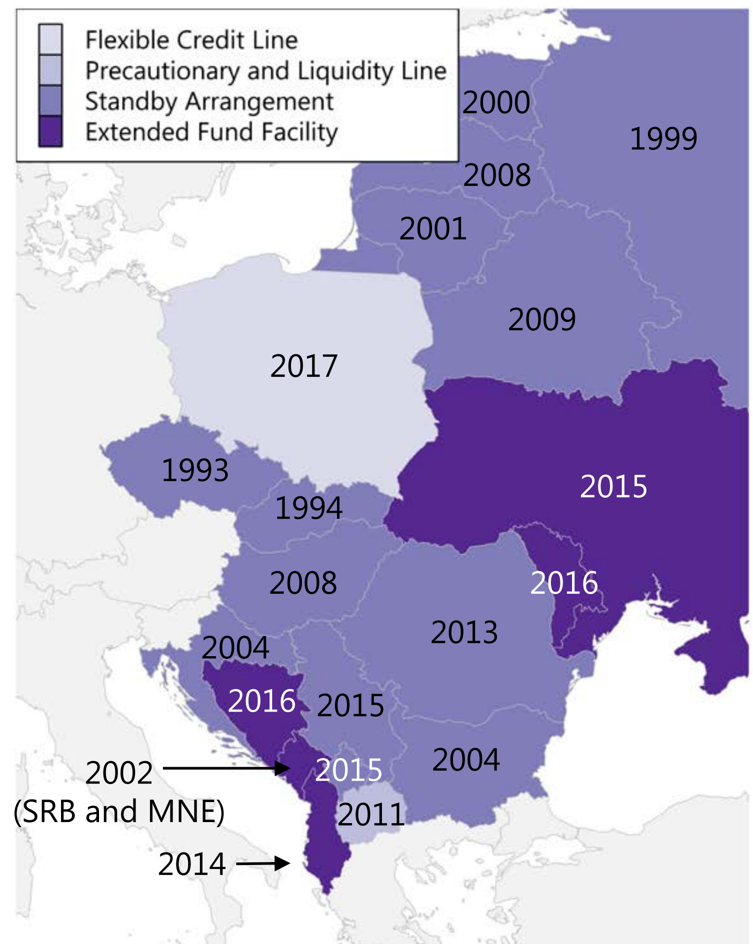
Two waves of IMF programs: early transition and post-2008

Number of countries with active IMF arrangements in CESEE



Note: Dashed pattern shows precautionary programs.

Latest IMF arrangements by country



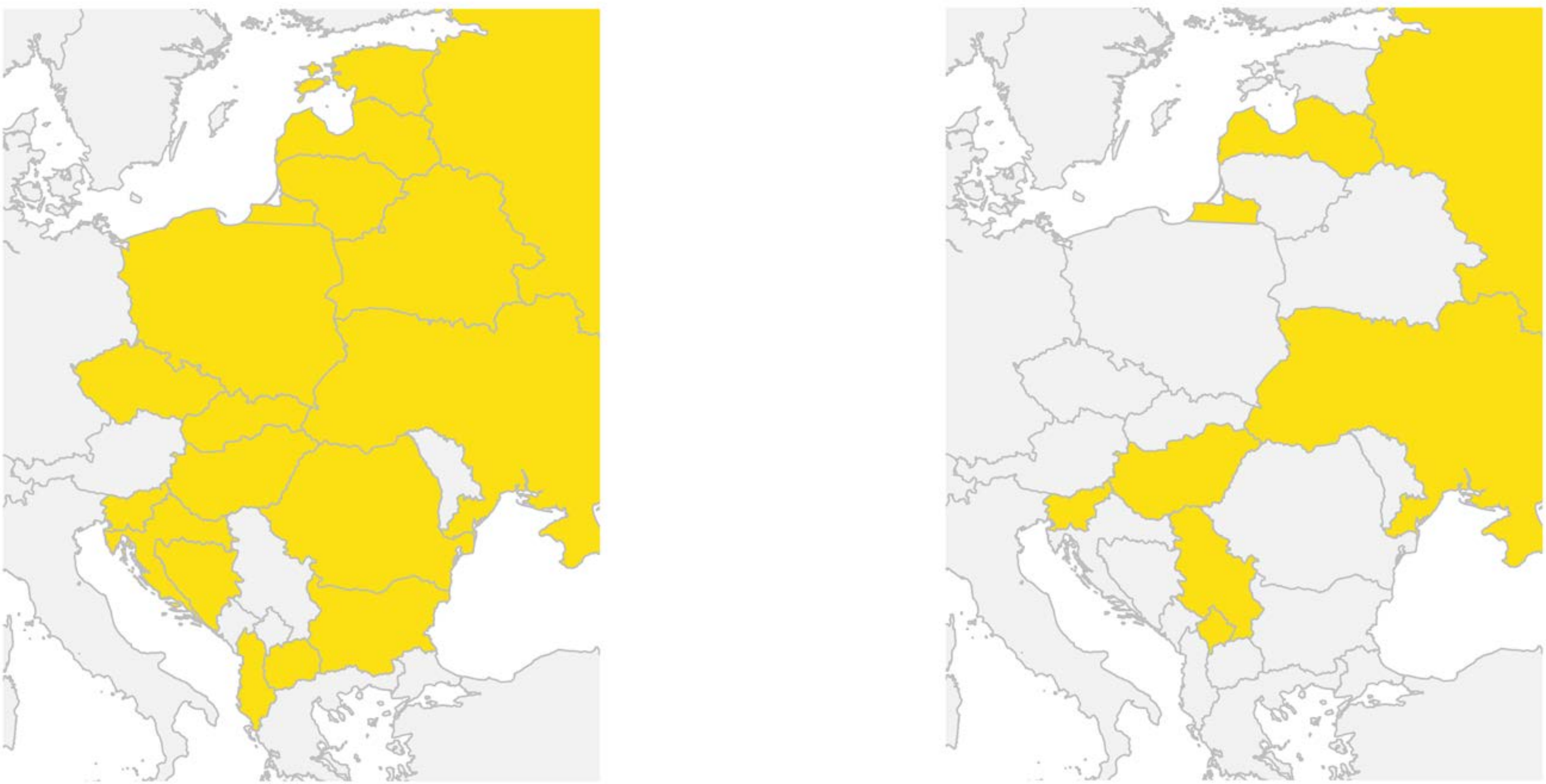
Note: Years indicate start date of arrangement.

Many of the IMF programs originated in banking sector problems

- Most countries had banking crisis in 1990s

Banking crises

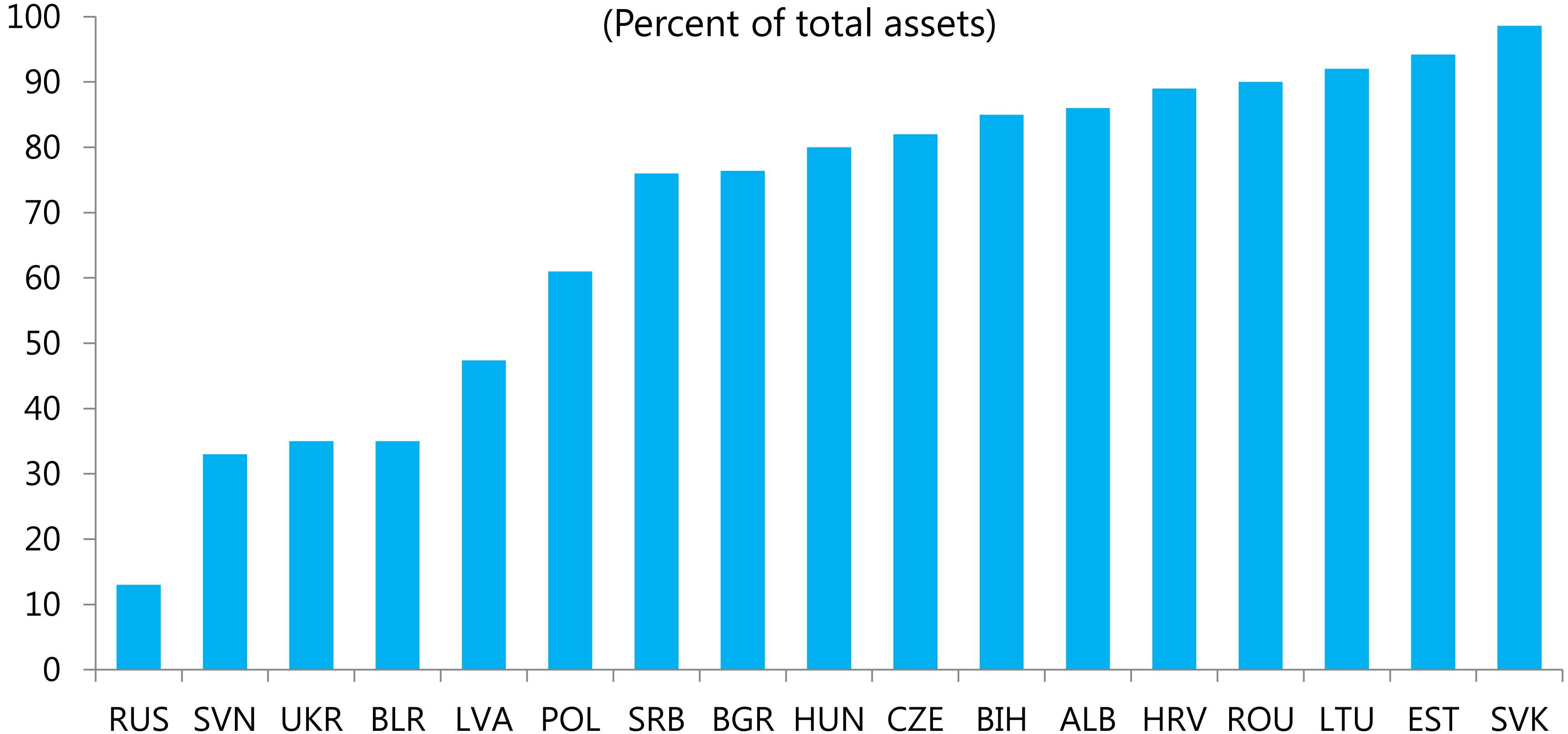
In 1990s **In 2008**



After banking crises in 1990s, banking systems were opened to foreign investors

- Much of the banking system in non-CIS CESEE is foreign owned

Market share of foreign-owned banks, 2015
(Percent of total assets)

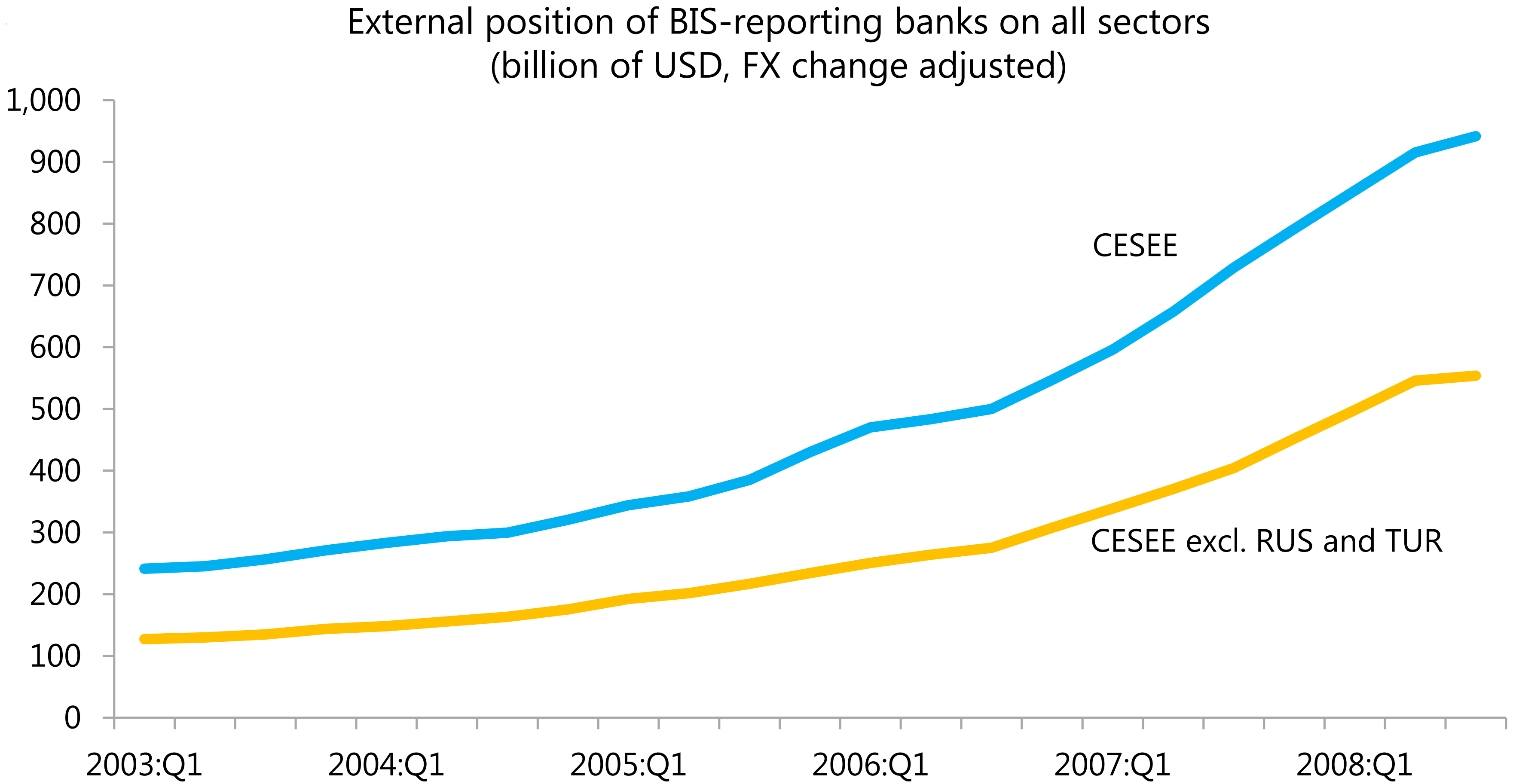


Note: for BLR and LTU data for 2014.

In pre-crisis boom years, CESEE was very profitable…

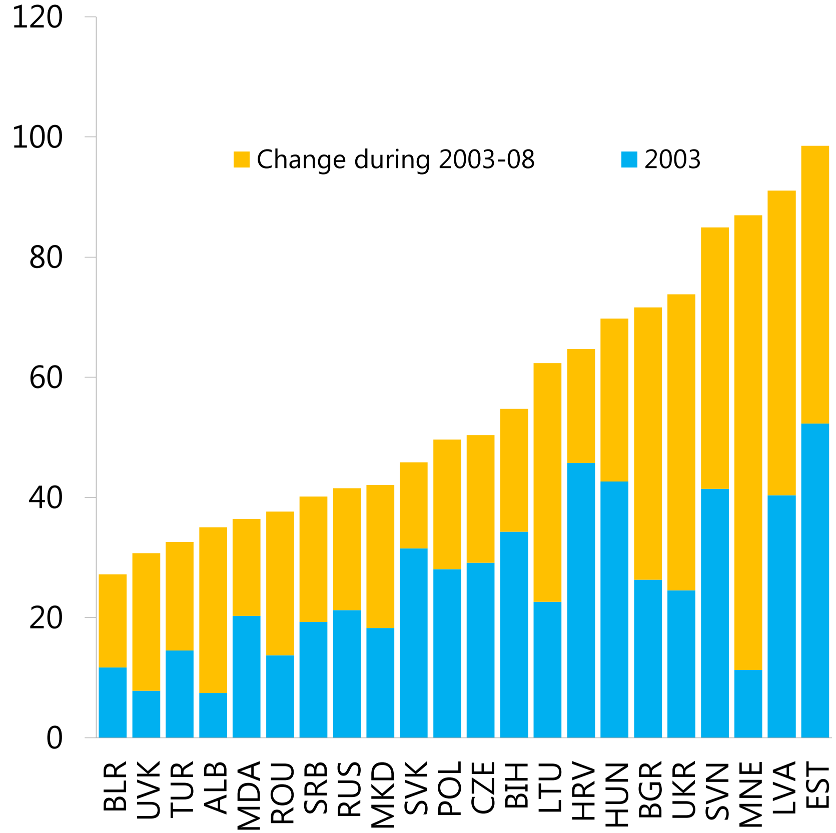
- Credit was growing rapidly
- Interest rate margins were relatively high
- Return on equity and capital was great

Between 2003 and 2008 there were large funding flows of Western European banks to CESEE…

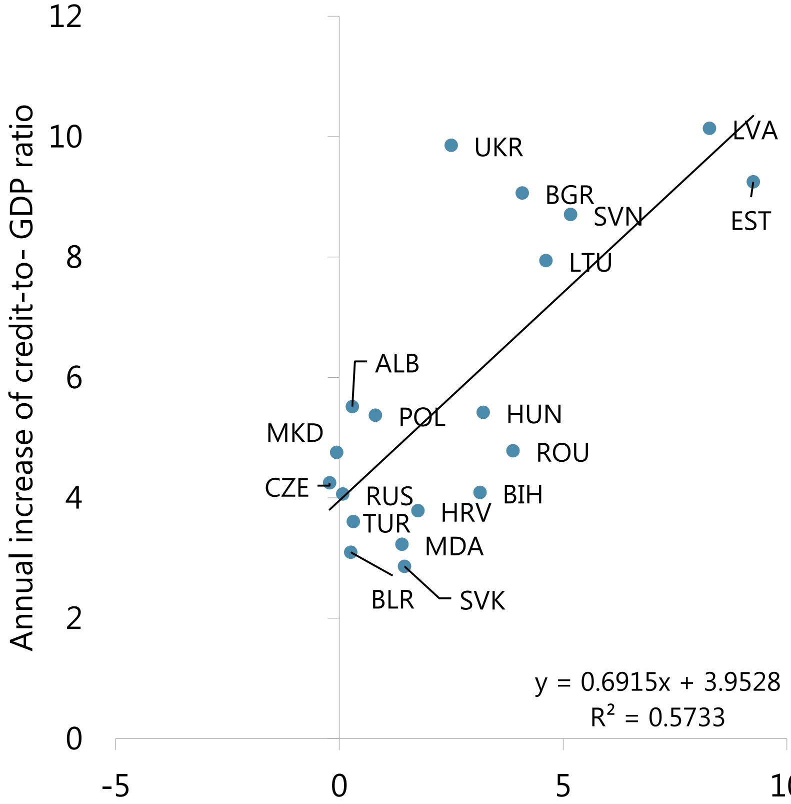


…which fueled and financed a credit boom…

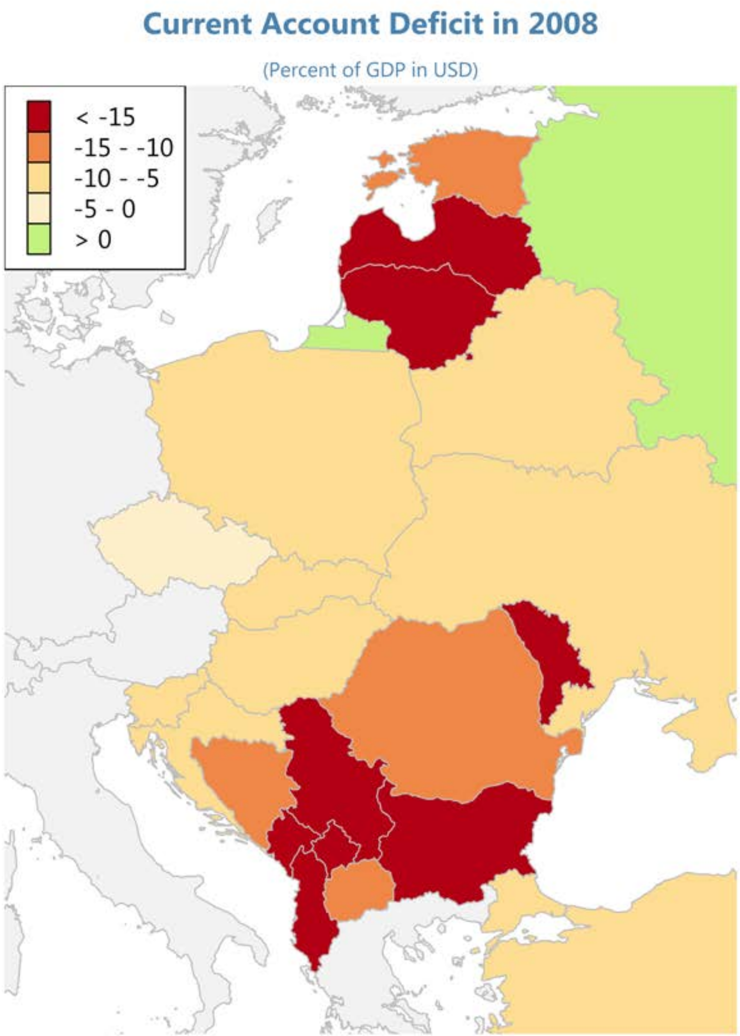
Credit-to-GDP ratio and its change
(Percent of GDP)



Increase of credit-to-GDP ratio and
increase of foreign funding to banks



…which led to high current account deficits and overheating economies



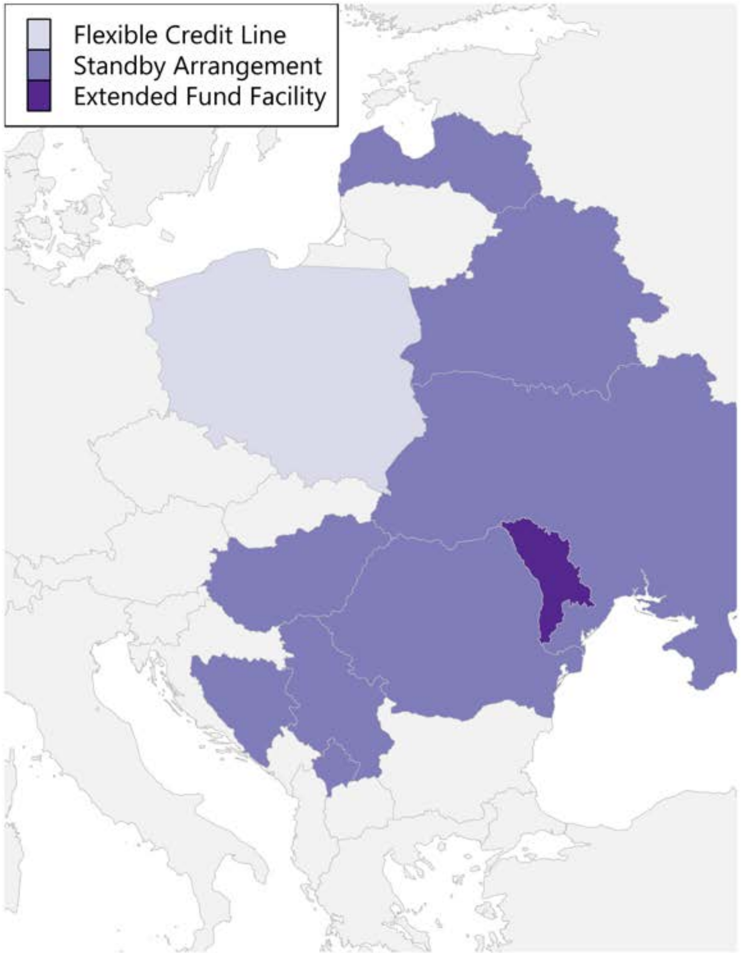
Note: For EST, LVA and LTU: 2007.

After Lehman Brothers this suddenly stopped

- As parent banks got under pressure they could no longer send new funding to CESEE
- Credit booms suddenly stopped
- Domestic demand plunged just as exports dried up as well
- Result was deep recession

IMF provided financial assistance to many countries

IMF programs, 2008-10



Vienna Initiative helped prevent uncoordinated withdrawal of foreign banks

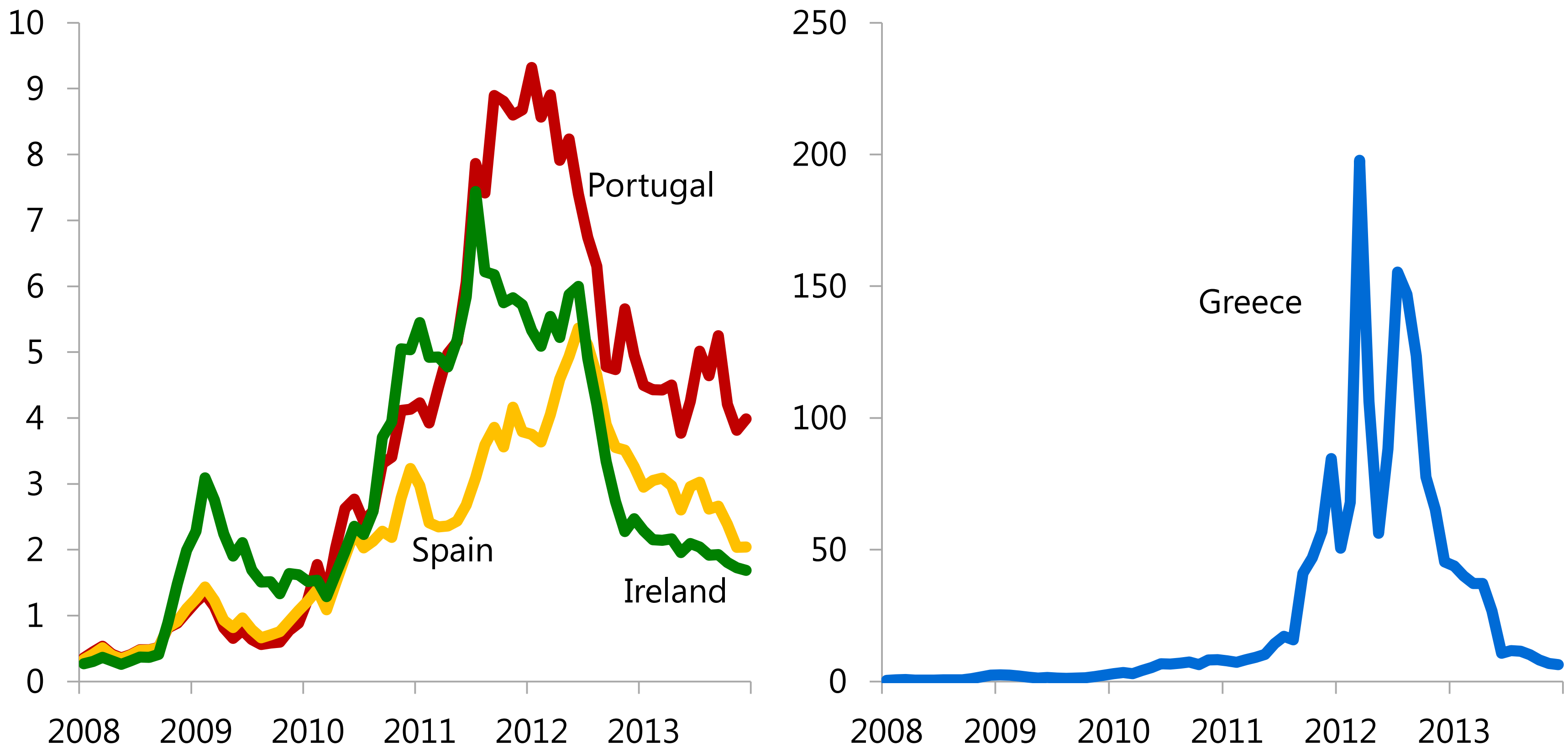
- Launched in January 2009, as a framework for safeguarding the financial stability of emerging Europe at the height of the global economic crisis;
- The main objectives were:
  - Prevent a large-scale and uncoordinated withdrawal of cross-border bank groups from the region;
  - Ensure that parent bank groups maintain their exposures and recapitalise their subsidiaries in emerging Europe
- These objectives were achieved and a potentially region-wide systemic crisis in emerging Europe’s banking sector was avoided.

By 2010, crisis seemed over

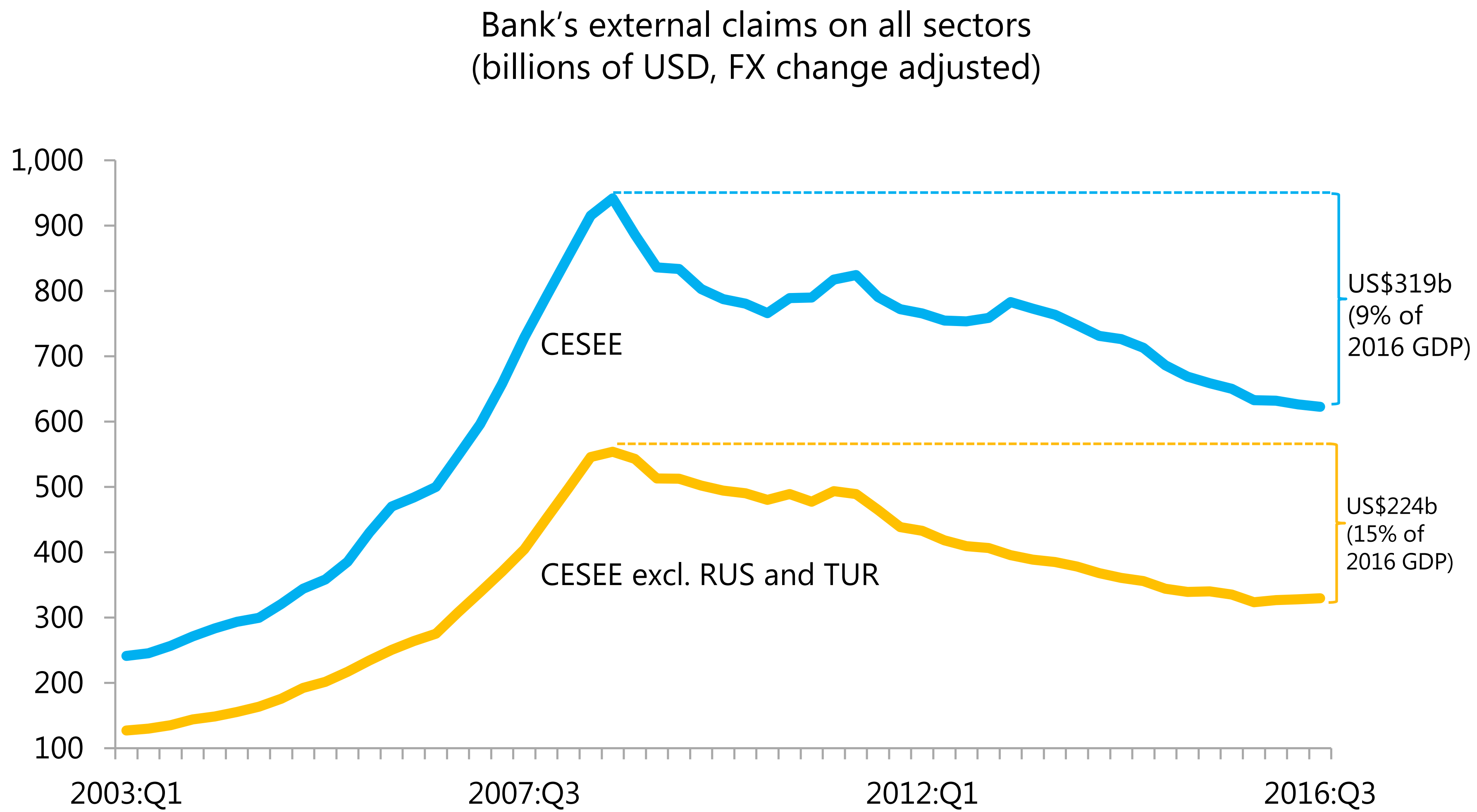
- Risk premia had declined sharply
- Region started growing again
- Bank exposure to region stopped falling

Then euro area crisis broke

10-year Government Bond CDS spreads
(Percent)

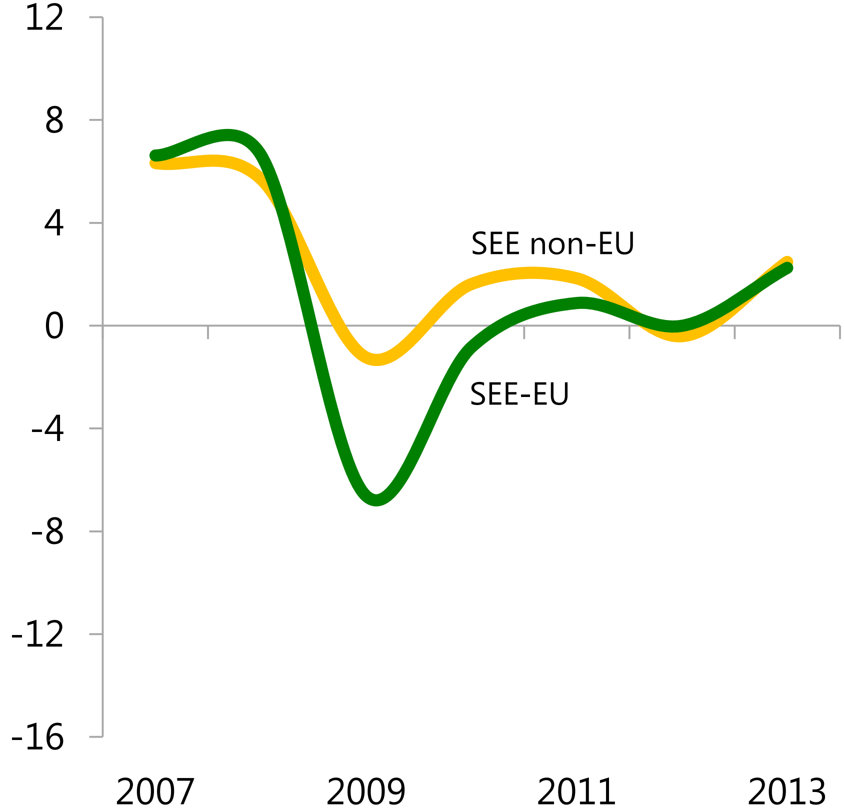


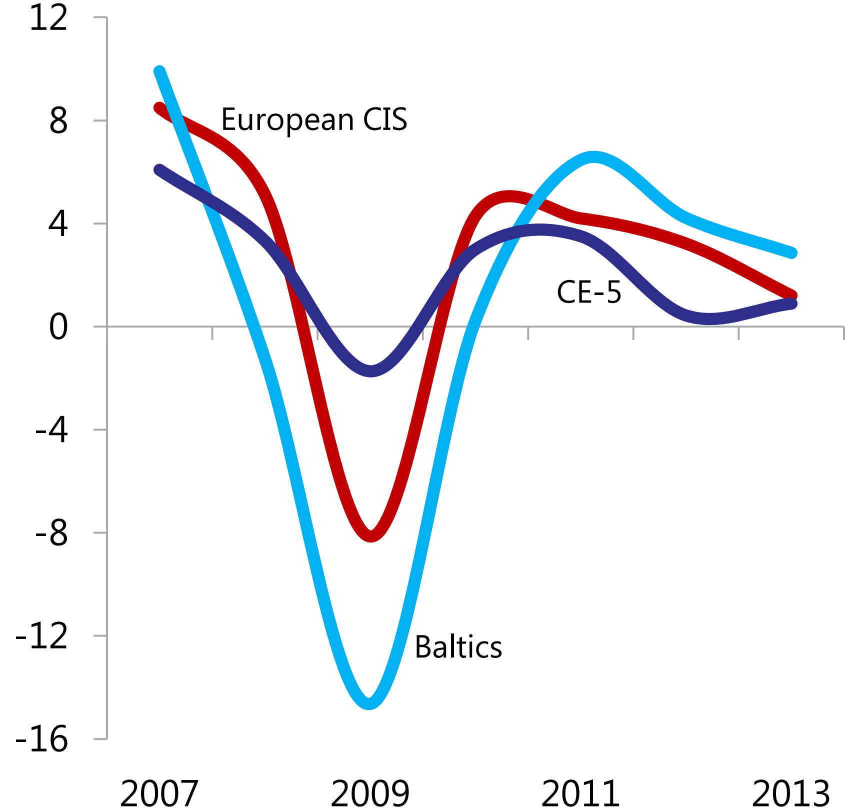
Bank deleveraging resumed



CESEE's economy experienced another downturn

GDP growth
(Percent)



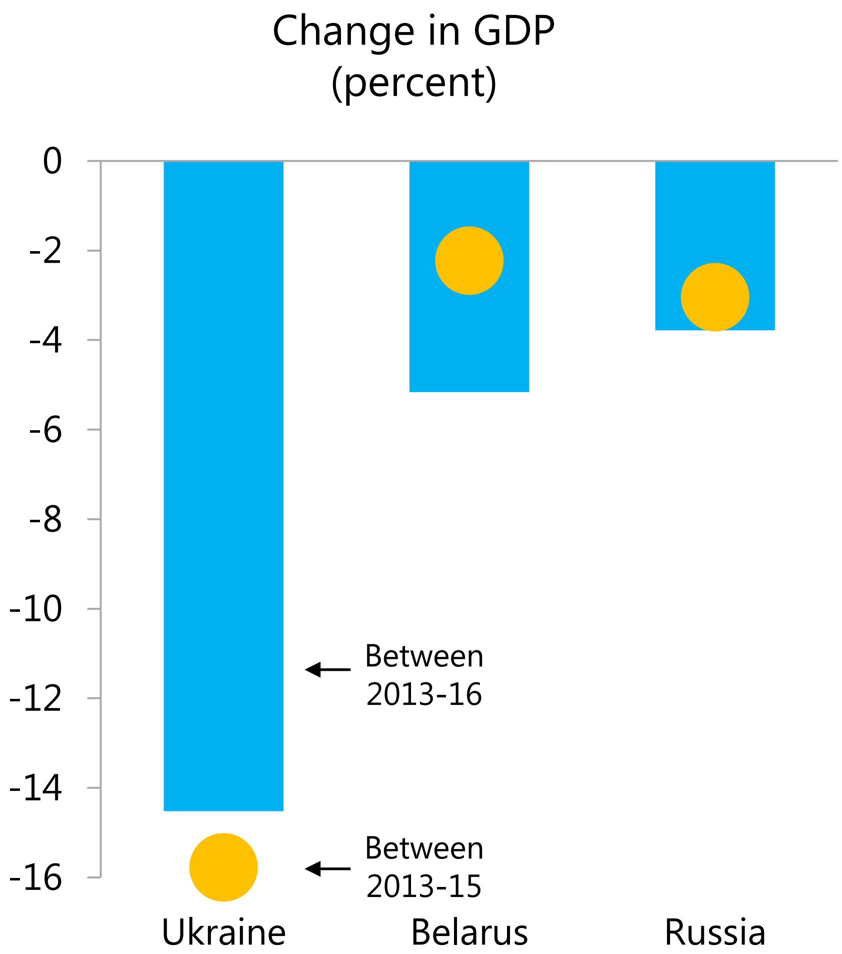


Many SEE countries asked for IMF assistance

SEE countries with IMF program, 2011-16

In 2014-16 CIS was hit by recession

- Collapse of commodity prices
- Sudden stop in capital flows to Russia, result of sanctions on Russia
- Conflict in Ukraine



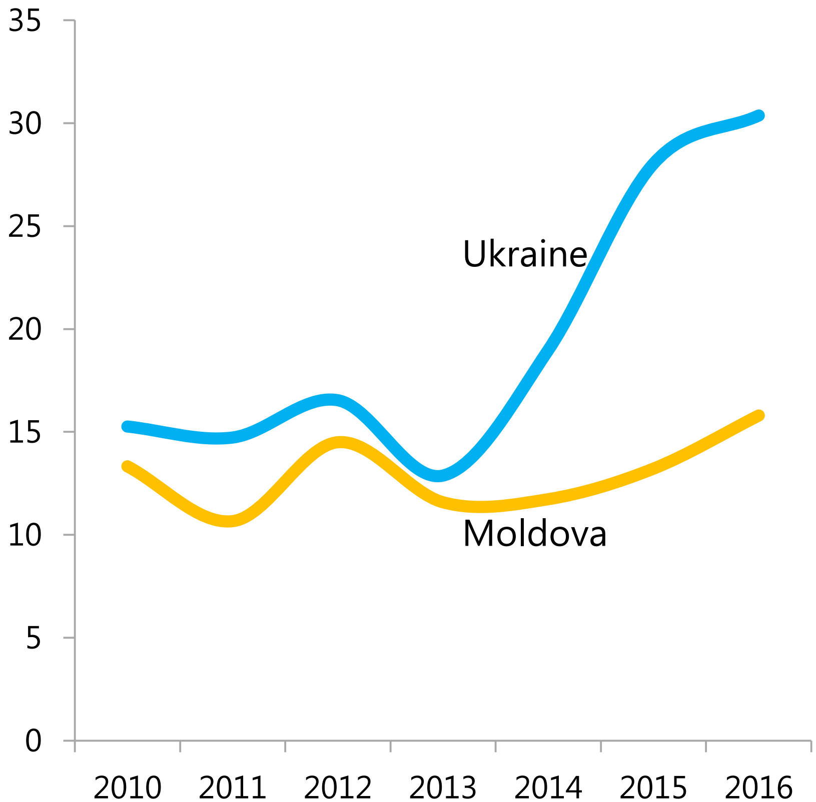
Moldova and Ukraine got help from the IMF

European CIS countries with
Extended Fund/Credit Facility program in 2016

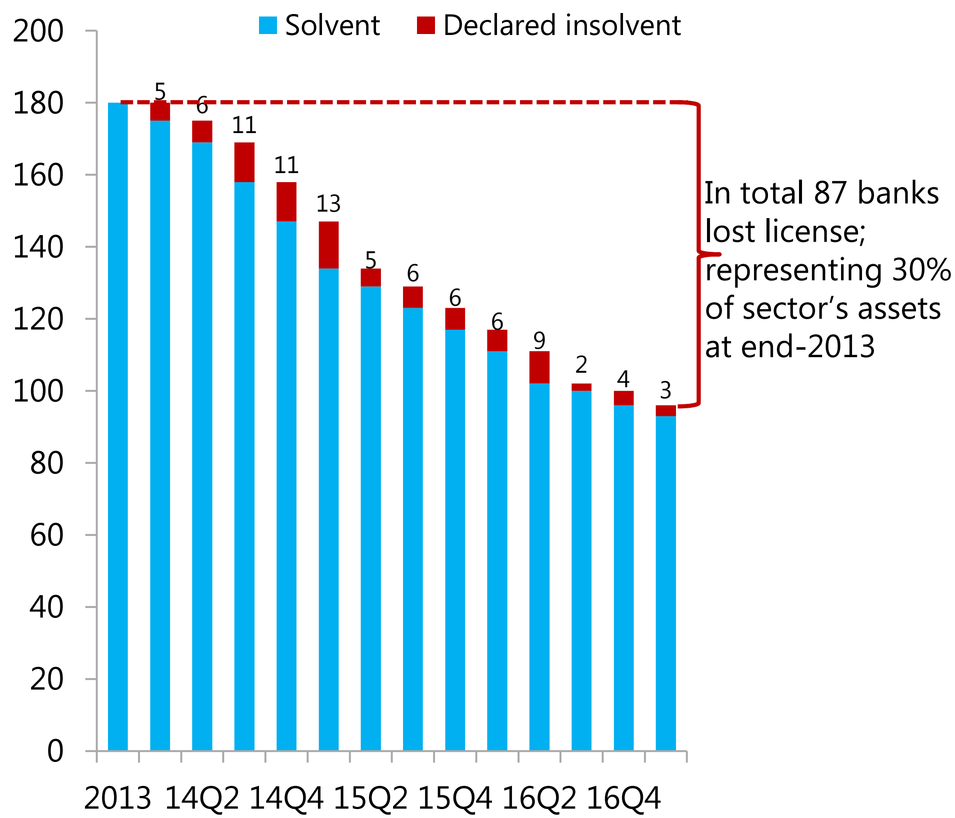
Note: UKR had a Stand-By Arrangement program in 2014-15.

Banking problems played prominent role in programs

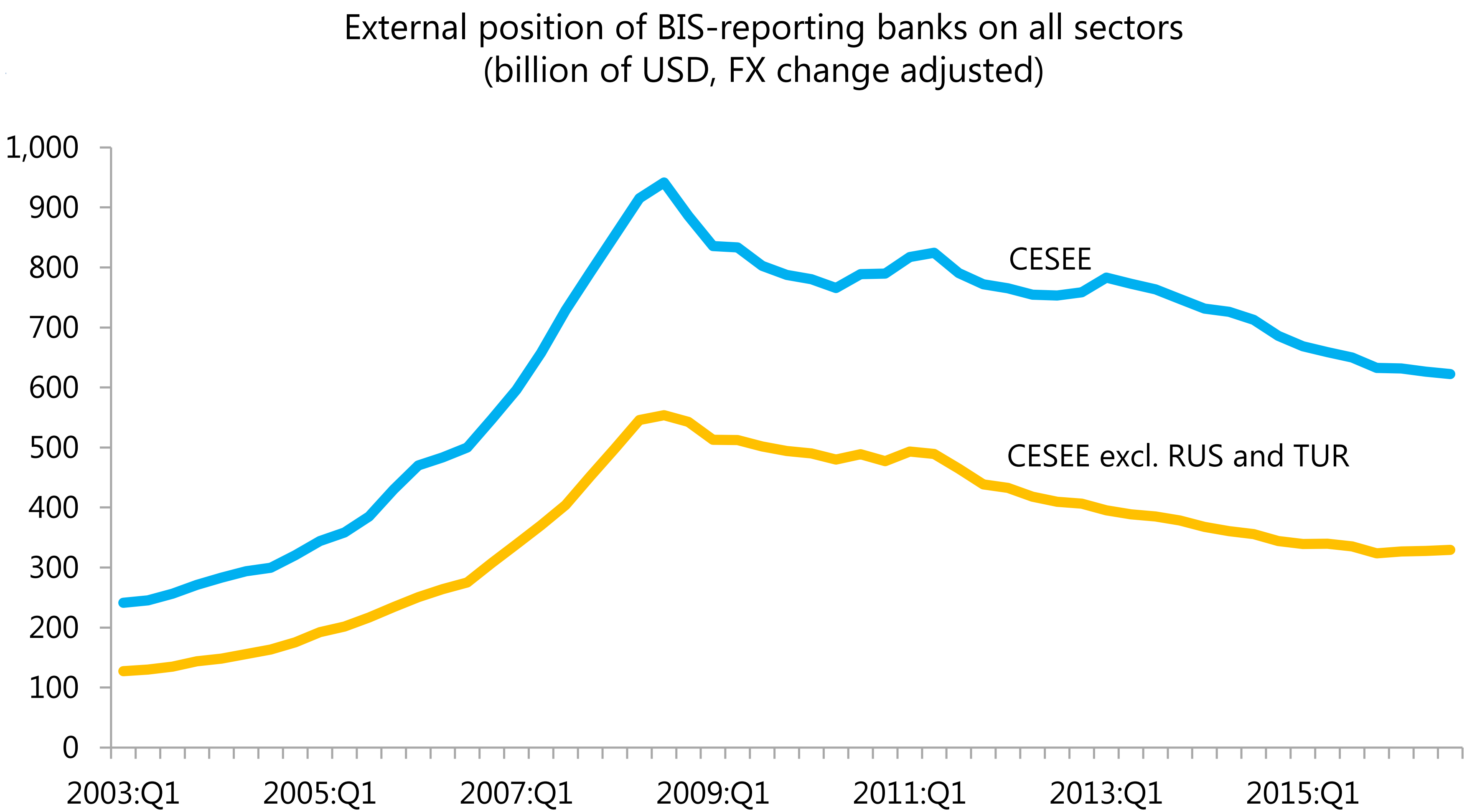
Non-performing loans to total loans (Percent)



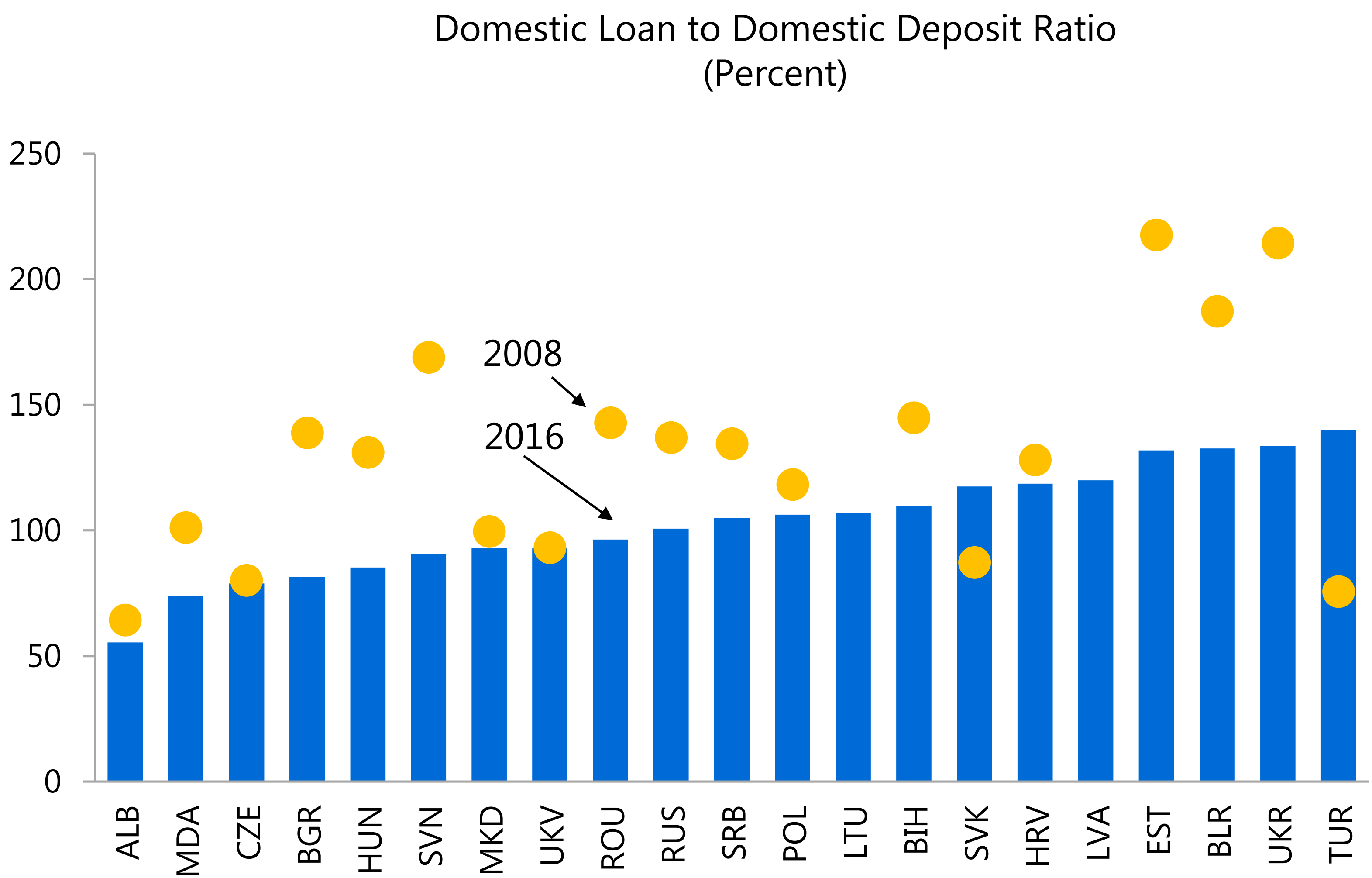
Number of Banks in Ukraine



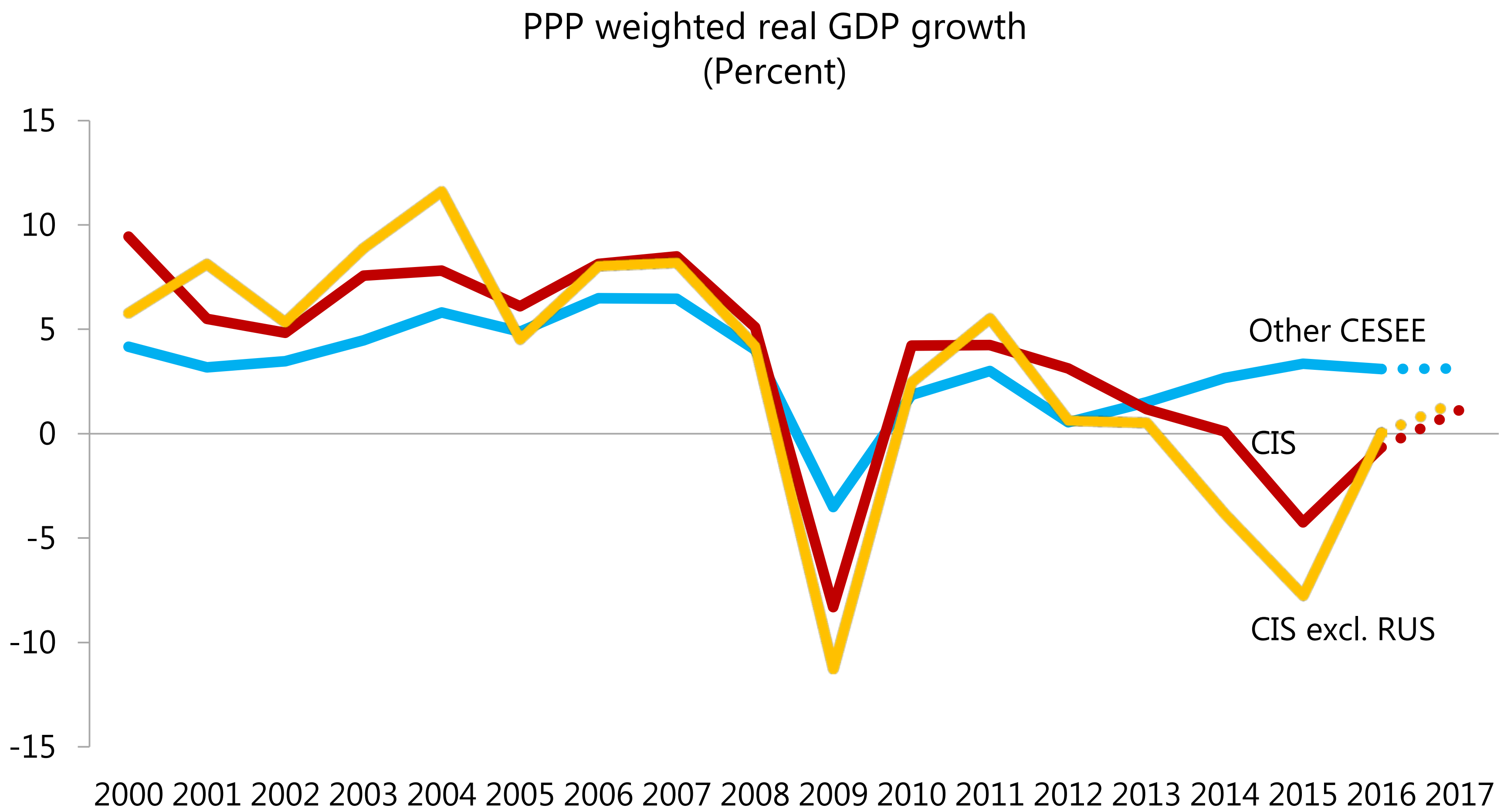
More recently, external position of BIS reporting banks in CESEE excl. Russia and Turkey appears to have stabilized…



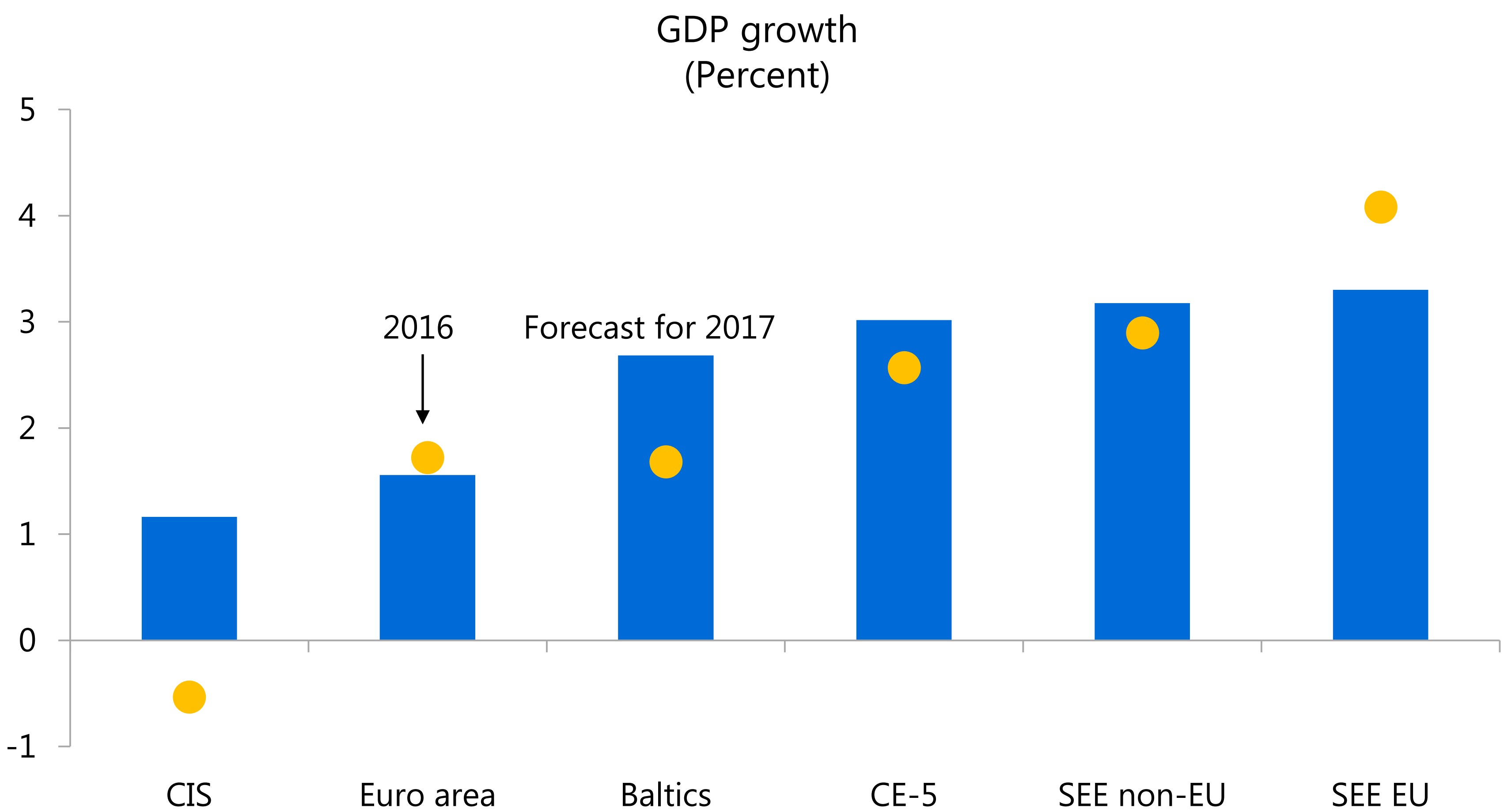
...as loan to deposit ratios in many countries have been reduced to much safer levels



CIS is now recovering; growth in non-CIS CESEE continues to be strong

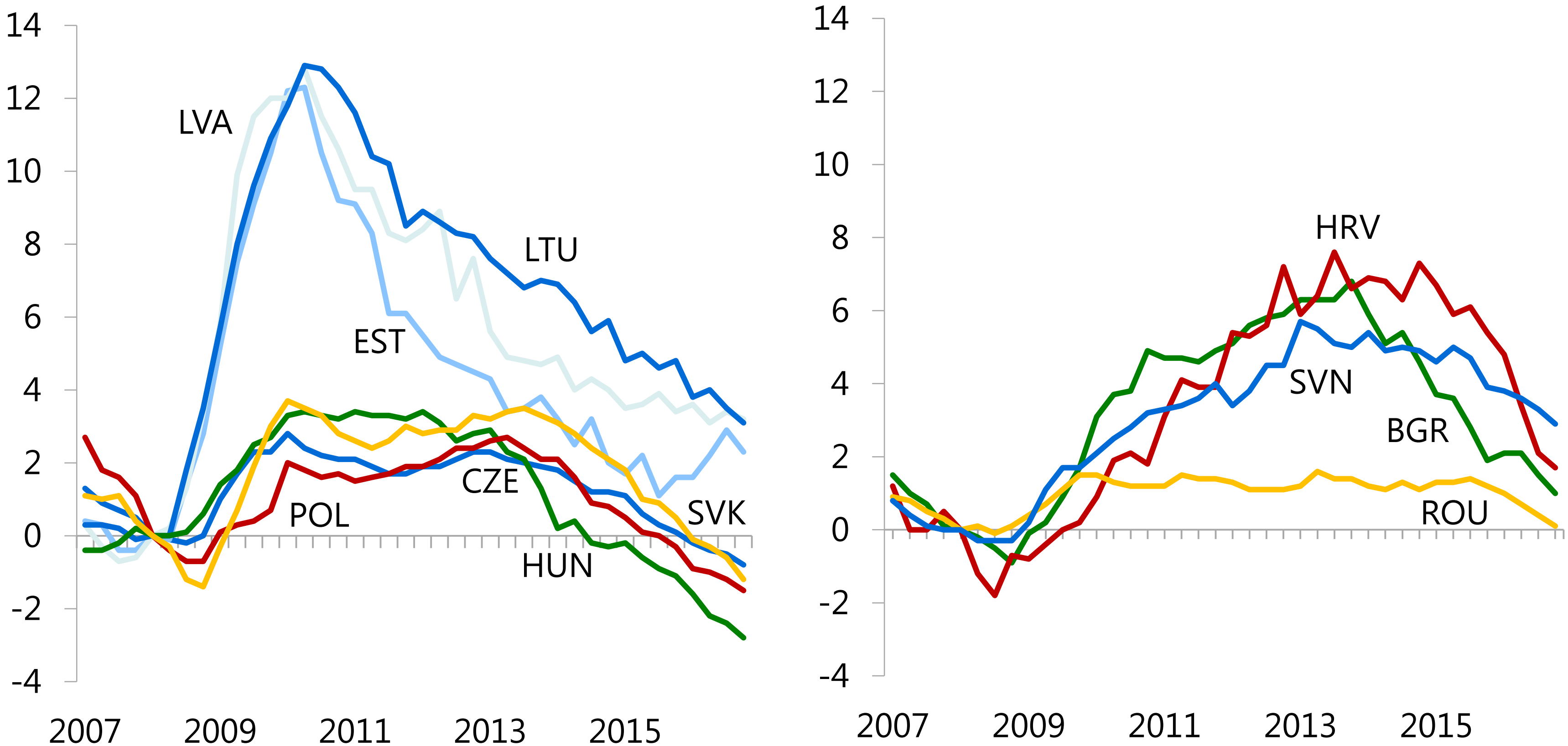


All regions are now showing positive growth



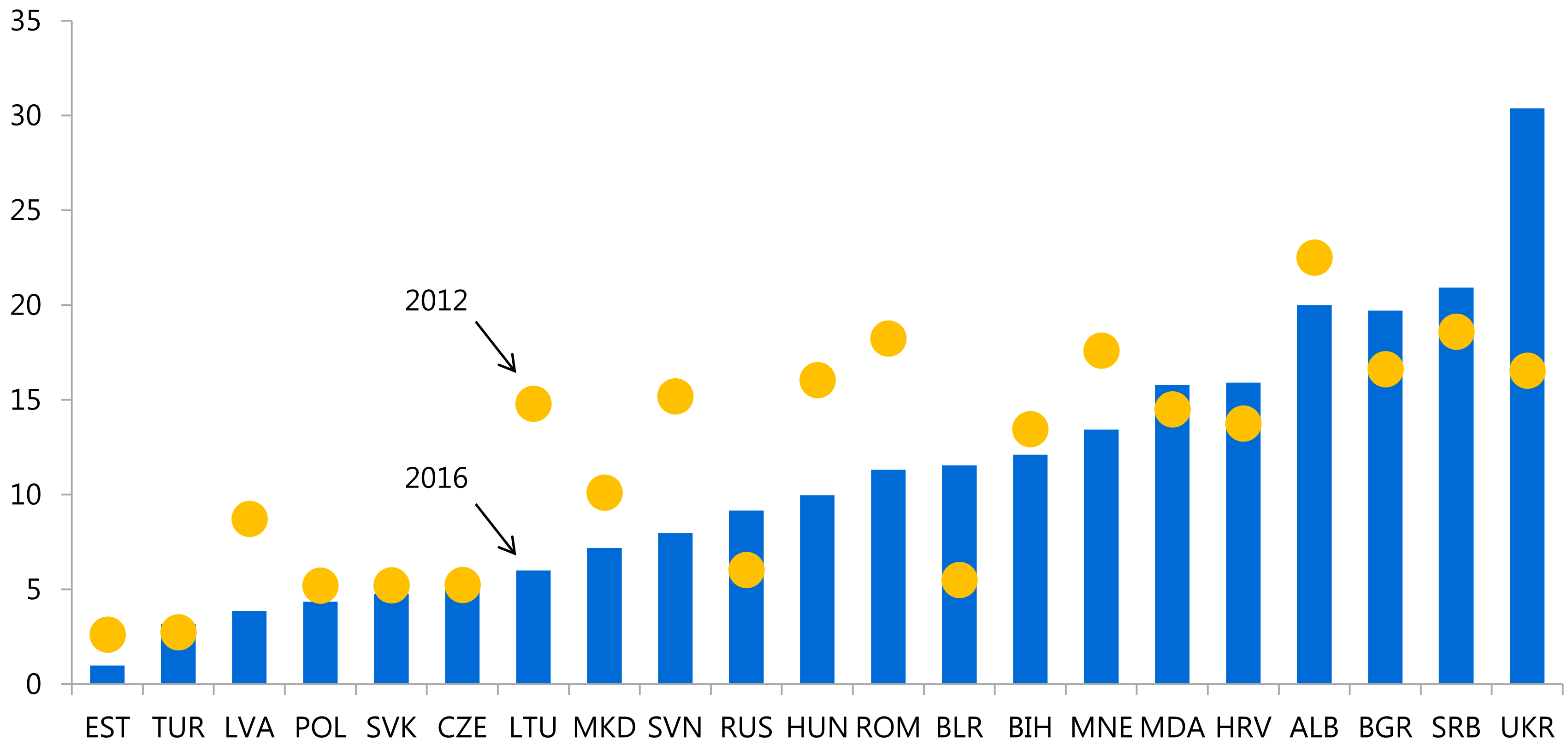
Unemployment in New Member States coming down rapidly

Cumulative changes in unemployment rate
(2008Q1=0, seasonally adjusted)



Crisis legacies remain: high NPLs (especially in SEE and UKR)

Non-performing loans to total loans, end 2016
(Percent)

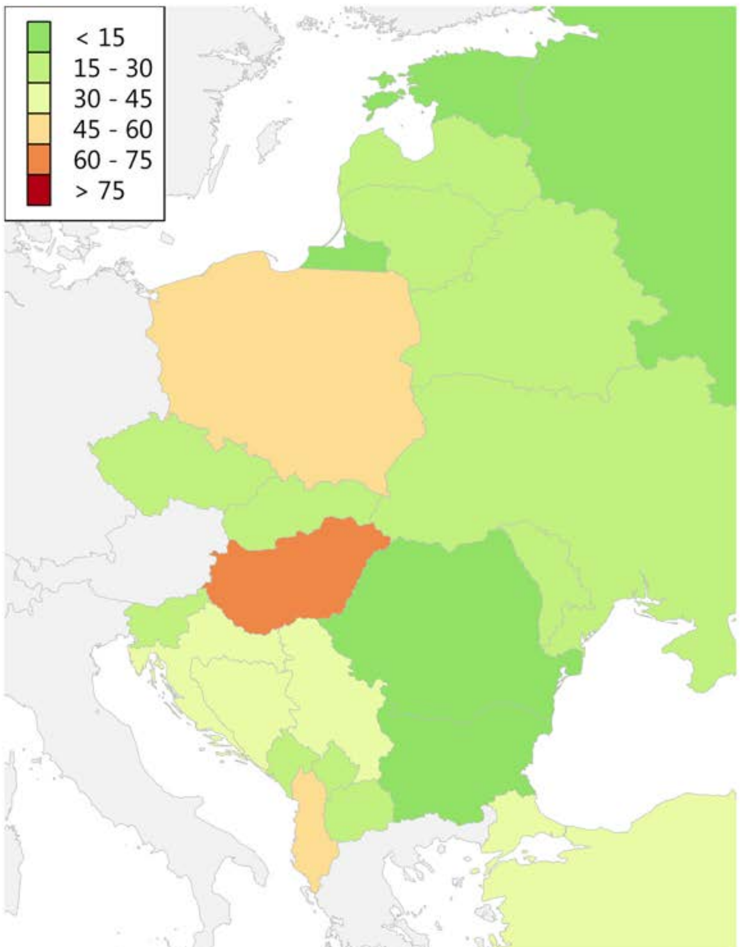


Note: for MNE data for 2012 and 2015.

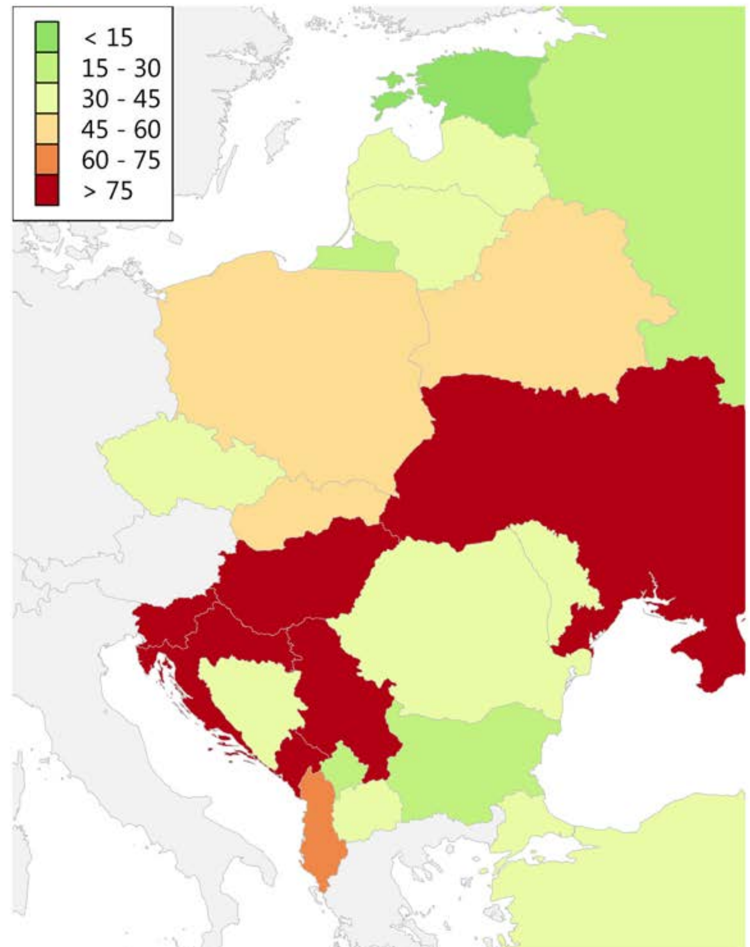
High public debt

Public debt
(Percent of GDP)

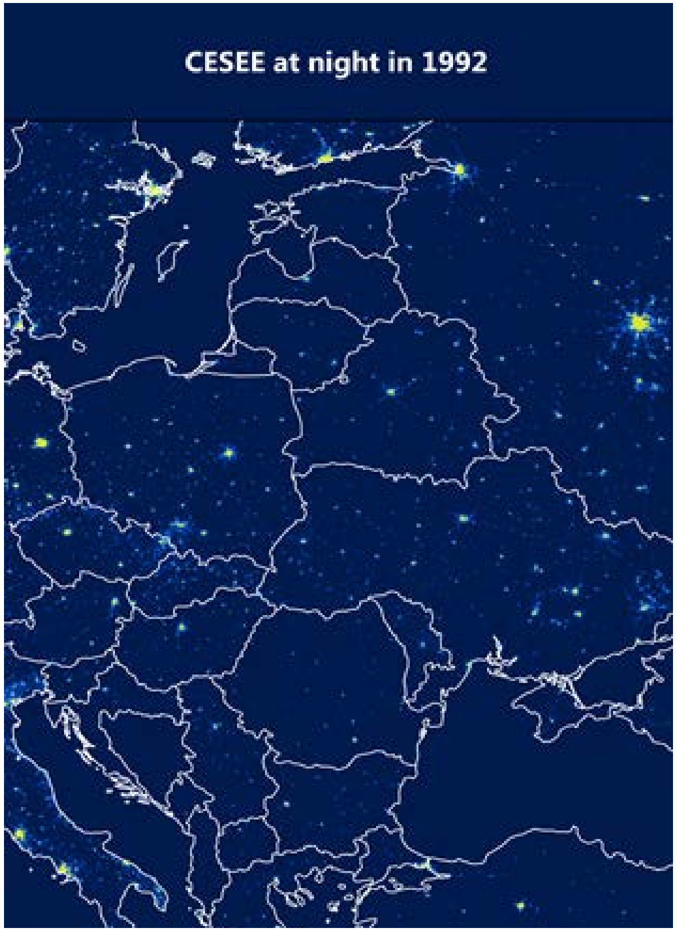
In 2008



In 2016



Since early 1990s CESEE has made tremendous progress



Banking sector has played an important role in this convergence

- But banking sector has also contributed to problems
- Not enough risk aversion during booms; very risk averse during busts
- Foreign funding has exacerbated boom-busts

Thank you