Review of IMF work on the Euro

In 2011, a comprehensive study was prepared by Jean Pisani Ferry,—then head of the Bruegel Institute and now advisor to the President of France—on IMF pre- and mid-Euro Area crisis work. It was prepared as part of the 3-yearly review by the IMF of its overall surveillance.

Below, bolded sentences of that report (which introduce each paragraph) are shown. This provides an "executive summary". The summary distinguishes the pre crisis IMF work from the mid crisis IMF work.

The full paper can be found here.

Note that in regard to the paper's finding that IMF analysis became "sharper" following the onset of crisis, this does not take into account that at the time of writing the report, the IMF was systematically underestimating the size of fiscal multipliers as subsequently reported by M. Blanchard here. As a result, the IMF was also endorsing Euro Area wide tightening of fiscal and monetary policies which has resulted in its more recent concerns that the Euro Area as a whole now faces deflation. Those recent IMF concerns are expressed here.

Summary

IMF surveillance on the Euro Area pre crisis.

IMF surveillance of the euro area suffered from similar problems as IMF surveillance more generally before the crisis.

For several member states of the euro area, the Fund issued strong and pertinent policy recommendations.

However, the focus of surveillance sometimes appears arbitrary and important issues were left untouched. Follow-up to previous policy recommendations was not always ensured. The Fund did not exploit its comparative advantage deriving from international experience with crises-prone countries.

Economic linkages in monetary union were not systematically taken into account. The Fund's surveillance failed to take account of the implications of being in monetary union. Divergences in monetary union were typically interpreted in a narrow way based on a trade view.

The link between capital inflows and systemic risk was ignored. The vulnerability deriving from the link between high debt and competitiveness adjustment was not identified.

FSAPs existed on a national level only and were not designed to be used as a warning tool. Multilateral surveillance provides useful guidance to national surveillance but can spot national problems only in general terms.

Weaknesses in the governance framework of the euro area were not fundamentally criticized.

In the area of financial supervision and resolution, the Fund played a leading role in pushing for progress towards more integration.

Surveillance was process-driven rather than analysis-driven and had difficulties to cope with the set-up of EMU. As a result, national and euro area-wide follow-up to recommendations were not sufficiently integrated. Staff often shied away from confronting national authorities despite support in the Executive Board.

IMF surveillance on the Euro Area mid crisis

Regular surveillance of euro area countries with difficulties became sharper during the crisis years.

Nonetheless, the urgency of problems in Greece was not properly captured in the regular AIV of 2009. The quality of the analysis and policy recommendations increased, but the structure of formal surveillance remained detrimental to an integrated assessment.

As regards monetary policy, the right course for action was debated in the summer of 2008 with the Fund making a positive contribution. As regards the aggregate fiscal policy stance, the IMF advice given to the euro area was appropriate and timely. However the Fund did not differentiate enough its advice on fiscal expansion for the different EA countries, thereby contributing to the build-up of vulnerabilities.

The IMF was the first institution publishing the numbers of potential write-downs in the European banking system thereby raising awareness of the problem. While the overall estimates were too pessimistic, this mistake derived mostly from securities.

The IMF's role in the discussion of the Irish bank guarantees and the following policy response including NAMA is limited.

In general the Fund pushed for more comprehensive and bolder solutions that what the Europeans were willing to accept.

In the discussions of the reform of financial supervision, the IMF was not a major player. In the area of macroeconomic imbalances, Fund involvement in the debate was limited. Overall, the IMF involvement to the governance reform was limited.

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