**Financial Markets and Eastern Europe: If you have a gas leakage in your apartment would you rather wait and see or fix it?**

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1. Introduction

Financial crises had shaken the developing economies in the 1990s and early 2000s. The price was high and having tasted the bitterness of deep recessions, many developing countries tried to avoid dependency on capital inflows, and cut their current account deficits and avoided the appreciation of their currency. Though important exceptions with huge current account deficits exist -Turkey, Central Eastern and South Eastern European countries, South Africa, and to some extent India. As of 2007 turmoil is taking place at the headquarters of the financial markets and the periphery seems to be now a profitable and relatively safer heaven for the financial investors. But how long will that last? For some Central Eastern and South Eastern European countries (particularly the Baltic countries, Turkey, Bulgaria, Romania) the opinion makers in the financial markets seems to be fearing a hard lending scenario, but keep on hoping for a soft lending. The aim of this paper is to analyze the fragility of the Central Eastern and South Eastern European countries (henceforth Eastern Europe) to the turbulences in the global economy and the changes in the direction of the international capital flows. In the early 1990s during the initial phase of transition Eastern Europe faced a severe recession due to both supply and demand shocks as well as major institutional changes. The transition crisis was replaced by a recovery in output starting from the second half of the 1990s in the Visegard

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* This is an updated and extended version of the article “Speculation-led growth and fragility in Turkey: Does EU make a difference or “can it happen again”?”, (in Macroeconomics and Macroeconomic Policies - Alternatives Approaches to European Policies, ed. Hein, E., A. Heise, and Truger, A., Metropolis-Verlag, Marburg, 2006, 199-226) and “International financial markets and fragility in the Eastern Europe: “can it happen” here?”, (in Dollarization, Euroization and Financial Instability, Ed.. Becker, J. and Weissenbacher, R., Metropolis-Verlag, Marburg, 2007, 129-148). The author is grateful to Joachim Becker and Engelbert Stockhammer for fruitful discussions.
Countries and Slovenia and in the late 1990s in the Baltic States and Bulgaria and Romania. The international financial flows, particularly FDI, have played an important role in this period. Nevertheless this process has also resulted in an increase in the current account deficits of quite many countries like Hungary, the Baltic States, Bulgaria, Romania, and Slovakia. The paper assesses the sustainability of these conditions and compares the current state of fragility with former crises in Asia and Latin America. Turkey, being a candidate country as well as a country, which has already experienced the bitter taste of financial crisis twice since 1994, will also be analysed providing an interesting basis of comparison. The paper aims at discussing the fragility in the emerging markets in the Eastern Europe and the possible evolution of the risk perceptions of both the creditors as well as the debtors in this “speculation game” based on the post-Keynesian/Minskyan concepts of endogenous expectations and financial fragility.

Although everyone would agree that the current account deficit can not increase forever, mainstream economists as well as international investors are hoping that increased investment, which could increase productivity, will guarantee a smooth adjustment of the exchange rate and the deficit. An important part of this optimism is due to the positive expectations about foreign direct investment (FDI) and the EU-anchor.

This paper questions this optimism: First EU-wide integration is not a project that aims at overcoming the structural bottlenecks of the Eastern European economies. The domination of neoliberal policies reduces the project of integration to the expansion of markets, and to securing the mobility of capital under stable conditions. Second can an economy, which is ruled by the rationale of profit seeking private capital flows, be stable, or is it the logic of those activities that will create a crisis sooner or later within the normal and even successful functioning of the system? The second part of the title of this paper is inspired by a similar question, which was asked by Minsky (1982) in the context of US, where he discusses the possibility of recurrence of depression. The Minskyan, and more generally the post-Keynesian theory suggest that financial markets are prone to speculation and intrinsically unstable. Stable growth phases will cause more risky investment practices, shaky financial structures, and thus boom periods will be followed by a bust. In that respect EU also does not make a difference, and even the more advanced economies themselves are not immune to crisis. This paper attempts to show that the fact that the Eastern European Countries did manage to live with their current account deficits until today, does not mean that they can do so in the future without facing a major crisis.
The giant global imbalances led by the huge US current account deficit, the possible recession in the US and major global turbulences in the financial markets add further dimensions to our question today. These may affect the emerging economies particularly through the decrease in the risk appetite and increase in the risk perceptions of international investors, and the decline in the private capital flows towards relatively riskier emerging markets. Emerging economies with high current account deficits, high ratios of short-term external debt, large share of foreign denominated or foreign currency-indexed debt, weak domestic banking systems would have particular disadvantages (Goldstein, 2005). Turkey, the Baltic countries, Bulgaria, Romania, and to some extent Hungary and Slovakia unfortunately have either all or parts of these vulnerabilities. Already in 2006 May-June Hungary and Turkey took their share of the global turbulences, and in August 2007 their stability was once again being tested by the financial panic in the global markets following the crisis of the hedge-funds and risky financial instruments. After the Federal Reserve Bank cut its discount rate in August investors eagerly returned back to the emerging markets including Eastern Europe. However if investors become more selective in the future, the vulnerabilities of these economies may lead to costly results.

Another important problem is the impact of an American recession and thus the contraction in export-markets of the emerging economies. So far investors are hoping for the so called “decoupling” of the Asian economies from the US, i.e. that emerging economies are no longer dependent on the US markets for exports. It is true that the sub-prime crisis has not had much impact on Asian growth so far\(^1\). Regarding financial flows a notable case is Turkey, who enjoys notable capital inflows, which in turn lead to a very strong Turkish Lira against the Euro despite its high current account deficit and inflation rates well above the

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\(^1\) The Economist (2007a:76) reports that “emerging economies’ exports to America slowed markedly this year, but their GDP growth has been supported by robust domestic demand and strong exports elsewhere….America is less important as an importer than it used to be. The share of China’s exports going to America (including re-exports through Hong Kong) has fallen from 34% in 1999 to 24% now. China exports more to other emerging economies, which as a group now send more to China than America…. This partly explains why as American imports have slowed this year, the emerging world has continued to boom. So long as China’s economy remains robust, it will help to pull other emerging economies along.”
euro zone in the last five years. But we have not yet observed the effects of a full-blown American recession.

So far the developments may look like the problem does not exist any more, however it may also be that the problem is just postponed given the more significant issues in the headquarters of finance. However when and if the problems deepen, it would be naive to hope that the emerging markets with high current account deficits would completely be decoupled. The important question for us is not “when will a crisis happen?”, rather “can it happen again and here in Eastern Europe?” and the answer of this article is “yes, it can happen here”. A common feature of bubbles, “such as America’s dotcom mania and more recently its housing boom, is that most people refuse to believe they are bubbles until they burst” (The Economist, 2007a:76). It suffices to say that the Wall Street Journal (Lahart, 2007) during the peak days of the rediscovery of the fragility in the global markets, wrote that Minsky’s views have become suddenly very popular, because his work indeed predicts the systemic crisis.

The rest of the paper is organized as follows. Section two discusses the leading indicators of fragility in Eastern Europe. Section three presents the effects of global turbulences up till now. Section four derives the conclusions.

2. “Can it happen” in Eastern Europe?

In this section we compare the values of some commonly accepted, major leading indicators of fragility and crisis\(^2\) for the Eastern Europe as of 2006 and 2007 with the values of the same indicators in ten Asian and Latin American countries before their crisis year (Turkey in 1993 and 2000, Mexico in 1994, Indonesia, Thailand, and Korea in 1996, Malaysia and the Philippines in 1997, Brazil in 1998, Argentina in 2000). The indicators that are discussed below are current account deficit as a ratio to GDP as well as international foreign exchange reserves, short term foreign debt as a ratio to total debt and international foreign exchange reserves, and appreciation rate of domestic currency. The comparison shows at times how close some Eastern European countries are to the ‘red zone’, but they also show that agents’ evaluation of risks do not follow a pre-determined rule of thumb.

Figure 1 shows the current account deficit as a ratio to GDP in the Eastern European Countries. The values of the current account deficit/GDP ratio before the crisis in ten other cases of crisis in Asian and

\(^2\) See Goldstein (2005) and Goldstein et al. (2000).
Latin American countries are also shown in the graph on the left hand side. With their current account deficits the Eastern European countries are the exceptions among the emerging economies, along with South Africa\(^3\). Estonia, Latvia, Lithuania, Bulgaria, and Romania have record high deficit ratios. Although all of these ratios are beyond what can be perceived as sustainable, the case of Latvia is a record among the records with a ratio of 23.8%. The hard peg in these countries (except for Romania) resulted in high current account deficits (Becker, 2007). Croatia is also among the rather high deficit countries. Hungary had until 2007 a high deficit (6.9% in 2005 and 5.8% in 2006), which is estimated to come down to 4.9% in 2007\(^4\). Although the decline is certainly perceived as a good signal for the markets, the ratio is nevertheless still high. Slovakia had also suffered from increasing current account deficit up to 8.3% in 2006, and a fall down to 3.8% is estimated. Nevertheless these are still high numbers, if countries get exposed to contagion effects from previous crisis. Finally Turkey has been experiencing high deficits since 2004, and with ratios approaching 8% in the last two years. Indeed this deficit ratio is much higher than the same ratios in Turkey before the crises of both 1994 (3.6% in 1993) and 2001 (4.9% in 2000).

While the ratio of the current account deficit to GDP compares the deficit with the size of the economy, the ratio of the current account deficit to foreign exchange reserves of the Central Bank (see Figure 2) gives an idea about the ability of the country to finance capital outflow in case of a reversal in the direction of the international flows. According to this ratio the picture looks a little better, but not fundamentally different for the Baltic countries, Bulgaria, and Romania. Estonia and Latvia have the highest rates, going beyond any historical record.

In terms of the foreign debt related risk indicators, the turn-over risk, i.e. the ratio of short term foreign debt in total foreign debt, which can be seen in Figure 3, is highest in Slovakia followed by Latvia and the other Baltic States, Bulgaria, Romania. Even the Czech Republic is playing in this risky league according to the turn-over risk. All these ratios are well above the nine former cases of crises and close to the highest ratio that Thailand had experienced before the crisis. The prospects are not much

\(^3\) South Africa is expected to have a current account deficit/GDP ratio of 6.2% in 2007 (www.economist.com/indicators). Mexico and India are expected to have minor deficits (1.0% and 1.4% respectively).

\(^4\) UniCredit Group New Europe Research Network, 2007 estimations.

The estimation of the Economist (www.economist.com/indicators) is 5.8%.
better in the case of the ratio of short-term foreign debt to foreign exchange reserves\(^5\) (see Figure 4); the ratio is rather high in the Baltic States and Slovakia. Bulgaria comes next, approaching the `red zone' of 100% (89.5%). Moreover it is also important, which agents in the economy are indebted. In these highly euroized economies of the East, private firms and households are expected to receive significant negative shocks in case of a sharp depreciation (Becker, 2007) with important spill-over effects to demand and production.

Finally the currencies of the Eastern European countries have been appreciating quite significantly in real terms for more than a decade together with inflation rates higher than the advanced countries and capital flows or pegs keeping nominal exchange rates low\(^6\). The Baltic States and Bulgaria have a currency board, thus their national currency is pegged to Euro and the emission of national currency is made dependent on currency reserves (Becker, 2007). The other countries have a managed float, but this also does not prevent appreciation. An overvalued currency increases the expectations for a correction, since the sustainability of the current account deficit becomes more and more suspicious. Goldstein et al. (2000) argue that real exchange rate overvaluation is one of the best performing leading indicators of a crisis. In spite of the depreciation during 2006 May-June turbulences in some countries like Turkey, the appreciation continued once again due to capital inflows in 2007, and the August depreciation was short lived, though volatility increased afterwards.

The relevant question is whether the risk indicators are above the critical values that would be an invitation to crisis. In 2001 Dornbusch (2001, cited in Uygur 2001) had argued that the red region of crisis begins with 4% current account deficit/GDP ratio. However we know that the critical rates can differ significantly depending on the conditions: for example 4.4% of real appreciation had been enough in the Korean case under the contagion effect.

In the case of Eastern Europe conventional wisdom in the market about what is risky seems to have changed. One important basis for the re-evaluation of the rule of thumbs is due to the contribution of imputed foreign profits to the current account deficit. As the foreign investors make profits, this is imputed as debit in the current account of the Eastern

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\(^5\) This indicates the hardship of the country to finance its short-term debt with its reserves.

\(^6\) Slovenia has already adopted the Euro at the beginning of 2007, therefore it is not included in this analysis.
European countries. Therefore Brada and Tomsik (2003) argue that the old rule of thumb of 5% current account deficit as a ratio to GDP being risky is not valid in this case. Although the argument makes sense, and markets indeed have apparently valued that fact, the question is then how high a current account deficit will be alarming? Regarding the appreciation of the currency a similar optimism about redefining more tolerant critical values also apply. Here the argument is that in emerging markets, in particular the transition economies the appreciation of the currency is a natural catching up phenomenon (Balassa-Samuelson effect). However, would the markets care much if a couple of unlucky events (like the global financial troubles) and a few of the not so favourable ratios coincide at a certain point in time?

Another important reason about the tolerance of the markets is the FDI optimism, which is forming an important part of capital inflows in these countries (Mencinger, 2007), and thereby financing the current account though the so-called safe means. In the case of Turkey this is also a point in which the FDI optimists expect that EU could make a positive impact on the dependency of Turkey on short-term capital flows until recently. Turkey has been attracting significant amount of FDI inflows particularly since 2006. The EU anchor, which guarantees the stability of the political regime, property rights, and the markets, is expected to keep FDI going. However, FDI inflow can also be interrupted when the country faces a severe crisis, or firms can even relocate. Moreover, other long-term problems in the absence of a systematic industrial policy remain to be valid, such as increased import dependency, which may generate further current account deficits. Mencinger (2003) reports that multinational enterprises contributed more to imports than to exports, and the spillovers from single firms to the sector does not seem to be relevant, which leads to a dual economy with significant productivity differentials. Another issue regarding the effects of FDI is the repatriated profits. After a certain phase, foreign investors start harvesting the fruits of their investments and transfer their profits back home, which may make the financing of the current account more problematic. The opportunities of the multinationals to invest in developing countries with even cheaper labor may further deter reinvesting profits in the initial affiliate (Mencinger, 2007).
In addition to FDI optimism, till now an important mechanism behind the changing perceptions of risk is the EU anchor. EU is a guarantee that the country will stick to liberal policies, fiscal discipline, and will avoid capital controls, which all secure the mobility of capital flight as well as the funds to finance debt payments. But ironically this anchor based on the integration to the EU economic zone creates another source of fragility. First more optimism and capital inflow leads to risky debt behaviour as well as the appreciation of the currency. Second these countries try to avoid depreciation because of preparing for the entry to the monetary union. But given the productivity and inflation differentials, this process invites real appreciation. Until now the Baltic countries had seen the Euro as an exit strategy (Becker, 2007), but since their entry to the Monetary union is delayed to a date after 2011/2012, they may face the market pressures to oblige a more bitter exit like Argentina had to do. However even if they achieve what they were hoping for, i.e. adopt the Euro without a major accident on the way, this time they will nevertheless experience the adverse effects of being an insider with huge productivity differentials with respect to the core countries. This has been the story of other peripheral countries like Spain, Greece, Portugal, and even Italy.

The Economist (2007b:29) resembles the situation of the ten East European member states of the EU to inexperienced drivers on a “smooth road in fine weather” and warns: “if the road gets slippery, bad brakes and bald tyres make a crash, even a pile-up horribly likely.” Latvia’s situation attracts particular attention. If Latvia has to abandon the hard peg the likeliest route for contagion will be Estonia, says the Economist (2007b:29) and adds to its list: “The other early candidate for a crash has long been Hungary.” Naturally Turkey has always been a part of this list of fragile countries (Onaran, 2007, the Economist, 2007a:75). These turbulent days seem to have converted the Economist (2007a:76) also to a Minskyan economist: “Vast capital flows can harm the economies in several ways. Not only can they inflate asset bubbles and spur excessive borrowing, but they can also cause a steep rise in the exchange rate, damaging the competitiveness of export sectors. If a country already has a current account deficit this will make it even more vulnerable to a quick reversal of capital. On the other hand if central banks intervene to hold down their currencies, the build up of reserves can lead to excessively

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In the case of Turkey the anchor is the accession process and FDI inflows, although membership is a far future prospect full of uncertainties.
loose monetary conditions and rising inflation. This is exactly what is happening in much of emerging Europe.”

To sum up until very recently the investors’ risk appetite had seemed not to be disturbed only marginally by these ratios. But the question is for how long? The answer depends on recent history, and how recently and how badly investors were punished by volatility in the returns, and how long the recent boom has been continuing (Grabel 1995). A dealer cannot afford to be conservative for a long time, since no one can be sure when the accumulated fragility will lead to a crisis. He/she has to follow the conventional wisdom and try to invest the funds as profitable as the other dealers, if he/she wants to keep his/her job. However shocks that are not necessarily intrinsic to these economies may play an unpleasant role. Thus the developments depend a lot on how the issue of the US current account deficit and the fragilities regarding the hedge funds will be solved. Below we will discuss this issue in more detail.

3. Global financial turmoil and implications for the emerging markets

In the global financial markets all these problems were seen much less relevant until May-June 2006, when the optimism in the East and elsewhere in the emerging markets was affected by the global turbulences in the world economy. This was a response to the rise in the interest rates in the US, and resulted in a massive flee of international investors out of the emerging markets. At the time the flight of international financial investors out of the emerging markets was explained mostly by the fear that rising interest rates and the slowdown in the US economy might ultimately upset the delicate harmony of the global economy8. Turkey, Hungary along with Brazil and South Africa were among the emerging markets, which were hit most severely. Poland and Slovakia were also affected slightly.

The May-June 2006 turbulences were short-lived and the investors soon started to enjoy the low asset prices even in the riskiest markets like Turkey after the initial panic. Aggressive risky investment behaviour looked for reasons to explain why the mechanism will not break down; the coercive competitive pressures led the conventional wisdom to shift again towards buoyancy (Onaran, 2007). Indeed it was defined as “a bit of profit-taking” and “a drama not a crisis” by The Economist (2006: 74). A kind of a consensus emerged that there is only real reason to worry if one believes that the world is going into a global recession and at that time this was a possibility that the market professionals have to rule out in order not to shift to overly conservative investment practices too early.

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8 See Onaran (2007) for a review of the business press at the time.
in time. Because that would then make them deliver lower profits to their customers compared to their competitor dealers, who have a higher risk appetite (Onaran, 2007).

However, soon other dark sides of the global financial markets emerged. In the past years “the absence of severe recessions or abrupt shifts in monetary policy had made investors more confident, and thus more willing to borrow” says the Economist (The Economist, 2007c: 59), almost reminding us of Minsky. This process brought together the invention of new risky financial instruments. Banks could bundle together risky assets with changing degrees of risk levels. That sounded good in theory. In the meantime hedge funds have relied on cheap credit to fund their risky investment across the globe as well as the huge takeovers and leveraged buyouts. Then in 2007 February the bad news from the US, in particular the subprime mortgage markets (loans to people without income and job assets) shook the markets for assets backed by these loans, but then the markets stopped worrying again (Dillow, 2007). On July 10 the chief executive of Citigroup had said: “when the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you’ve got to get up and dance” (in Elliott, 2007). Two weeks later the music stopped —apparently sooner than what Citigroup expected. As the defaults in the subprime markets (loans to people without income and job assets) have been much higher than expected, and as the riskiest mortgage backed securities’ prices have fallen, some hedge funds experienced serious problems of liquidity. Indeed the market for such securities had become suddenly very illiquid (The Economist, 2007c: 59). The markets started to realize that the global economy is in a credit crunch territory, where banks either reduce the amount they are willing to lend or make that lending so expensive that it deters borrowing (Elliott, 2007). But this will be big problem for some hedge funds. Furthermore banks themselves have vulnerabilities (The Economist, 2007d: 60): “Wall Streets five big investment banks have piled potentially illiquid risky assets…. Several European Banks and insurers are rumoured to be sitting on mortgage bombs-troubled assets linked to America’s subprime mess”. The Banks’ link to the hedge funds within their own group to which they may also have to supply rescue capital is a second source of vulnerability. As the risks of a credit crunch grew, the Central Banks have injected massive amounts of liquidity to the markets after July 26, but this did not calm down the financial investors; instead they thought “the ECB is bailing out banks –things must have been even worse than we knew” (Dillow, 2007).

There was a shake in emerging markets in July-August 2007, but after the Federal Reserve Bank’s interest cut investors returned back, since the
peripheral countries not only were profitable but also looked like not directly affected by the sub-prime mess. According to the IMF, net inflows of private capital to emerging economies have increased to almost 4% of their GDP on average in 2007, going beyond the peak of the previous wave in the first half of the 1990s (The Economist, 2007a:76). Net inflows to emerging Europe are even higher. The Economist (2007a:76) claims that in the emerging markets “bubbles will get bigger before they burst.”

The further implications of the global credit squeeze for Eastern Europe are however yet to be seen. The process brought a re-pricing of risk, increasing credit spreads, depreciation in some of the currencies and a fall in share prices in most countries, but the impact has been lower than the one recorded in May–June 2006 and February–March 2007, and lower than that recorded in some more developed financial markets like Japan; furthermore, by mid-September most of the losses in both equity and currency markets had been already reversed (UniCredit Group New Europe Research Network, 2007a). As there are no safer heavens to go now, some Eastern European countries may remain stable. However some others may not be that lucky. According to the risk ranking of the Economist (2007a:75) the Emerging Europe is “flashing red”. Tighter liquidity, relatively higher spreads, and lower risk appetite is expected to increase the cost of financing in the region, and to penalise particularly those more vulnerable countries, with substantial current account deficits, relatively high inflation rates, external borrowing by the banks, soaring domestic credits, and property bubbles, like the Baltics, Bulgaria, Romania, and Turkey.

In the Baltic countries the fixed exchange rates is adding to the “risky mix.” The Economist (2007e:92) writes that “some fear the region could be Eastern Europe’s Achilles heel”. The majority of bank lending being denominated in, or indexed to, foreign currency in the Baltics and other parts of emerging Europe creates large external financing needs and private-sector currency mismatches, which makes these countries “look suspiciously like Thailand in 1997” (The Economist, 2007a:76). These economies are simply highly vulnerable to a change in investor sentiment, which could lead to capital outflow and depreciation, thereby soaring debts in local-currency terms. What happened in East Asia, i.e. over-borrowing and the severe currency mismatches which caused the

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9 Apart from Eastern Europe, the Economist (2007N17) mentions also India as a risky country, even if the country has a current account deficit of just 2.1%. 

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local currency value of debt to explode when currencies fell, is seen to be serious risk also in the Baltics. UniCredit Group New Europe Research Network (2007a:3-7) also argues that as inflation accelerates and credit growth shows only timid signs of slowdown, the risks of a hard landing in the overheated economies of the Baltic countries are now enhanced, but they “continue to believe in a soft landing scenario” and “controlled correction, with gradual credit squeeze”. This sounds more like hoping than genuine belief. It is also admitted that in Estonia the perception by foreign lenders might strengthen that the currency board arrangement is at risk UniCredit Group New Europe Research Network (2007a:3-7). Indeed as was seen in the panic sales of November in Estonia, when the economy is fragile even irrelevant rumors like “a report on the website of a radical Russian-speaking youth movement, which claimed that the Estonian government had decided to devalue” (UniCredit Group New Europe Research Network, 2007b:1) may cause problems. As of now the foreign exchange reserves of the central bank seem to be sufficiently high to defend the peg. In Latvia also growing fears of exchange rate devaluation led to pressures on the lat, which raises the pressure over the central bank to support the currency by selling foreign reserves (UniCredit Group New Europe Research Network, 2007a:22-23; The Economist, 2007e:92). According to the Economist (2007e:93) the only thing that could prevent a devaluation is the fact that Latvia’s banking system is largely foreign-owned; thus “if overstretched borrowers start to default, that will hurt shareholders abroad, mainly in Sweden”. Furthermore, it is again trusted that the Latvian Central Bank has enough reserves.

Slovakia is another country that seems to become increasingly more fragile, particularly regarding its rush to adopt the Euro in 2009. As euro adoption approaches, more volatility is expected in the exchange rate, as the investors become very sensitive to all information which could threaten or confirm euro adoption (UniCredit Group New Europe Research Network, 2007a).

4. Conclusion

If the conventional wisdom of the markets shifts from optimism to pessimism, can the EU-anchor help Eastern Europe? Simply ignoring the possibility of a massive capital outflow, which will trigger deeper real effects in the future, seems to be gambling in policy making. This behaviour is like ignoring a gas leakage in your house, and choosing a “wait and see” strategy, rather than trying to fix the leakage. “When the music stops”, as the chief executive of Citigroup had said, even the major responsible actors of the crisis, like himself, leaves the game, having
already pocketed generous income and even seniority benefits. But the effects of the bust might be bitter for the indebted and the wage earners as their wages fail to catch up with inflationary shocks following depreciation (Onaran, 2009).

Sound policy requires taking the global turbulences and their consequences seriously and considering them as cases in defence of financial regulation and international capital controls. Financial regulation along with industrial policy is the only long-run policy alternative to prevent financial fragility and the potential causes of a future crisis.

So the question is what makes this so obvious fact be ignored by the domestic policy makers and international organizations. The obvious measures like capital controls are not in the interest of the national and international capital that they are representing. Investors have to follow the short-term profit seeking motive and find innovative ways of making more profits without borders, even if they are risky.

The policy lesson of this analysis is that markets can not prevent systemic risk, but only postpone it and make it bigger. There is need for a democratic, but yet regulatory intervention to make the economy meet the needs of the people. Only then we can talk of a European enlargement project that can make a difference.
Figure 1: Current Account Deficit in relation to GDP (in %), 2007* for Europe and crisis years of others

Current Account Deficit/GDP (%)
2007* for Europe & Crisis years for others

I: Indonesia 96, K: Korea 96, M: Malaysia 97; P: Philippines 97; Th: Thailand 96; A: Argentina 00, B: Brazil 98; Me: Mexico 94; Tur93 and Tur00: Turkey 93 & 00
Tur: Turkey; Cz: Czech Republic; Hun: Hungary; Pol: Poland; Sk: Slovakia; Sl: Slovenia; Est: Estonia; Lat: Latvia; Lit: Lithuania; Bul: Bulgaria; Rom: Romania
Source: UniCredit Group New Europe Research Network estimations for Europe and for the other countries own calculations based on Economic Intelligence Unit Online Database (EIU).
Figure 2: Current Account Deficit in relation to FX Reserves (in %), 2007-March for Europe and crisis years of others

<table>
<thead>
<tr>
<th>Country</th>
<th>2007-March</th>
<th>Crisis Years</th>
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<td>Tur</td>
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<td>Tur00</td>
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Source: Own calculations based on Economic Intelligence Unit Online Database (EIU).
Figure 3: Short-term Foreign Debt in relation to total Foreign Debt Stock (in %), 2006 for Europe and crisis years for others

<table>
<thead>
<tr>
<th>Country</th>
<th>Short-term Foreign Debt /total Foreign Debt Stock (%)</th>
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<td>Cz</td>
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Source: Own calculations based on Economic Intelligence Unit Online Database (EIU)
Figure 4: Short-term Foreign debt Stock in relation to FX Reserves (%), 2006 for Europe and crisis years for others

Mexico 94 not in graph: 626%
I: Indonesia 96, K: Korea 96, M: Malaysia 97, P: Philippines 97, Th: Thailand 96, A: Argentina 00, B: Brazil 98, M: Mexico 94, Tur93 & Tur 00: Turkey 93 and 00.
Tur: Turkey; Cz: Czech Republic; Hun: Hungary; Pol: Poland; Sk: Slovakia; Sl: Slovenia; Est: Estonia; Lat: Latvia; Lit: Lithuania; Bul: Bulgaria; Rom: Romania
Source: Own calculations based on Economic Intelligence Unit Online Database(EIU).
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