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NAVIGATING THROUGH COVID-19 IN THE MEDITERRANEAN ACT 1: STRATEGIES FOR INTEGRATION AND RESILIENCE

Financial reforms for resilience in the Mediterranean

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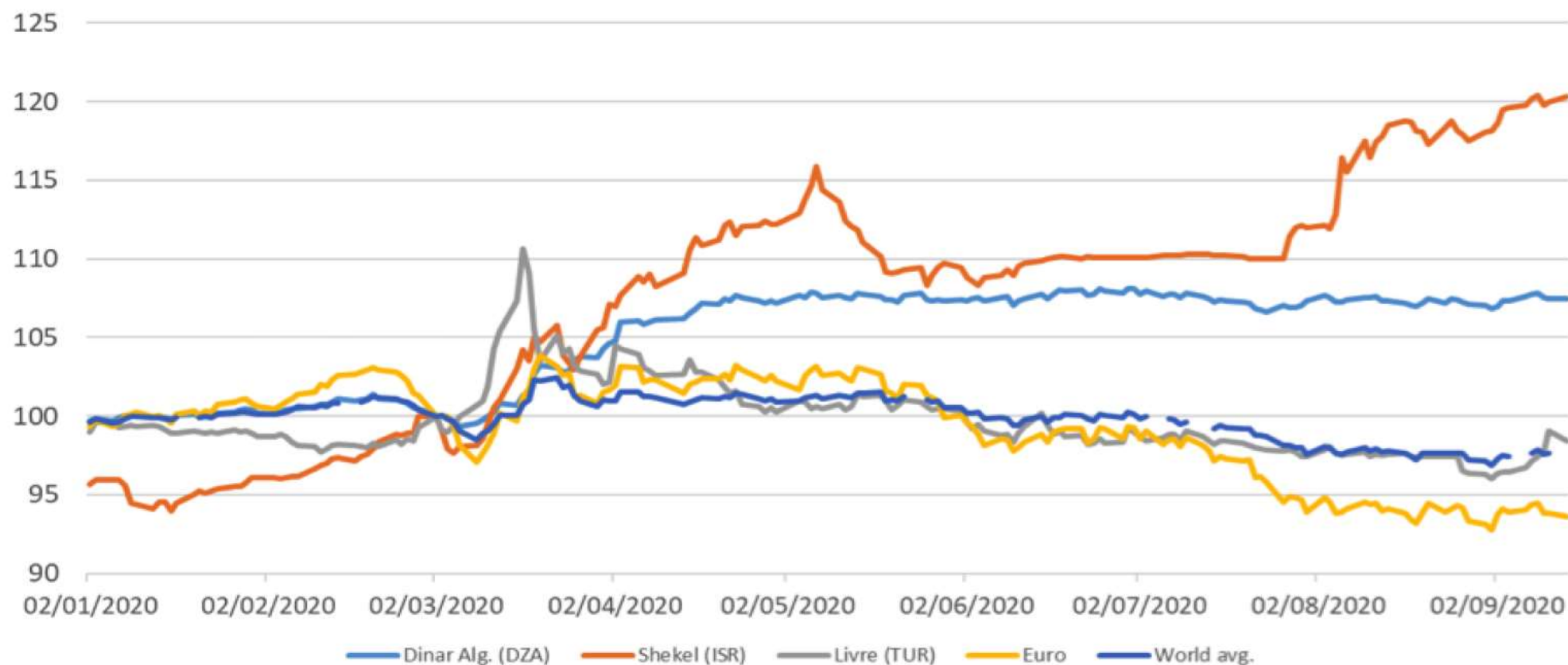
Introduction

- Inclusive growth and poverty reduction are important for fostering justice and reducing inequalities
- The COVID crisis has hit a region under severe economic and social and political stress
- Mediterranean countries are simultaneously suffering the consequences of the pandemic and the pre-existing international financial instability
- Oil producers/exporters have been directly affected by the decline in demand and the price of oil
- These economies are vulnerable to the slowdown in FDI, especially coming from Europe

Vulnerability of Southern Mediterranean countries

- Global financial transmission mechanisms of the lockdown include:
 - Adverse commodity price developments (especially for oil-producing and exporting countries)
 - ↑ in global risk aversion
 - Rush to the USD
 - ↓ the value of the domestic currency against the USD
 - ↓ in capital inflows (particularly FDI)
- These developments make foreign debt more difficult to honor
- Since the USD is the dominant currency, capital has been flowing from South to North, instead of the other way around

Nominal exchange rate vis-à-vis the USD, 2/3/2020 = 100



Conclusion and some policy recommendations

- ECB swap lines to cover liquidity needs
- Given the possibility of a USD devaluation starting next year, financing investments could be
 - Also denominated in other currencies (euro, yen, yuan, sterling)
 - Rapidly provided via Special Drawing Rights, managed by the IMF
- Regional cooperation measures for the regulation of capital flows (in particular to prevent further devaluations)
- Creation of an extra-financial Euro-Mediterranean rating agency, which takes into account ESG criteria