



THE EUROPEAN UNION AND THE CRISIS OF THE EURO



FIVE DRIVING FORCES FOR THE EU DEVELOPMENT

1.THE MEMORY OF WAR

THE “NEVER AGAIN”

THE RECONCILIATION BETWEEN FRANCE AND GERMANY

MOTIVATION FOR THREE GENERATIONS OF EUROPEANS

NOW IS VANISHING BECAUSE THE PERSONAL MEMORY IS PASSING ON



2.THE SOVIET THREAT

COLD WAR WAS AN STRONG INCENTIVE FOR WESTERN
EUROPEANS TO UNITE

UNITED STATES ACTIVE SUPPORTER OF EUROPEAN INTEGRATION

FROM MARSHALL PLAN TO THE GERMAN REUNIFICATION

BUT TODAY

PUTIN IS NOT STALIN

AND...

WASHINGTON HAS OTHER PRIORITIES



3. REHABILITATION OF GERMANY

UNTIL 1990 THE EUROPEAN INTEGRATION WAS DRIVEN MAINLY BY THE FRENCH-GERMAN ENGINE

GERMANY FELT A DESIRE OF REHABILITATION IN THE EUROPEAN FAMILY

FOR GERMANY EUROPE WAS A WAY OF REAPPEARING IN THE POLITICAL SCENE

FOR FRANCE EUROPE WAS THE WAY OF PLAYING A ROLE AFTER THE LOST OF THE COLONIAL EMPIRE

GERMANY KNEW THAT ONLY BY GAINING THE TRUST OF THEIR NEIGHBORS THE REUNIFICATION COULD BE POSSIBLE

THE CONSTRUCTION OF A BIG EUROPEAN MARKET AND A COMMON CURRENCY WAS GOOD FOR THEIR EXPORT CAPACITIES



3. REHABILITATION OF GERMANY

BUT TODAY....

THE NATIONAL PURPOSE OF THE REUNIFICATION HAS BEEN ACHIEVED

THE YOUNG GENERATIONS OF GERMANS DO NOT FEEL GUILTY FOR THE SINS OF THEIR GRAND FATHERS

GERMANY IS NOT READY TO CONTINUE PAYING FOR MORE EUROPE

NEITHER IS READY TO TAKE THE LEAD



4.THE FALL OF THE BERLIN WALL

WHEN THE EASTERN NATIONS OF EUROPE BECOME FREE FROM THE SOVIET DOMINATION THEY WANTED TO JOIN THE EUROPEAN FAMILY

THE WESTERN NATIONS FELT THAT IT WAS BETTER TO LET THEM PARTICIPATE THAN TO KEEP THEM OUT

THE “BIG BANG” TO 27 MEMBER STATES

ENLARGEMENT AS OPPOSED TO DEEPENING OF THE UNION



4.THE FALL OF THE BERLIN WALL

BUT TODAY.....

THE ONCE-CAPTIVE NATIONS OF EASTERN EUROPE HAVE JOINED THE UK ON HIS RELUCTANCY ON LOOSING SOVERIGNITY

THEY ARE NOT UNIFORMLY PASSIONATE ABOUT THE EU :

POLAND IS MUCH IN FAVOUR

CZECH REPUBLIC AND HUNGARY ARE AMONG THE MOST SKEPTICAL MEMBERS

FOR SECURITY THEY RELAY MORE IN THE UNITED STATES AND THE NATO THAN IN THE EU



5.TO FACE GLOBALIZATION

SIZE MATTERS : THE 21ST CENTURY WILL BE ONE OF GIANTS

EUROPE WILL NOT REMAIN THE WORLD'S LARGEST ECONOMY FOR A LONG TIME

EVEN GERMANY WILL BE TOO SMALL IN A GLOBALIZED WORLD

EUROPEANS NEED THE SIZE OF THE EU TO PRESERVE THE COMBINATION OF PEACE, SOCIAL SECURITY (RELATIVE) AND QUALITY OF LIFE

“EUROPE” WOULD MEAN A WAY OF RISING STANDARD OF LIVING AND SOCIAL SECURITY



5.TO FACE GLOBALIZATION

BUT TODAY

THE BENEFITS OF BELONGING TO THE EU ARE NOT SO CLEAR FOR MANY

THE EU FACES

AGING POPULATION

ACCUMULATED DEBT,PUBLIC BUT MAINLY PRIVATE

GLOBAL COMPETITION

THE CRISIS OF THE EURO

WELL, THE EURO IS NOT IN CRISIS....IT IS STILL AT 1,3 \$

SOME EUROPEAN STATES ARE IN CRISIS DUE TO THE DEBT AND COMPETITIVITY PROBLEMS AND THE EURO DO NOT ALLOW THEM TO USE SOME ECONOMIC POLICY TOOLS AS CURRENCY DEVALUATION



THE TEN ROOTS OF THE CRISIS



1.THE FAILURE OF THE SGP

THE STABILITY AND GROWTH PACT WAS BASED ON RULES TO CONTROL THE PUBLIC SECTOR

PUBLIC DEBT LESS THAN 60 % OF THE GNP

PUBLIC DEFICIT LESS THAN 3 % OF THE GNP

THIS RULES-BASED PACT FAILED BOTH ON ITS CONCEPTION AND IMPLEMENTATION

GERMANY AND FRANCE WERE THE FIRST ONES TO NOT FULLFIL WITH IT...AND AVOIDED SANCTIONS

GREECE CHEATED FOR YEARS ABOUT ITS PUBLIC DEFICIT

HIGH PUBLIC DEBT IN GREECE AND ITALY BEFORE THE CRISIS

RECENT AGREEMENTS TRY TO FIX IT WITH STRONGER FISCAL RULES AND QUASI AUTOMATIC SANCTIONS

BUTTHEY CAN MAKE THE SITUATION WORST



2.SOLE FOCUS ON FISCAL ISSUES

NOT ALL PROBLEMS ARE FISCAL

IT WAS CONSIDERED THAT ONLY THE PUBLIC SECTOR SHOULD BE CONTROLLED
BECAUSE THE PRIVATE SECTOR WOULD BE CONTROLLED BY THE MARKET

BUT...INSUSTAINABLE CREDIT AND HOUSING BOOMS IN SPAIN AND IRELAND

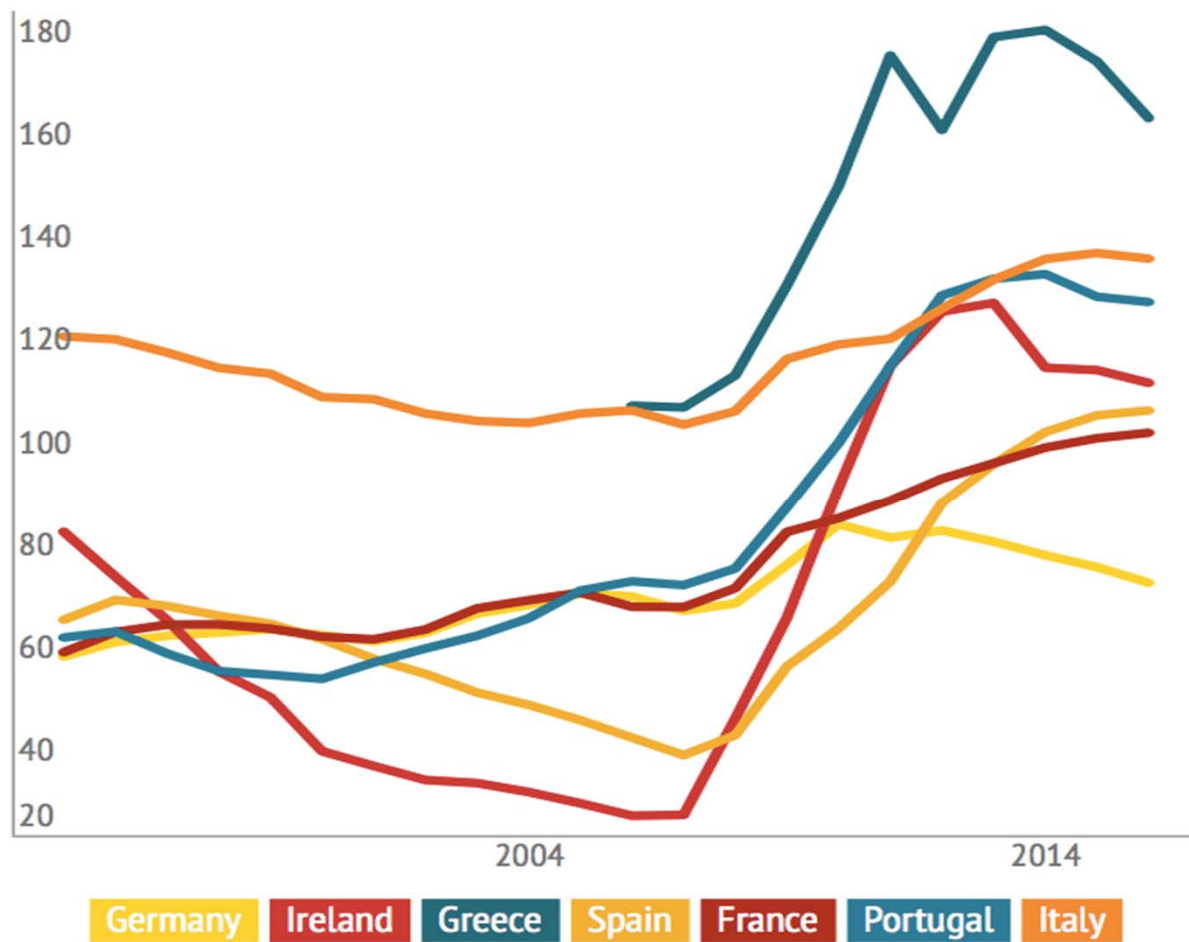
GREECE WAS A FISCAL CASE BUT SPAIN AND IRELAND WERE NOT

IN GREECE THE DEFICIT CREATED THE CRISIS

IN SPAIN AND IRELAND THE CRISIS CREATED THE DEFICIT

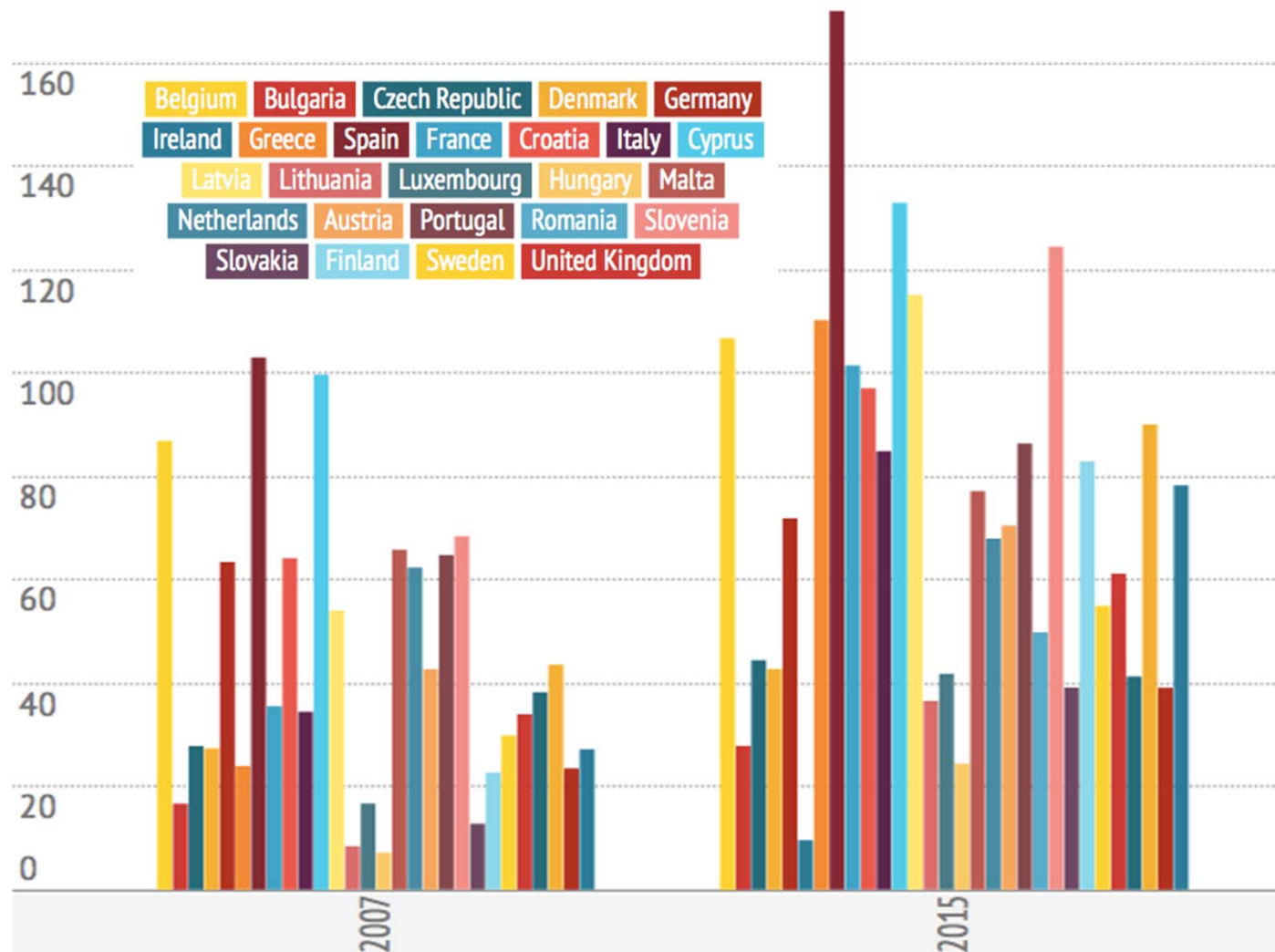
EMERGENCE OF STRUCTURAL IMBALANCES SUCH AS HIGH CURRENT ACCOUNT
DEFICITS AND ERODED COMPETITIVITY

DEVELOPMENT OF PUBLIC DEBT IN SOME EUROZONE COUNTRIES (% OF GDP)



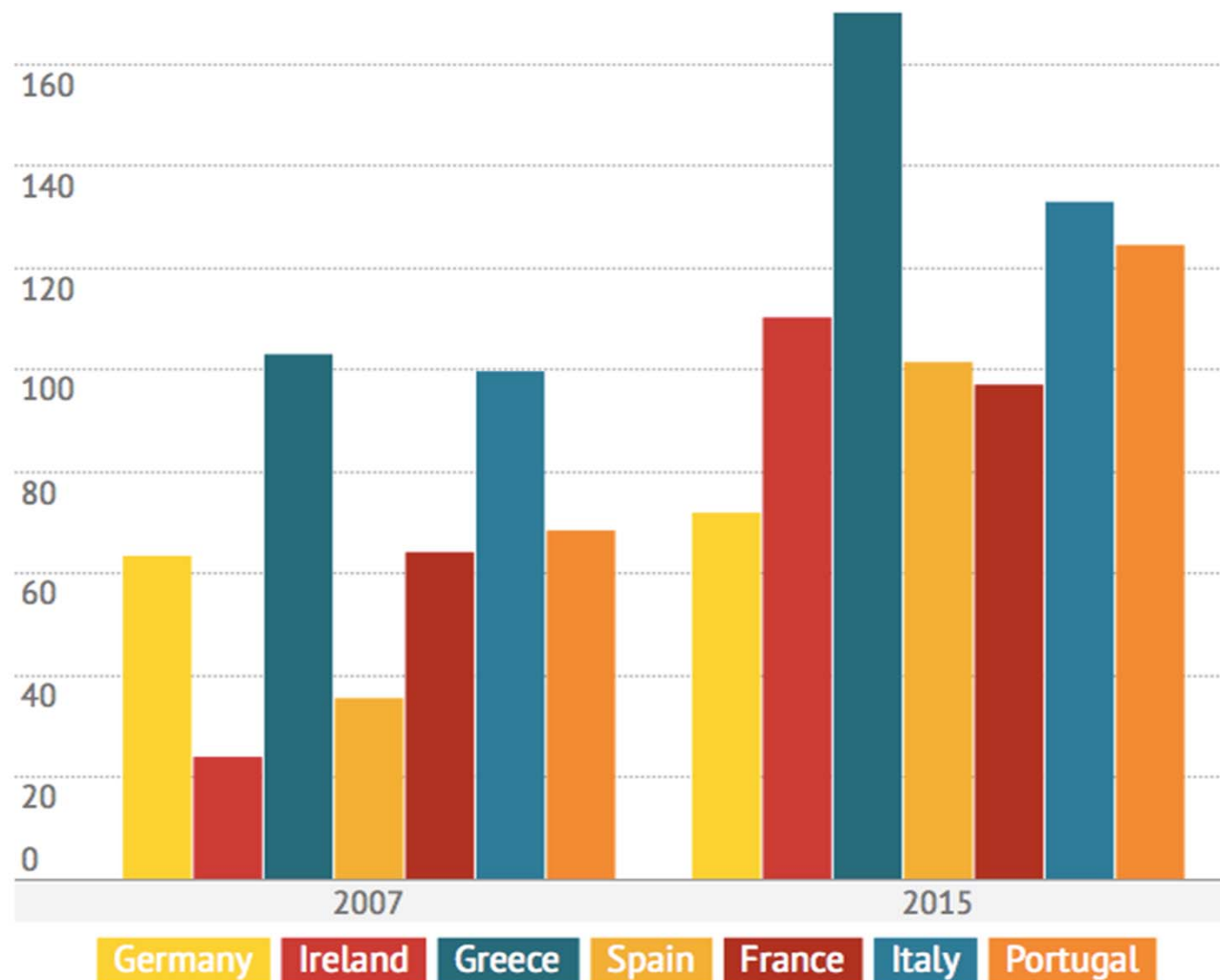
Source: Eurostat

GENERAL GOVERNMENT DEBT EU 27, 2007 VS. 2010 (% OF GDP)*



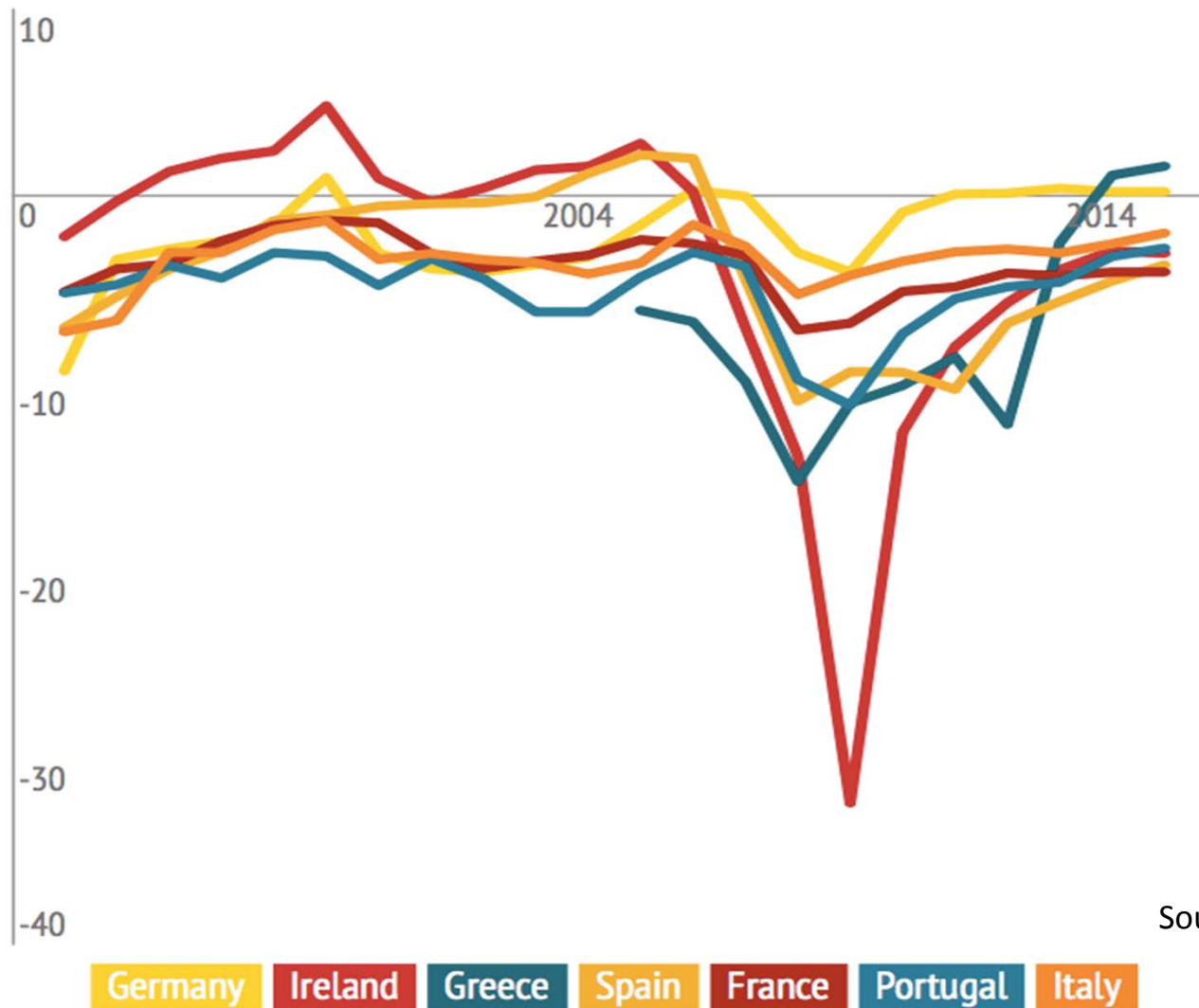
* General government consolidated gross debt as a percentage of GDP;
Source: Eurostat

GENERAL GOVERNMENT DEBT EU 27, 2007 VS. 2010 (% OF GDP)*



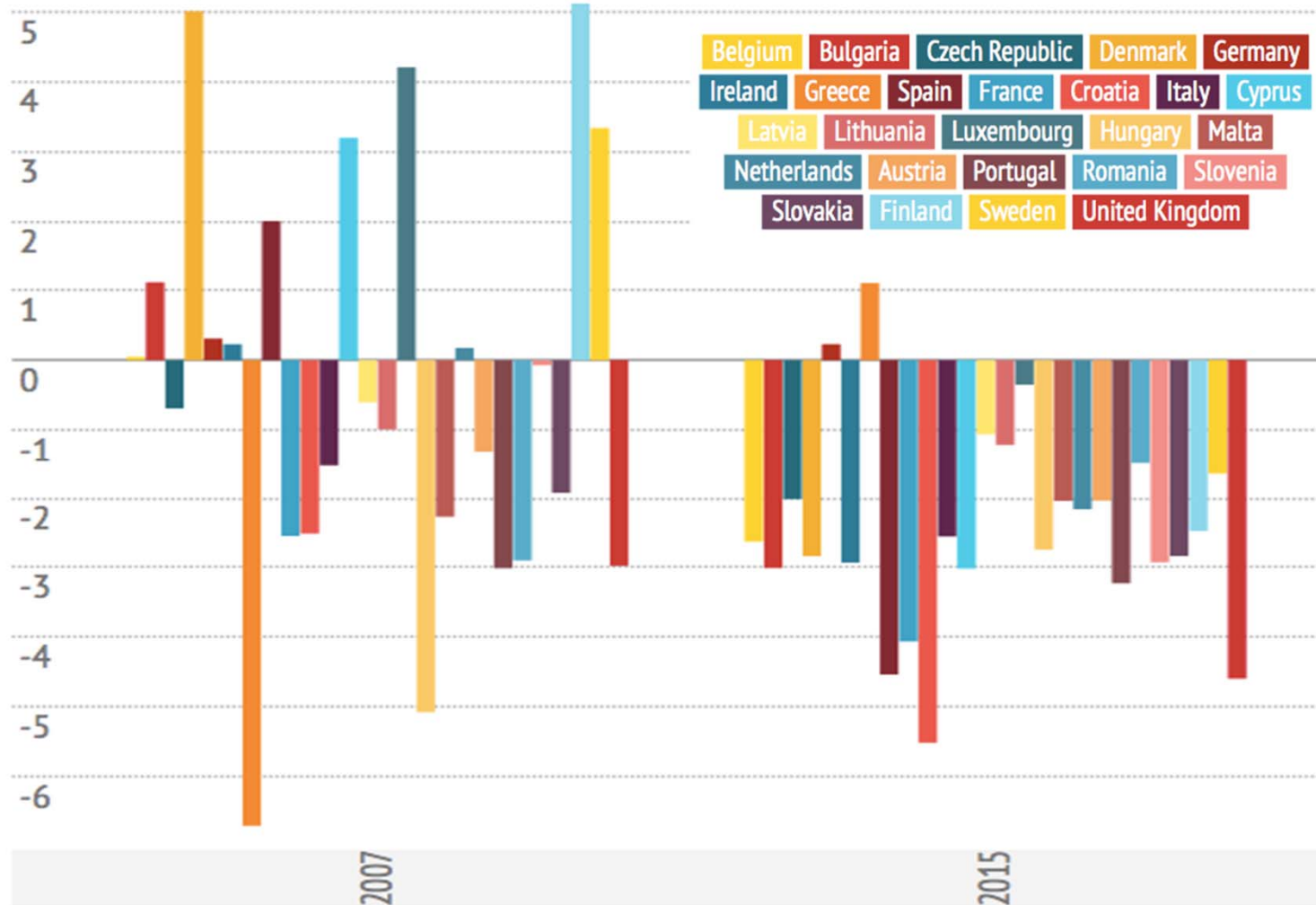
* General government consolidated gross debt as a percentage of GDP; Source: Eurostat

DEVELOPMENT OF PUBLIC DEFICIT, SELECTED COUNTRIES (% OF GDP)



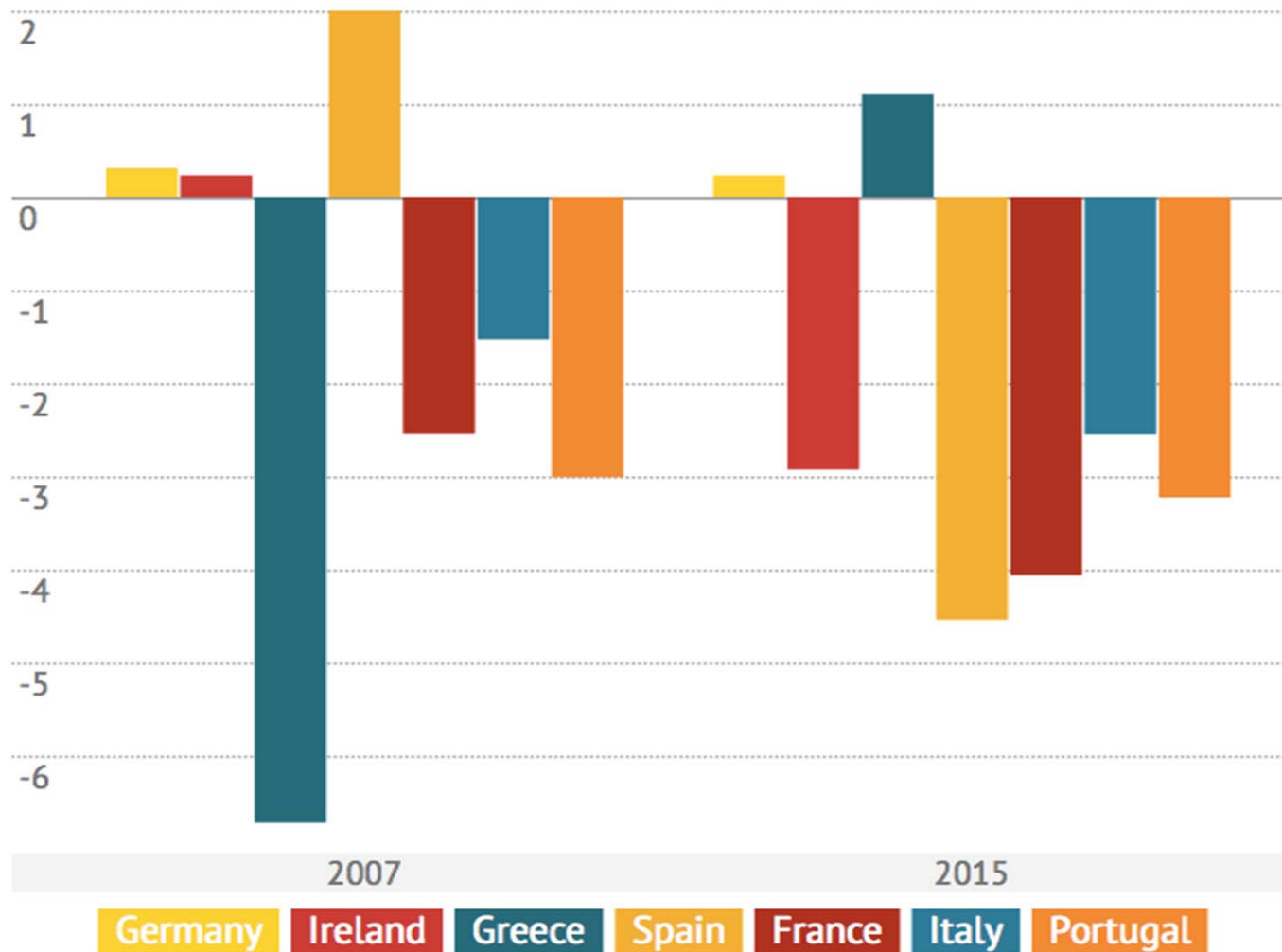
Source: Eurostat

PUBLIC BALANCE EU27, 2007 VS. 2010 (% OF GDP) *



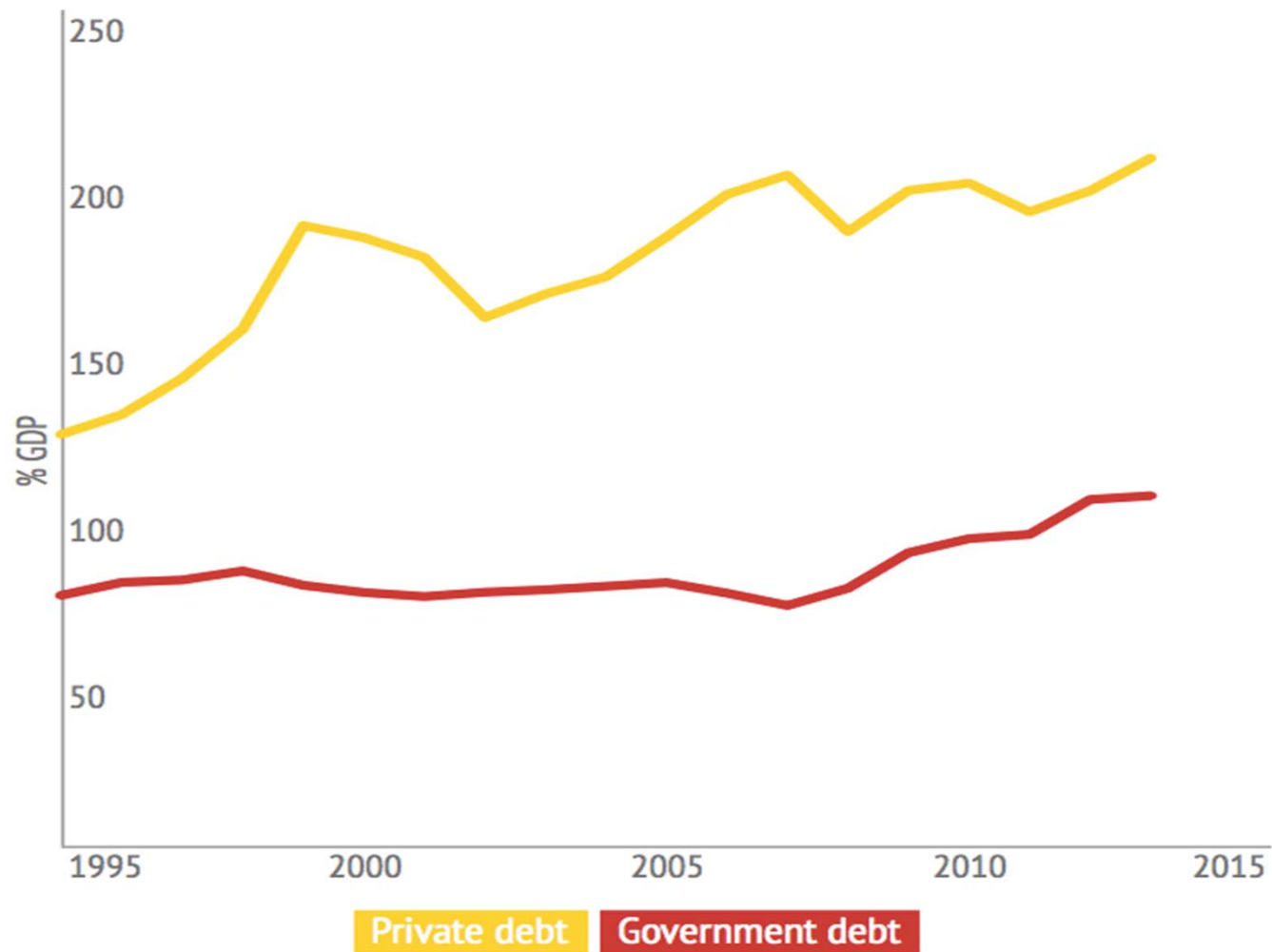
*Net borrowing /lending of consolidated general government sector as a percentage of GDP;
Source: Eurostat

PUBLIC BALANCE EU27, 2007 VS. 2010 (% OF GDP) *



*Net borrowing/lending of consolidated general government sector as a percentage of GDP;
Source: Eurostat

DEVELOPMENT OF PUBLIC AND PRIVATE DEBT IN THE EUROZONE (% GDP)



Source: ECB



3.NO MECHANISM FOR STRUCTURAL ADJUSTMENT

THE COMMON CURRENCY WAS SUPPOSED TO MAKE THE MEMBER STATES ECONOMIES TO CONVERGE

IN FACT THE CONTRARY HAS HAPPENED,THE ECONOMIES HAVE DIVERGED

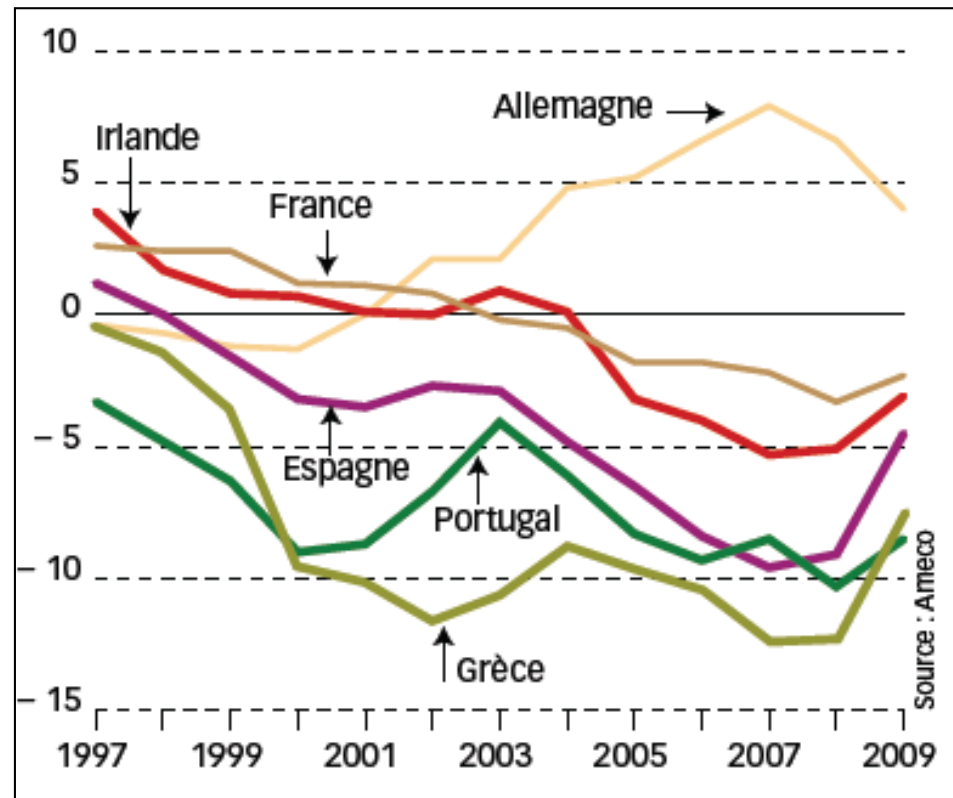
SOME COUNTRIES,LIKE GERMANY WERE ABLE TO ADJUST WITHIN THE EURO AREA IMPROVING COMPETITIVENESS

OTHER COUNTRIES LIKE ITALY,SPAIN AND PORTUGAL HAVE LOST COMPETITIVITY

STROG DIFFERENTIALS ON INFLATION AND LABOR COSTS

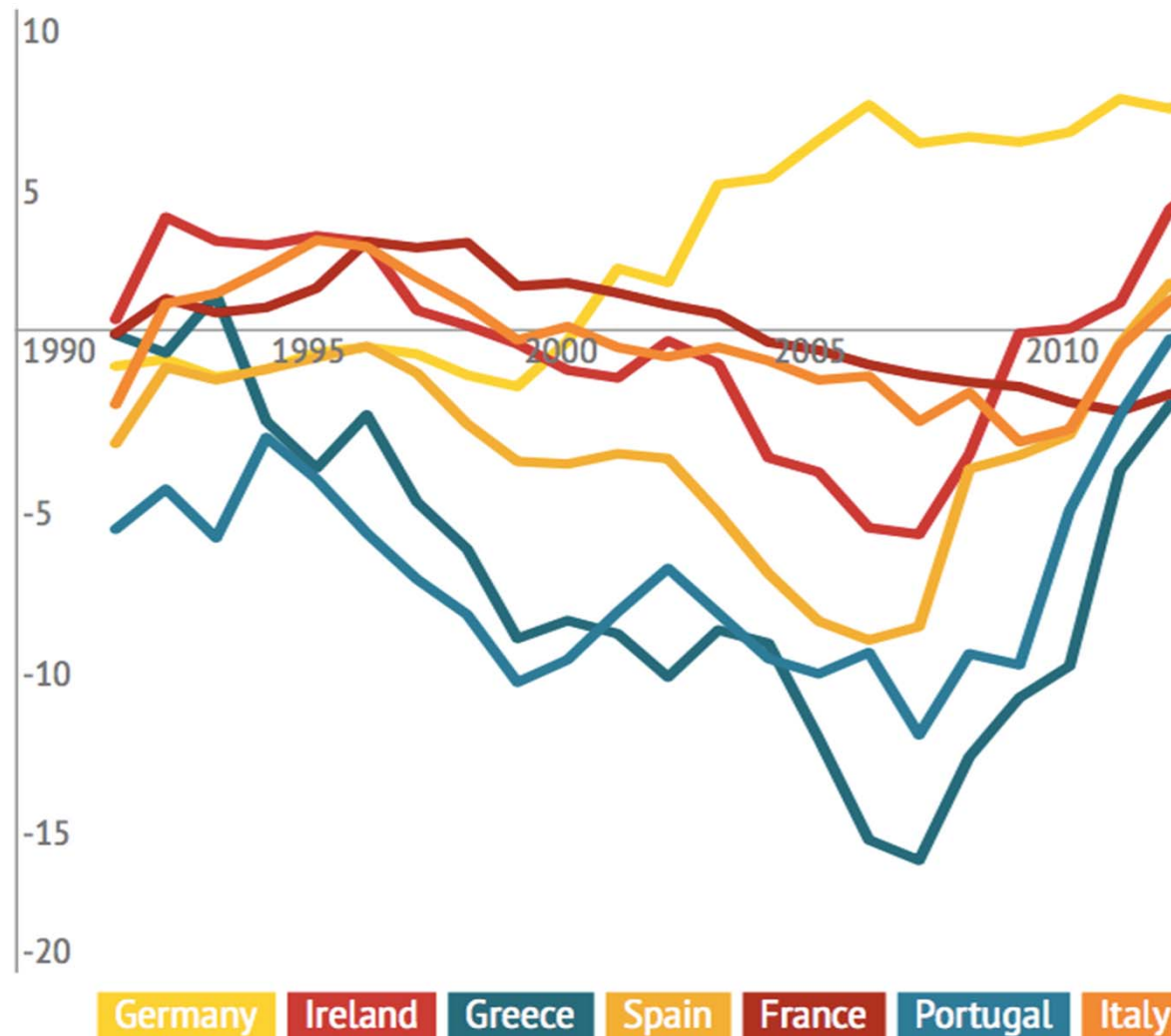
NOW A SYSTEM OF MUTUAL ASSESSMENT ON STRUCTURAL ISSUES WAS INTRODUCED IN 2010...BUT IT WILL TAKE A LONG

Balance of payments, selected countries (in % GDP)



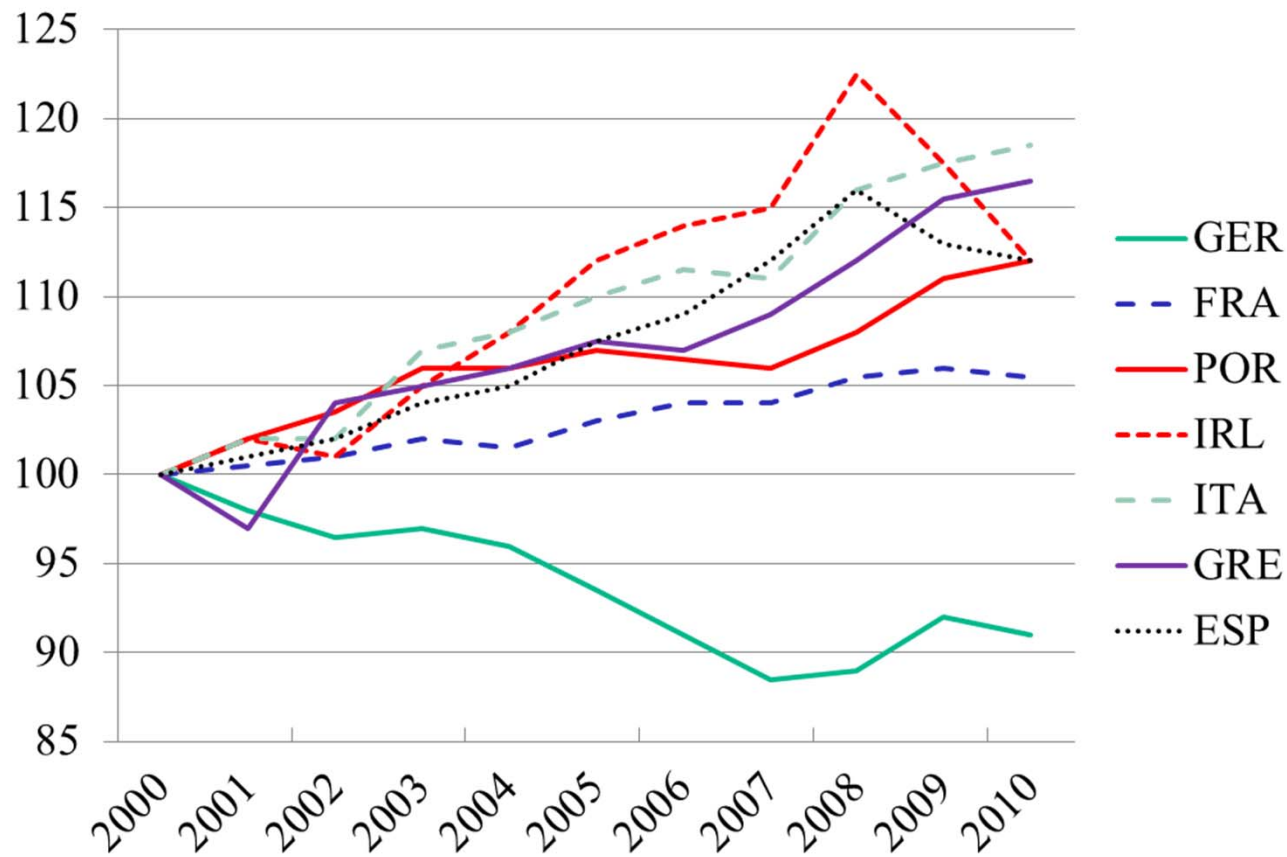
Source: Alternatives Economiques

BALANCE OF PAYMENTS, SELECTED COUNTRIES (IN % GDP)



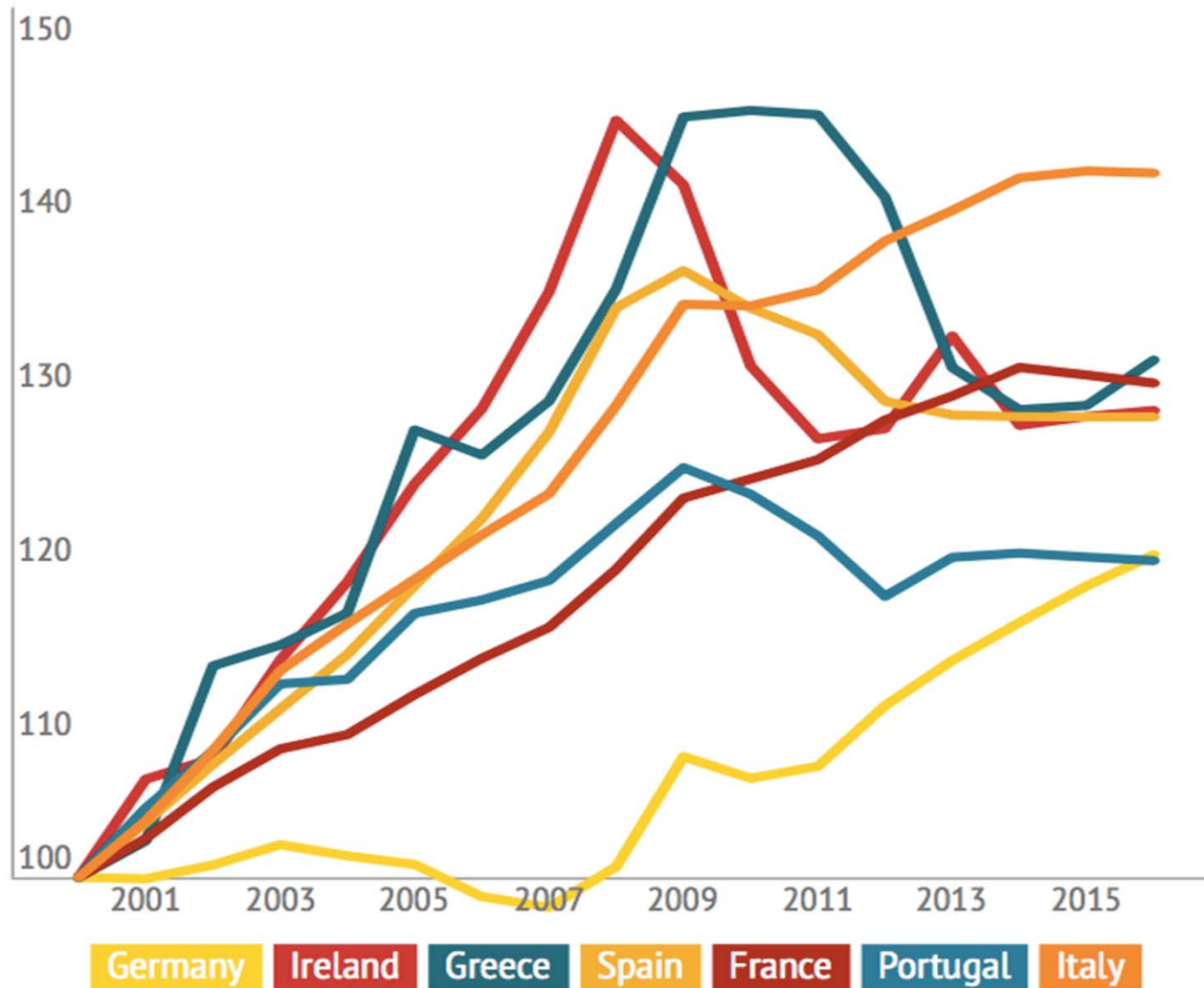
Source: European
Commission
(AMECO)

Evolution of unit labour costs in eurozone (2000=100)



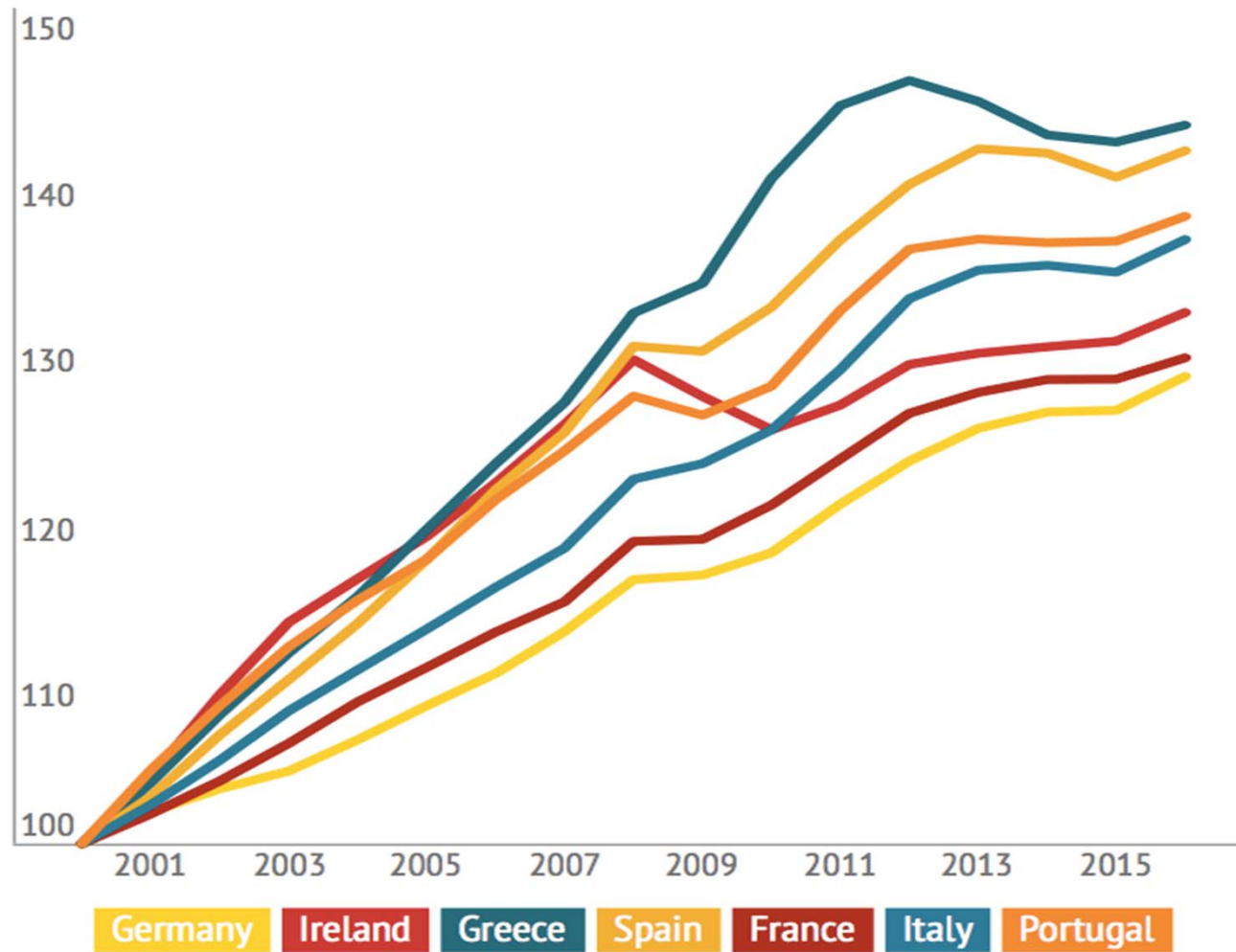
Source: European Commission

EVOLUTION OF UNIT LABOUR COSTS IN THE EUROZONE (2000=100)



Source: European
Commission
(AMECO)

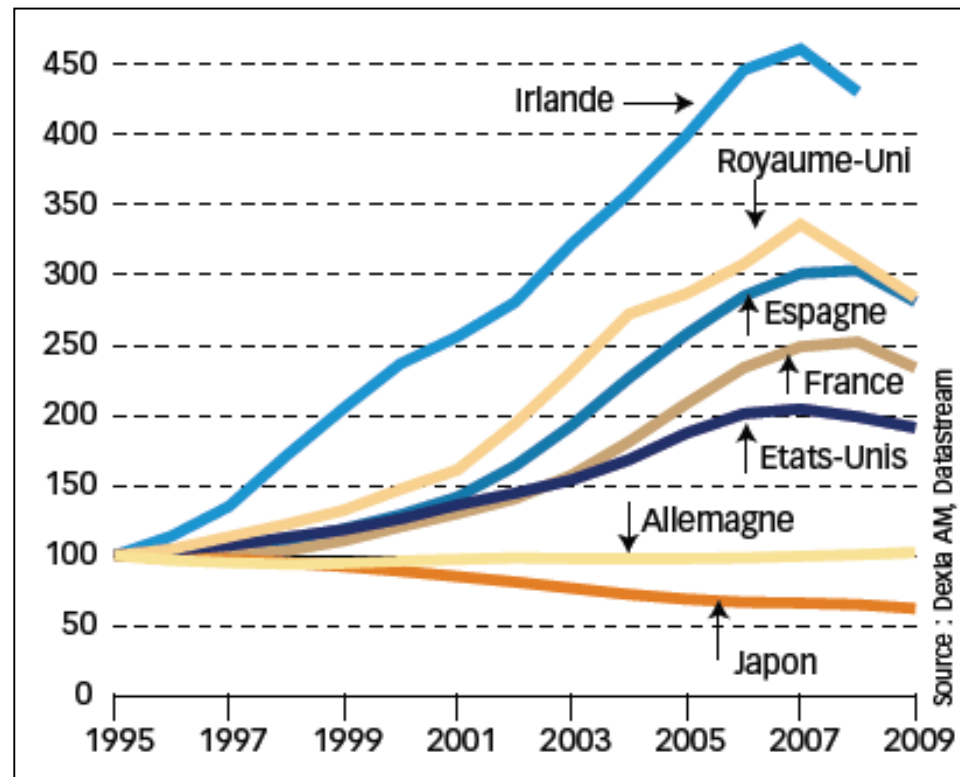
INFLATION IN THE EUROZONE*



*Harmonised consumer price index (All-items)

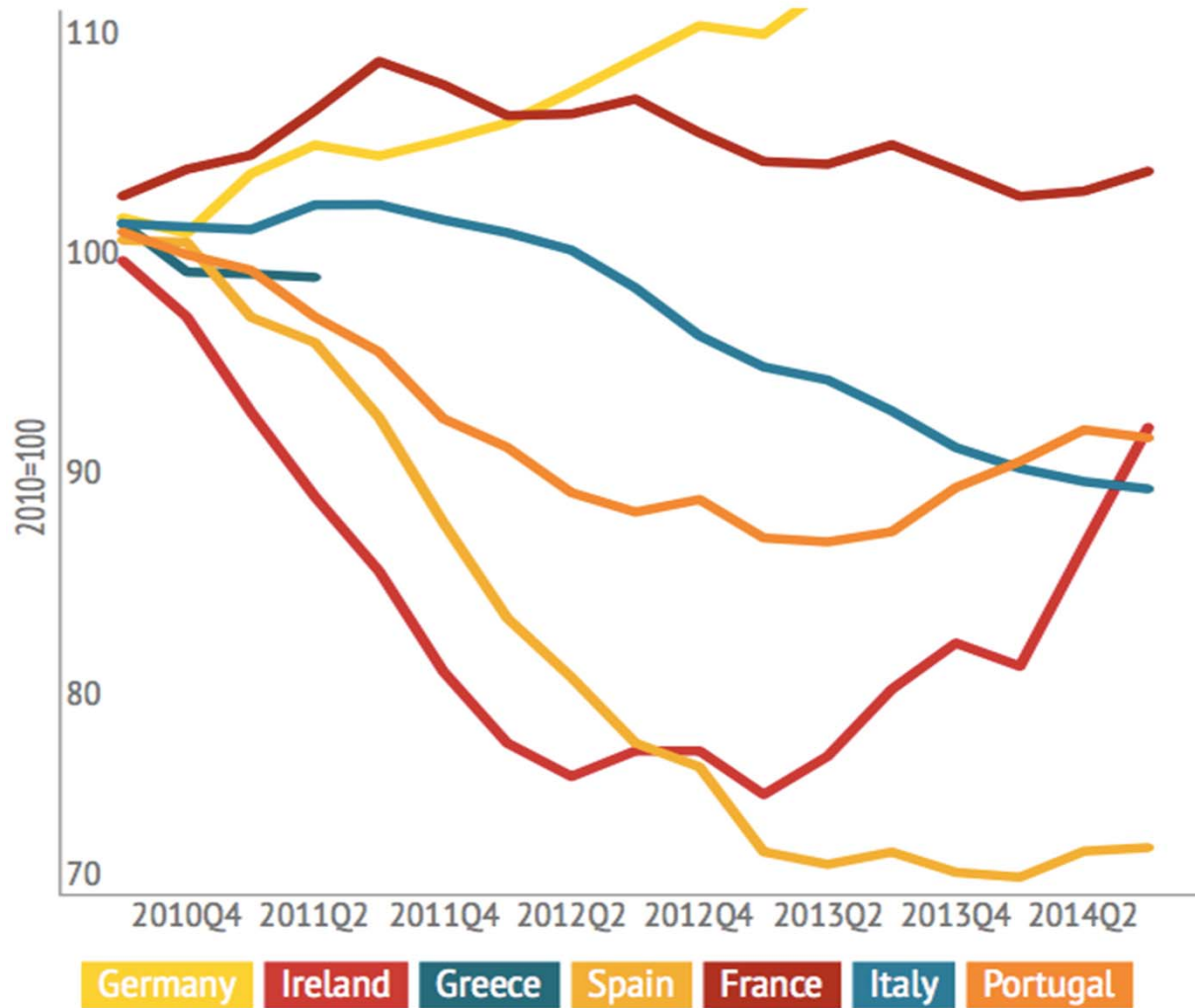
Source:
European Commission (AMECO)

Housing prices (1995=100)



Source: Alternative Economiques

HOUSING PRICES AFTER THE CRISIS (2010=100)



Source:
Eurostat



4.NO CRISIS RESOLUTION MECHANISM

THE EURO CRISIS CAME AS A SURPRISE

NO CLUES ABOUT WHAT TO DO

IN ORDER TO FOSTER FISCAL DISCIPLINE THE TREATIES FORBID THE MEMBER STATES TO HELP OTHERS MEMBERS IN TROUBLE

TEMPORARY ARRENGEMENTS WERE MADE (EFSSF;EFSM)

NOW A PERMANENT RESCUE FUND (ESM) IS BEEING APPROVED WITH 500 € BILLIONS.BUT ...IT MAY NOT BE ENOUGH

IN OTHER FEDERATIONS LIKE THE USA SIMILAR FUNDS DO NOT EXIST

ONLY THE ECB HAS ENOUGH FIRE POWER...BUT IT CAN NOT USE IT



5.CORRELATION BETWEEN BANKING AND DEBT CRISIS

BANKING FEDERATION MEANS CENTRALISATION OF

BANK RESOLUTION, REGULATION AND SUPERVISION

DEPOSIT GARANTEES

IT IS ON THE WAY BUT NOT FOR THE DEPOSIT GUARANTEE CENTRALISATION

DEBT MUTUALISATION :EUROBONDS

IT MEANS POOLING NATIONAL BONDS ISSUANCES INTO A COMMON BOND FOR WHICH ALL COUNTRIES WOULD BE JOINTLY LIABLE

IT IS NOT ON THE WAY BECAUSE IT REQUIRES A MUCH STRONGER POLITICAL UNION

REMINDE WHAT HAMILTON DID IN 1792 :CONSOLIDATE THE DEBT OF THE STATES INTO US FEDERAL DEBT.BUT....WE ARE NOT IN AN HAMILTONIAN MOMENT IN EUROPE



6.STRONG INTERDEPENDENCE BETEWEEN COUNTRIES

MUCH STRONGER THAT WE ENVISIONED DURING THE GOOD YEARS BEFORE THE CRISIS

BUT THE EUROPEAN STATES CONTINUE BELEIVING IN THE MIRAGE OF INDEPENDENCY

THE GERMAN BANKS INVESTED IN THE SPANISH HOUSING BUBBLE

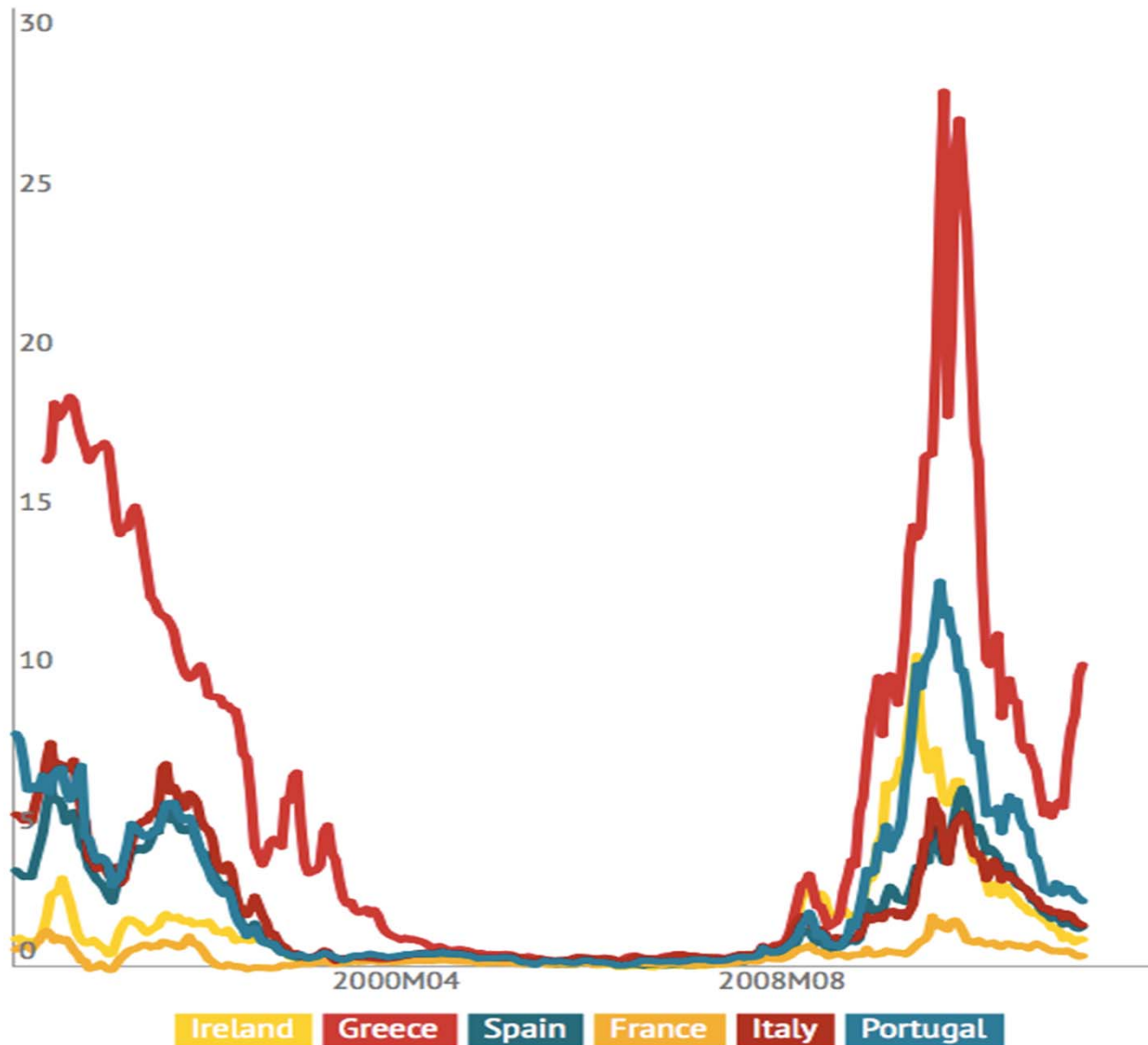
THE FRENCH AND GERMANS BANKS HAS (HAD) A LOT OF GREECK BONS

THE FALL OSF A “SMALL” STATE PRODUCES CONTAGION TO OTHERS

THE FALL OF A “LARGE” SATATE AS ITALY LEAD TO A MELTDOWN OF THE EUROPEAN ECONOMY

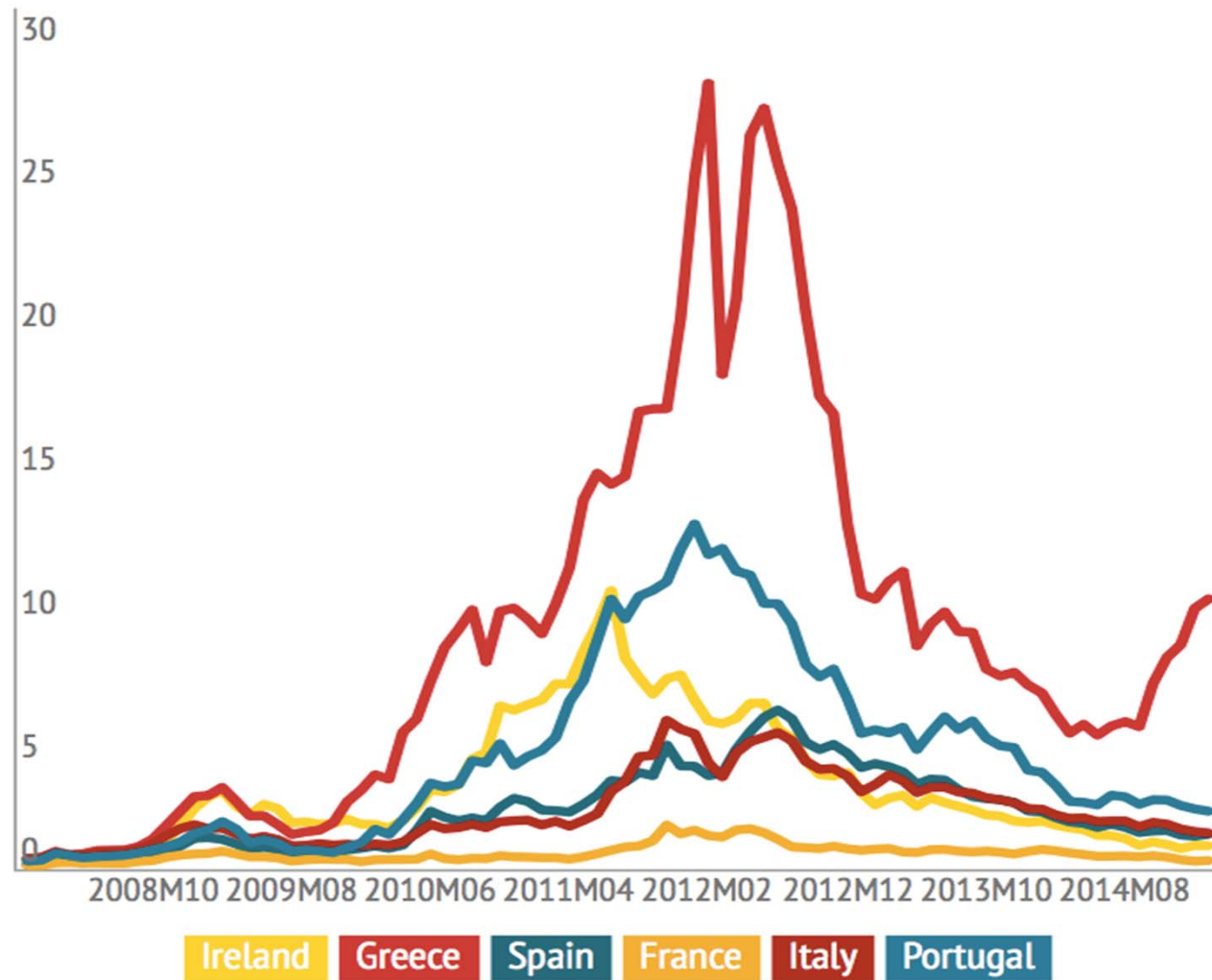
ITALY CANNOT BE ALLOWED TO GO BANKRUPT...BUT TO SAVE IT IS VERY EXPENSIVE

RISK PREMIUM, SELECTED COUNTRIES (1992-2015)



Source:
Eurostat

RISK PREMIUM, SELECTED COUNTRIES (2008-2015)



Source:
Eurostat

7.NO LENDER OF LAST RESORT

THE ECB IS NOT ALLOWED TO FINANCE THE GOVERNMENTS
SO, IT IS AS IF THEY WERE BORROWING IN A “FOREING” CURRENCY,A CURRENCY THAT
THEY DO NOT CONTROL

THE FED (AND THE BANK OF ENGLAND AND JAPAN) CAN ACT AS A LENDER OF LAST
RESORT FOR THE STATES PRINTING MONEY TO BUY GOVERNMENT BONDS

IN SPITE THE TREATIES THE ECB HAS STARTED BUYING BONDS BUT ONLY IN THE
SECONDARY MARKET

ONLY THE ECB CAN SAVE THE EURO. DRAGHI SEEMS TO UNDERSTAND IT NOW.

BUT HE WILL NEVER BE ABLE TO BEHAVE LIKE BERNANKE

BERNANKE CAN SAY THAT HE CARES ABOUT UNEMPLOYMENT,DRAGHI NOT

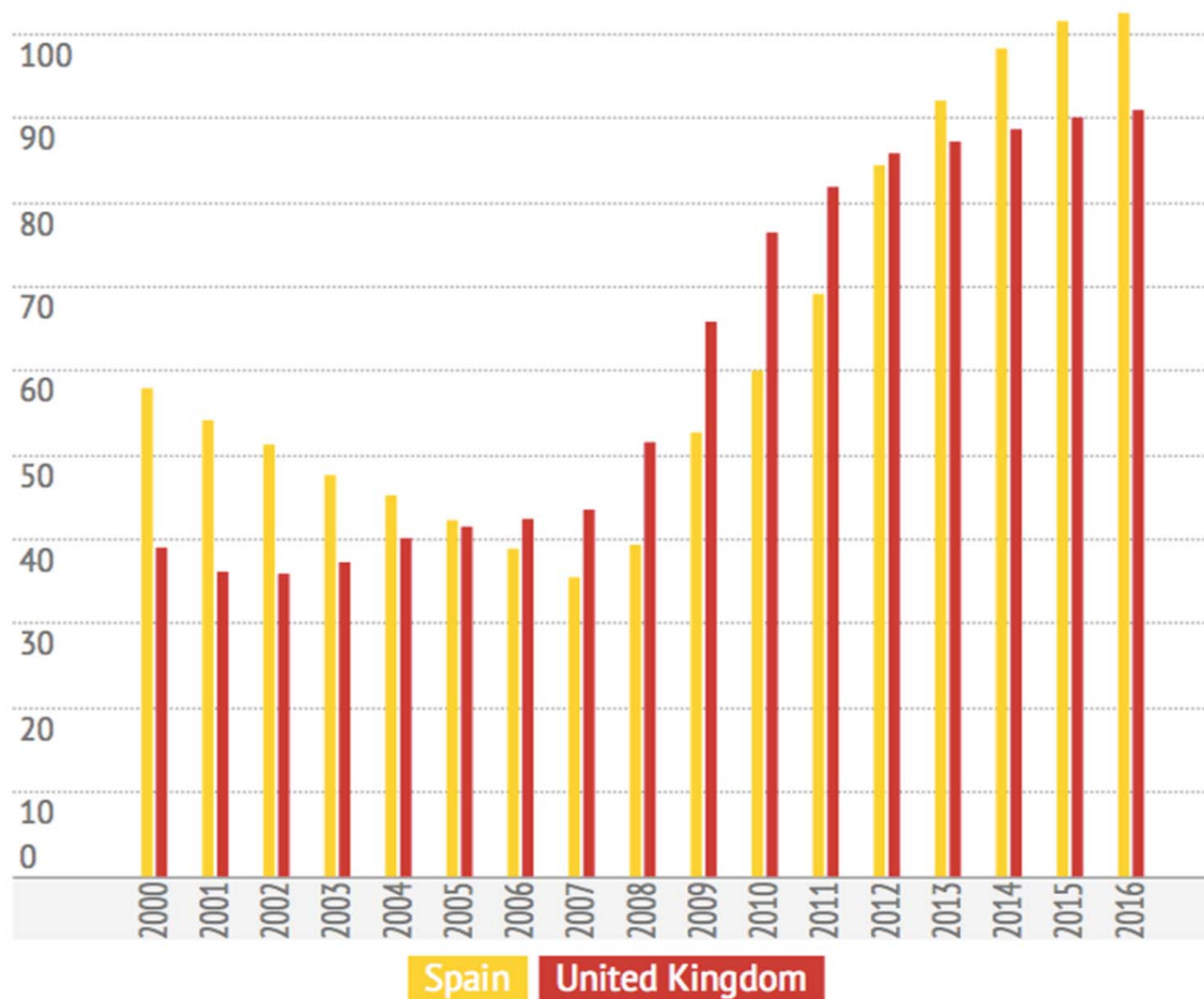
REMINDE THAT THE FED DOES NOT BUY THE DEBT OF THE US STATES

DEVELOPMENT OF PUBLIC DEBT, EUROZONE VS. US (% OF GDP)

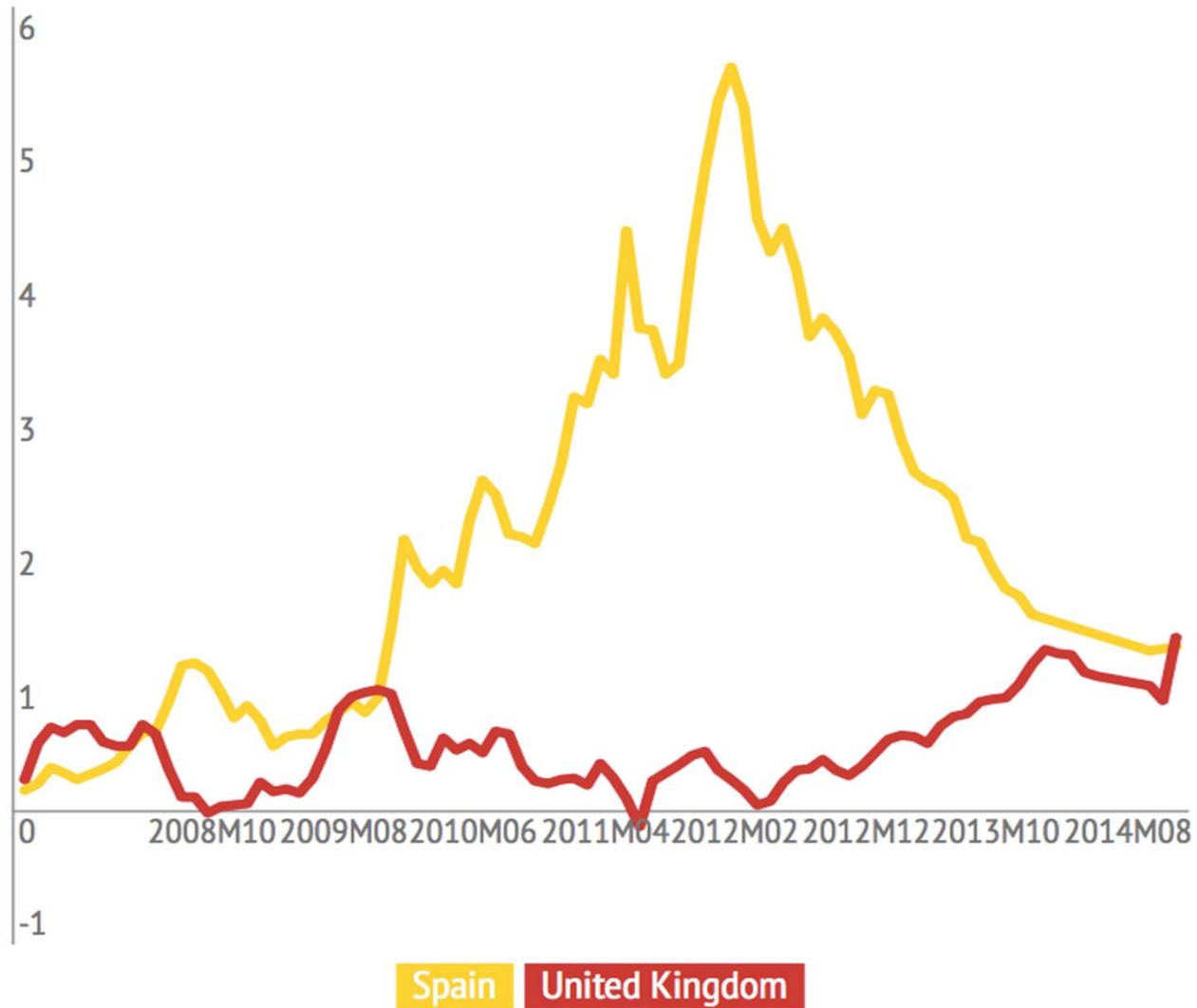


Source:
IMF

EVOLUTION OF THE PUBLIC DEBT IN UK AND SPAIN (% GDP)



RISK PREMIUM SPAIN AND UK (2008-2015)



Source:
Eurostat



8. RECESSIVE DOWNWARD SPIRAL

IN COUNTRIES UNDER SEVERE ADJUSTMENT PROGRAMS THE FISCAL CUTS LEADS TO A WEAKER ECONOMY

THEREBY LOWERING PUBLIC REVENUES AND CREATING THE NEED FOR MORE FISCAL ADJUSTMENT

DIFFICULT TO BREAK THIS VICIOUS CIRCLE

IN THE US THE FEDERAL BUDGET ACTS AS AN AUTOMATIC STABILISER
(FOR EXEMPLE INVESTING MORE IN DISTRESSED STATES)

THE US FEDERAL BUDGET IS MORE THAN 20 % OF GNP
BUT.....IN THE EU THE “FEDERAL” BUDGET IS LESS THAN 2 % OF THE GNP

WE SHOULD INCREASE THE EU BUDGET....BUT IT REQUIRES UNANIMITY

AUSTERITY ALONE WILL NOT SOLVE THE PROBLEM



9. REDUCTION IN CREDIT SUPPLY

THE NEGATIVE FEED BACK LOOP BETWEEN CRISIS AND GROWTH IS AFFECTING ALL EURO AREA COUNTRIES THROUGH THE REDUCTION OF CREDIT SUPPLY

THE MOST IMPORTANT THREAT FOR THE EUROPEAN ECONOMY IS A CREDIT CRUNCH

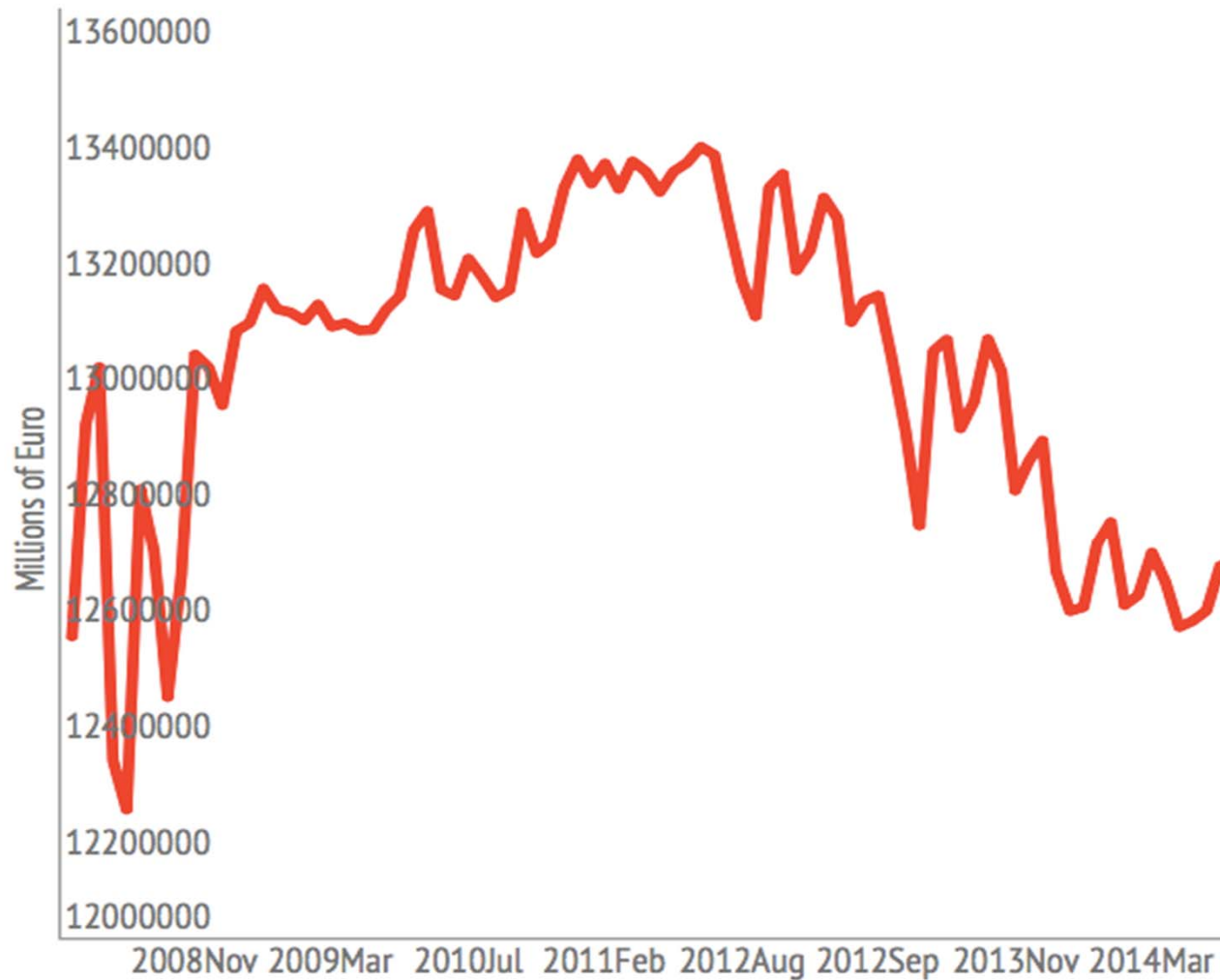
IT IS A STRONG REDUCTION IN CREDIT SUPPLY DUE TO
FUNDING STRAINS FOR THE BANKS
INCREASING CREDIT RISK DUE TO THE WEAKENING ECONOMY
INCREASE IN BANKS CAPITAL RATIOS

REDUCED CREDIT AVAILABILITY WILL DAMPEN ECONOMIC GROWTH STILL FURTHER

TO AVOID IT THE ECB IS PROVIDING VERY CHEAP LIQUIDITY TO THE BANKS

WITHOUT RESTORING CONFIDENCE GROWTH IS UNLIKE

EVOLUTION OF THE CREDIT FLOW TO THE PRIVATE SECTOR IN THE EUROZONE



Loans and securities

Source:
ECB



10.THE CRISIS IS ,OR HAS BECOME,A GOVERNANCE CRISIS AS WELL

THE POLITICAL RESPONSE HAS BEEN PATCHY,INADECUATED AND BELATED

THE GOVERNMENTS HAVE BEEN PLAYING POKER WITH THE MARKETS...AND THEY
HAVE LOST SO FAR

TOO MUCH “HISTORICAL” SUMMITS TO SAVE THE EURO

IN FACT ONLY THE ECB ACTIONS HAVE SAVED THE EURO..AND ONLY THE ECB CAN STILL
SAVE IT

A TOO MUCH PUNISHING APPROACH TO THE SOLUTION

INCREASING DEFIANCE BETEWEEN GERMANY AND THE SOUTHERN COUNTRIES

WHAT KIND OF AN EUROPEAN ECONOMIC MINISTER?



LOOKING AHEAD

GOING BACKWARDS IS VERY EXPENSIVE

GOING FORWARD REQUIERES A STRONGER
FEDERATION...AND IT IS VERY DIFFICULT DUE TO
THE LACK OD POLITICAL WILL

BUT AT THE END THE EURO WILL SURVIVE
BECAUSE IT IS TOO DAMAGING FOR ALL
TO GO BACKWARDS