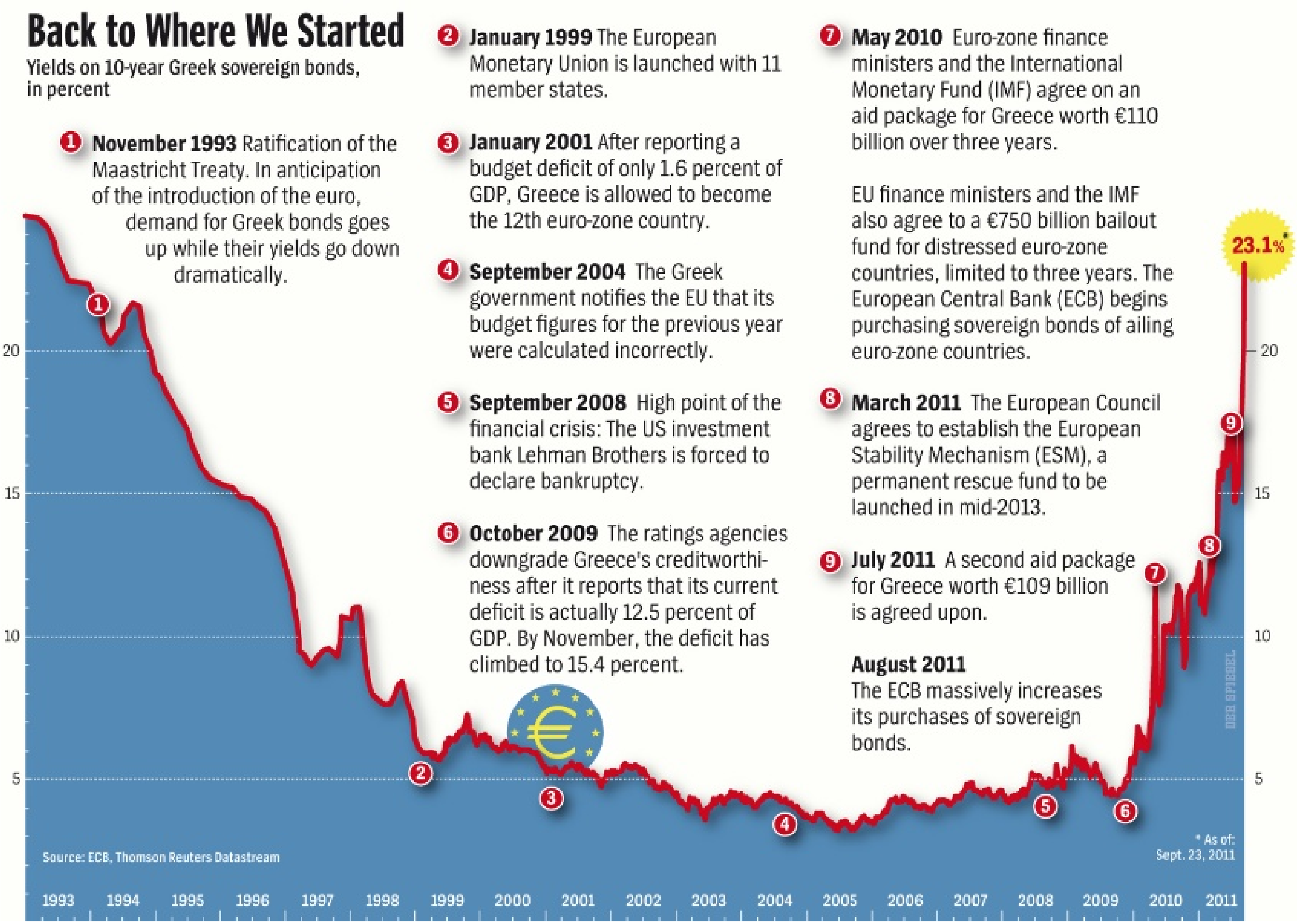
The Euro Crisis

What happened, Why, What are They Doing to Save the Euro?

What Happened? Why?

- **Who has been blamed for the crisis?**
  - Greece and the other PIGS
  - The EU (flawed economic governance of EMU)
  - The US (deregulation of financial services led to subprime crisis that spread to Europe)
  - The Market

What Happened? Why? The Greek Tragedy



Main question Raised by the Euro Crisis

- Is it a crisis that will propel the EU forward (e.g. lead to further integration) or a crisis that signifies the end of Jean Monnet’s dream of ever closer union?

Social Consequences of the Crisis: Questioning the Legitimacy of the EU

Spanish anti-austerity protesters burn EU flag in Madrid

Source: EU Observer, Photo: tom.tziros, 2012

Protesting the “dictatorship” of the Troika

Demonstrators in Athens on October 9th, 2012 protesting against the visit of Germany's Chancellor Angela Merkel.

Source: USA Today, Photo: Lefteris Pitarakis, AP

Source: Foreign Policy

Creation of the EU: Founding Treaties

- **Treaty of Paris** (1952): Created the European Coal & Steel Community (ECSC)
- **Treaties of Rome** (1957): Created the European Economic Community (EEC) and the European Atomic Energy Community (EURATOM)
- **Maastricht Treaty or Treaty on European Union** (1993)

The Maastricht Treaty and EMU

- In 1988, the European Council mandated a committee to study the feasibility of achieving monetary union
- Delors Committee devised detailed plan on how to achieve monetary union in 3 stages
- Stage 3 of EMU would be the irrevocable fixing of exchange rates, creation of a ECB, and adoption of a single currency by 1999 at the latest with countries that qualify according to the “convergence criteria”

The Convergence Criteria

- **Price stability:** the inflation rate of a Member State must not exceed by more than 1½ percentage points that of the three best-performing Member States in terms of price stability

- **Government finance:**
  - Goverment deficit must be below 3% of GDP
  - Government debt must be below 60% of GDP

- **Exchange rate:**
  - Membership in the ERM for 2 consecutive years w/out a break

- **Long-term interest rates (LTIR):** Should not exceed by more than 2 percentage points that of the 3 member states with the lowest inflation

The Introduction of the Euro

- **Qualified countries in 1999:**

  Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxemburg, the Netherlands, Portugal, Spain

  + Greece (in 2001)

- Introduction in non-physical forms: January 1, 1999

- Introduction in physical forms: January 1, 2002

Stability and Growth Pact (SGP) 1997 + revised in 2005

- **Government finance:**
  - Goverment deficit must be below 3% of GDP
  - Government debt must be below 60% of GDP

Preventive arm:

- Member states submit annual stability programs
- Early warnings by Council to prevent occurrence of excessive deficit
- Policy advice by Commission

Dissuasive arm: Excessive Deficit Procedure (EDP)

- The EDP is triggered by the deficit breaching the 3% of GDP threshold of the Treaty
- The Council sends request to correct the excessive deficit to the member state within a specific time frame
- Noncompliance can lead to sanctions (fines)

Problems with Implementation of Fiscal Rules of SGP

- Germany and France violated its rules with no consequences in 2003 (no sanctions applied)

- Today, 21 of the 27 member states are in the excessive deficit procedure (down from 23 since June 2012)

What are They Doing to Save the Euro?

1. **Reinforcement of Fiscal Rules**
   - More stringent rules
   - Adoption of EU fiscal rules into national law
   - Increase implementation through sanctions

2. **Creation of permanent bailout fund: Treaty on the European Stability Mechanism (ESM)**
   - Effective lending capacity of 500 billion euros

3. **Creation of a Banking Union**

Reinforcement of Fiscal Rules

The Six Pack

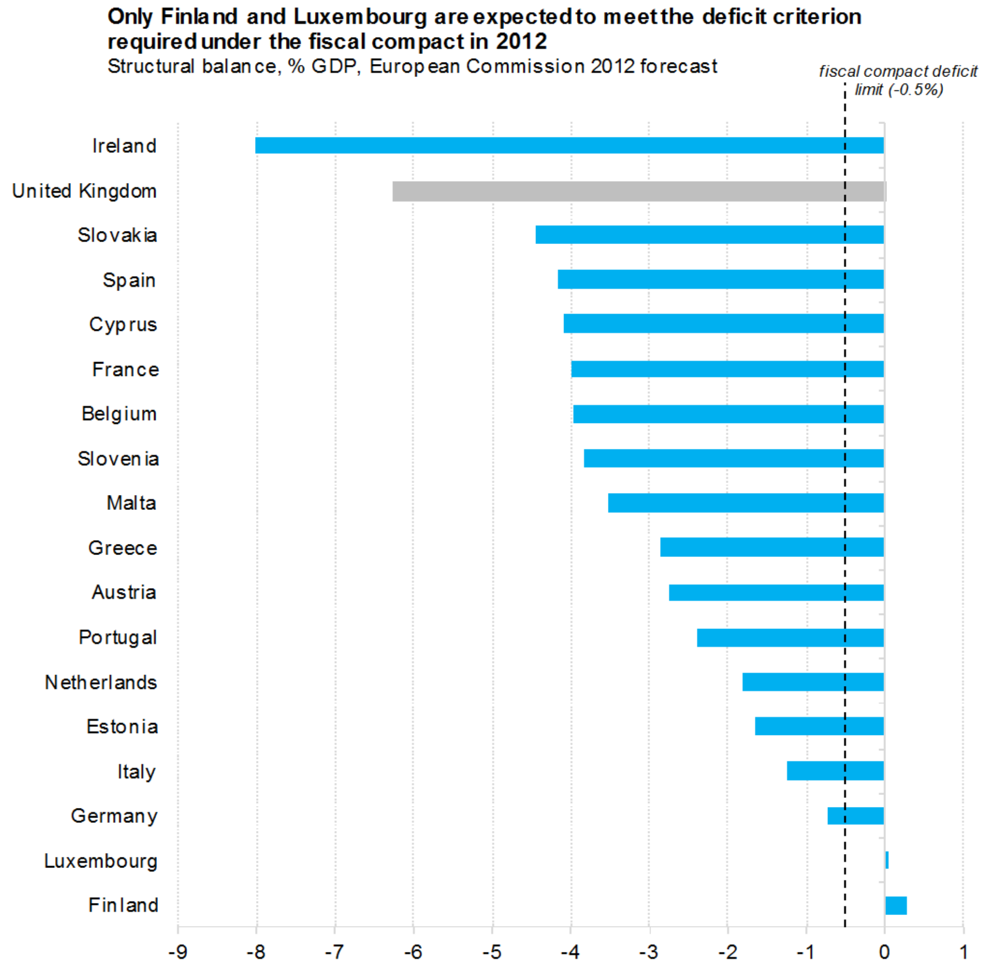
- EU secondary law (December 13, 2011)
- Excessive Deficit Procedure can be launched because of member state’s public debt <u>not just its deficit</u>
- Sanctions for not correcting debt or deficit (equivalent to 0.2% of GDP in the form of deposit or fine)
- Reversed Qualified Majority Voting Procedure to apply sanctions

Reinforcement of Fiscal Rules

Treaty on Stability, Coordination, and Governance

- Signed by all EU members except the UK and Czech Rep
- Will enter into force after ratification by at least 12 members
- Fiscal part of the TSCG is referred to as “the fiscal compact”
- New budget rules: lower limit of *structural* deficit (not general deficit), 0.5% of GDP to be implemented in national law
- European Court of Justice may impose financial sanction (0.1% of GDP) in case of failure to properly implement new budget rules in national law

More Austerity Required?



Source: UK Parliament, Economic Policy and Statistics Section

Other Proposals

- Proposal for stronger surveillance of member states' budgets in the euro area

- Proposal for stability bonds or eurobonds