

JOHN RYAN (ed.)

Towards a Resilient Eurozone

**Economic, Monetary
and Fiscal Policies**

Peter Lang

Introduction

This book discusses monetary and fiscal policies needed for European Monetary Union (EMU) to function properly. As in this matter the view from Germany is fundamental, this book offers a particular German perspective that should stimulate discussion and lead to more effective strategies for policymakers from all sides of this debate.

John Ryan and John Loughlin, in their chapter on 'Historical Monetary Unions: Lessons for the Current Eurozone Crisis', examine three historical monetary unions: the Latin Monetary Union (LMU), the Scandinavian Monetary Union (SMU), and the Austro-Hungarian Monetary Union (AHMU) in an attempt to derive possible lessons for the EMU. Special attention is paid, in particular, to the importance of economic and political integration in the success and failure of historical monetary unions, with the goal of shedding light on the fraught question of whether sustained successful monetary union is possible without high levels of economic convergence in the common currency area and indeed fiscal and banking union. The chapter further discusses the political and institutional aspects and whether a federal set of arrangements is necessary in order to sustain monetary union successfully.

'Towards a resilient EMU? The German inspired response to the Euro crisis assessed' by Lothar Funk examines the emergency measures and 'rules-of-the-game' changes which were driven by particular German ordoliberal economic based ideas, although these measures and changes were seen as too pragmatic by many German economic experts. A comparison of various assessments of progress towards a more stable Eurozone by international institutions and the European Commission with the German-inspired crisis strategy demonstrates traditionally different views especially regarding the question of rebalancing. The Grand Coalition federal government consisting of Christian Democrats (CDU/CSU) and Social Democrats (SPD) will stick to the German mantras of fiscal consolidation and price stability being of prime importance and of not combining national control

over fiscal policy with mutualization of sovereign debt. Moreover, there is a consensus that structural causes of the crisis must be further corrected even if details of how the assignment of tasks in order to achieve a better economic performance differ among different groups of economists, on the one hand, and between many economists and the government, on the other hand. It remains to be seen if Germany accepts responsibility to create a more growth-orientated budgetary and economic policy, which has been rejected until the worsening of the conditions of the German economy that became obvious only in October 2014. The chapter will also assess existing 'Euro-myths' (such as that the Euro is fundamentally a political project only) and will show that the step-by-step approach adopted as a strategic response in a simple game-theoretical sense can explain many actions taken during the crisis.

Michael Wohlgemuth in his chapter asks 'Is Germany's Current Account Surplus 'Unfair'? With German exports reaching record highs, the German 'business model' has come under attack from Washington, Paris and Brussels. Germany is held responsible for imbalances in the world economy and in the Eurozone. But are the allegations justified? Has Germany really been profiting unfairly from the common currency? What are the reasons behind Germany's current account surplus? Is it likely to stay? Would boosting imports in Germany really help the peripheral economies in the Eurozone?

Germany's long standing surplus prevents a decline of the Euro exchange rate, making the periphery's adjustment harder. But there are also plenty of other factors which influence the Euro, including but not limited to actions of other central banks (notably the Fed weakening the US Dollar) and the capital flight towards Germany as a 'safe harbour'. Also, while Germany may have previously been the flip side of other countries deficits, these deficits are now getting smaller (mostly due to less imports from periphery countries during recession) and Germany has maintained a surplus by trading with non-Euro countries.

'After Austerity: Lessons from the Spanish Experience' by Sebastián Royo examines the Spanish economy between 1996 and 2007, which was one of the fastest-growing and most successful economies in Europe. This success, however, came to a halt in 2008 and Spain is still suffering a very

painful economic recession. While the global economic crisis was a significant contributing factor in this downturn, domestic imbalances largely help account for the current economic problems. The Spanish government responded with a severe austerity programme, which has had dramatic economic and social consequences. The chapter will explore the consequences of austerity and draw some lessons from the Spanish experience.

Heribert Dieter and Maria Krummenacher, in 'Maastricht 2.0: Alternatives for Monetary Union beyond the Centralization Fetish', argue that beyond the centralization fetish the continuing financial crisis in some member countries of the Eurozone has intensified the debate about reforms of the monetary union. Whilst the crisis appears to have been resolved, the structural difficulties of the Eurozone remain unresolved. The original architecture of the Treaty of Maastricht did not prevent the outbreak of the crisis and thus has to be revised. The two alternatives suggested by the proponents of deeper integration – either deeper integration regarding monetary and fiscal policy, or a return to antagonistic, national policies – are far from inevitable. By contrast, it is possible to make the monetary union more crisis-proof while at the same time giving the European nations a high degree of responsibility for their own economic development. The frequently cited assertion that transferring – i.e. centralizing – hitherto national competencies to the European level would make fiscal policy and financial regulation easier to manage does not convince. That approach ignores the downside of centralization. Far-reaching centralization may result in new problems and will weaken, not strengthen, the economic dynamism of the EU.

Jacob Kirkegaard, in 'Closer Fiscal Policy among Eurozone Members', explains the progress made to date and future prospects for one of the key missing components of EMU, namely closer fiscal policy integration in the Eurozone. It does so by initially separating the issue of European fiscal integration into two distinct categories: short-term fiscal integration directly related to emergency crisis stabilization measures (e.g. bailouts); and longer-term fiscal integration associated with ongoing fiscal transfers among Eurozone members through permanent constantly operating institutions (e.g. supra-national budgetary institutions in the Eurozone). Optimal currency area (OCA) theory and the focus of the earlier Werner

and Delors reports are evidently on the latter type of fiscal integration. This chapter draws also on the historical experiences of the United States in its analysis of the Eurozone.

The final chapter by Clemens Fuest, Mathias Dolls, Dirk Neumann and Andreas Peichl on 'Fiscal Integration in the Eurozone: Economic Effects of Two Key Scenarios' examines the redistributive and stabilizing effects of two scenarios of fiscal integration in the Eurozone, namely the introduction of a joint tax and transfer system that replaces 10 per cent of national systems, and of a system of fiscal equalization that equalizes 10 per cent of differences in taxing capacity. Based on the European tax-benefit calculator EUROMOD and representative household micro data for the current seventeen Eurozone member states, this conceptual experiment shows that a joint tax and transfer system would only lead to moderate gains in terms of stabilization while redistribution would flow especially towards the Eastern European member states. In contrast, a fiscal equalization mechanism that redistributes revenues across countries could even lead to destabilizing effects.