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The Maastricht Treaty at Twenty: A Greco-European Tragedy?

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Abstract

Since 2010, the financial crisis has raged across Europe, taking down governments of several members of the euro-zone in the process. Despite strong pressure for reform, and many meetings of heads of state, the problems are far from over. The crisis has been widely represented as a sovereign debt fiasco and a failure of fiscal policy by five peripheral member states (Greece, Portugal, Spain, Italy, and Ireland). However, the real causes of the predicament of the euro-zone are more complex. A satisfactory understanding of the crisis is only possible if we distinguish among four phases: background factors, including structural flaws in the original design of the Maastricht Treaty; capital flows and fiscal deficits; dynamics of divergence, especially regarding competitiveness; and the crisis dynamics. In this contribution we identify three sets of factors — i.e., market spillovers and policy externalities, insufficient information related to the management of risk, and perverse incentives related to the configuration of rules

and institutions — that may lead to inefficient international outcomes in the environment of structural interdependence and full capital mobility, address how policy coordination can improve the results, explain how the euro-zone crisis developed, and explore a number of possible solutions.

Key words:

Euro-zone crisis fiscal deficits market spillovers policy externalities Stability and Growth Pact

Notes

1. We use the acronym GIIPS.

2. For example, see Robert O. Keohane's After hegemony (1984) for a seminal treatment of the role of cooperation in international relations theory. For theories of coordination, see Richard N. Cooper, The economics of interdependence (1968) and Economic policy in an interdependent world (1986). In this piece, we use the terms cooperation and coordination interchangeably. The first term is prominent in political science; the second in economics.

3. We hasten to add an important qualification, namely that cooperative behavior may not be necessary for the realization of gains. It is possible, though we think unlikely, that unilateral action leads to Pareto superior outcomes. It is also possible, and much more likely, that unilateral action can maximize the welfare of a powerful country while harming the welfare of a weaker country. This result may be stable but it is not Pareto superior.

4. For example, trade among countries with well developed pollution and patent laws will not experience the same level of externalities as two countries with weak pollution and patent laws.

5. Cooper quickly acknowledges that this definition differs from our notion of risk in games of chance, where the probability distributions are known, even if the particular event is not.

6. Article 121 of the TEU specifies the five convergence criteria. First, the inflation rate of participating countries of Stage III must be within 1.5 per cent of the average of the three EU countries with the lowest inflation. Second, the long-term interest rates should be no more than 2 per cent of the three countries with the lowest interest rates. Third, the national currency's exchange rate would have to be kept within the normal fluctuation margin of ERM II (plus or minus 15 per cent) of the EMS. Fourth, the national budget deficit must be lower than 3 per cent of GDP. Fifth, the national debt must not exceed 60 per cent of GDP.

7. See Figure 3, 'Credit growth to the private sector and average current account levels', in Wolff (2011, 3).

8. The Socialist Party won general elections in October of 2009. Soon after that, Papandreou admitted that Greek debt was substantially higher than reported earlier. In January 2010, the EU revised upward estimates of Greek debt from 3.7 per cent of GDP to 12.7 per cent.

9. For example, if one looks at nominal compensation per employee relative to a sample of 15 other EU countries, Ireland score is very high. However, we readily admit to being puzzled by the Irish case.

10. Austria's performance is just behind Finland's by a small margin but Finland is slightly behind Austria in terms of the competitiveness indicator. See Marzinotto, Pisani-Ferry, and Sapir (2010, 7).

11. The major provisions of the new fiscal compact for the single currency area included: Euro-zone members should keep their annual structural deficits below 0.5 per cent of GDP and their overall deficits below 3 per cent of GDP; states that exceed deficit limits would be subject to automatic penalties although they could be overridden by a qualified majority voting; Euro-zone members would be obliged to submit their budgets to the European Commission for approval; While the existing EFSF will remain active until mid-2013, the ESM, the euro-zone's permanent bailout fund, will enter into force in July 2012. The two funds will have a combined funding capacity of up to 500 billion euros; Euro-zone and other EU states will provide up to 200 billion euros in the form of bilateral loans to IMF to help it tackle the crisis.

12. The new rules of the Six Pack were first applied to Hungary on 11 January 2012. Concluding that Hungary had not made sufficient progress towards a timely and

sustainable correction of its excessive deficit, the Commission proposed to the Council to move to the next stage of the EDP and recommended that the Council decide that no effective action had been taken to bring the deficit below 3 per cent of GDP in a sustainable manner.

13. The TSCG will enter into force once it is ratified by at least 12 euro area member states. Its target date is 1 January 2013. Since it is not a regular revision of the EU Treaty, the so-called ‘repatriation clause’ commits the EU to take steps to incorporate its substance into Union law five years after its entry into force.

14. Ireland is of course not a ‘southern’ country but it is generally included among the countries on Europe’s periphery.

15. According to the Eurostat (the EU’s statistics office) news release on 2 July 2012, euro-zone unemployment has risen to its highest level (11.1 per cent in May 2012) since the euro was introduced. The seasonally adjusted unemployment rates for GIIPS and Germany in May 2012 are as follows: Greece (21.9 per cent in March 2012), Ireland (14.6 per cent), Portugal (15.2 per cent), Spain (24.6 per cent), Italy (10.1 per cent), and Germany (5.6 per cent).

16. In this regard, the decision on 29 June 2012 at the European Council meeting on a ‘Compact for Growth and Jobs’ is a welcome progress, since it indicates European leaders’ recognition that persistent low growth and macroeconomic imbalances, along with the sovereign debt crisis, are slowing down economic recovery and creating risks for the stability of EMU, Nonetheless, more resolute actions and practical measures need to be taken to boost the crisis-hit countries’ growth and employment and to strengthen their competitiveness.

Source: Unknown Repository

The Euro's Never-Ending Crisis

Source: Current History

Europe after the crisis: less or more role for nation states in money and finance?

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