

## **EU financial and debt crisis**

**Briefing paper  
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### **Developments in June**

Developments in June demonstrated again that Greece continues to be in the centre of attention of EU political leaders. Election in Greece resulted in the speedy creation of the government that promised to continue with domestic efforts enabling continuation of financial flows from the rescue funds to the struggling Greek economy and thus averted immediate speculations about Greece leaving the Eurozone. June brought to the attention also the situation in Spain, which became the next country officially requesting assistance of the EU financial rescue mechanism.

Although the EU political leaders put over recent weeks still significant attention to the situation in Greece, the gradual stages of the crisis confirm that the root cause of the crisis is not necessarily linked exclusively with the situation in one country. Irregularities of the financial and taxation system in Greece have contributed without any doubt to the massive extent of the difficulties EU has to face nowadays with not a small share. However, along with that the EU has to face a challenge of more systemic nature. In the core of it are growing imbalances in the EU internal market. These include growing gap in the economic performance of the countries of the EU periphery and the EU average demonstrated in particular in trade imbalance, and nonexistence of an efficient corrective mechanism for addressing these imbalances, the lack of fiscal instruments which would effectively accompany monetary unification in the Eurozone and divergence of the national economic policies at the level of EU Member States.

The crisis does not have a single root cause which would be possible to address with a single, even if decisive measure. Recent developments confirm an assumption presented at several occasions by economic experts (e.g. <http://varoufakis.files.wordpress.com/2010/11/modest-proposal-3-0-may-2012-without-rebalancing-mechanism.pdf>) that the crisis can be effectively tackled only by a coordinated series of political decisions, which will address at the same time different facets of the crisis, in particular the need of fiscal discipline,

stimulation of necessary investments and healing of an ailing banking sector. The crisis needs a coordinated action not only of EU member states; it has to be a coordinated action involving several sectors of policies.

### **EU Politics**

EU summit in June was 19<sup>th</sup> meeting of the EU political leaders since the crisis erupted in the beginning of 2010. To most of these summits have been attached significant expectations and in the run up to them, they have been described as 'important' some of them even 'decisive.' However, none of these summits have been able to provide a sign of political authority and generate the decision which would effectively address the crisis. All attempts of this kind have been short lived and optimism they eventually generated did not last for more than couple of days. One of significant outcomes of such a development is losing trust of the population towards the EU, as well as, more generally trust of the electorate to the European political elites. This has been with increasing clarity demonstrated by several recent opinion polls in a number of EU member states. One of the worrying outcomes of the crisis is growing distancing of the population from the EU project. It is to be noticed rapidly growing number of EU member states in which prevails negative attitude of the population towards the Union over those who are ready to demonstrate they support for it. Although the President of the European Commission J.M.Barroso admitted at several occasions that the crisis put in the centre of attention the trust towards the Union ( e.g. annual State of the Union speech to the European Parliament, [http://ec.europa.eu/news/eu\\_explained/110928\\_en.htm](http://ec.europa.eu/news/eu_explained/110928_en.htm)) the EU political elites has not been in position by now to avert this negative trend.

### **Consequences of the crises**

Social impacts of the crisis, in particular in the most affected countries of the EU put continual pressure on population. The crisis gradually raises an increasing number of questions about functionality and sustainability of European social model. One of the guiding principles that have driven the tone of by now presented political responses to the crisis has been *socialising of private losses*. The politics has allowed creation of banks, which are no more manageable. At the same time economies are dependent on private banks. Their further functioning has been alas declared as the condition *sine qua non*. In such a situation their debts have to be healed and the easiest solution has been found in the pockets of tax payers. They have to provide funds for it. To what extent is this approach fair and just, what is the nature of accountability between private and public and to what extent precisely this approach contributed to growing an alarming gap between wealth and poverty has to be asked.

To the impacts of the crisis has to be counted along with social impacts and loosing trust toward the EU equally the raise of political extremism. In France, a third of the electorate recently voted for a far-right or a far-left candidate for the presidency. In the Netherlands and Germany the far right and the far left are

running first and second in the opinion polls. In Austria, the far right are at nearly 30 per cent in the polls.

### **EU summit**

Outcomes of the EU summit in June 2012 produced more optimism than any other summit since 2 years. The President of the European Council in cooperation with Presidents of the European Commission, the European Central Bank and the Eurogroup outlined a plan for a coordinated EU action comprising a combination of strengthened budgetary coordination, creating an effective supervision of banks and ensuring sufficient mechanisms for promoting sound economic growth and employment.

In elaboration of the submitted scheme the summit has been labelled as the one that achieved the breakthrough towards creating a banking union. One of the crucial phrases of the outcomes of the summit is an affirmation of political leaders that 'it is imperative to break the vicious circle between banks and sovereigns.' The summit decided to establish a single banking supervisory mechanism run the by the European Central Bank and to provide the ESM with the possibility to inject funds into banks directly instead of involving into this mechanism national governments. The summit agreed to build up a stimulation package of 120 bills, which should help with funding of investments guaranteeing economic growth and employment.

The summit agreed on strategic political decisions. Concrete proposals for implementation of these decisions will be submitted by the summit in December 2012.

### **Challenges**

The summit along with the major political decisions made sufficiently clear that a number of challenges EU will need to solve in the coming period of time is not diminishing. First of all it is now clear that the tone which has guided the talks about European integration in recent years has definitely changed its substance and character. If in the recent past the European integration has been mostly limited to its geographical aspects and to the talks about finality of the EU external borders. The content of the EU integration talks has now very different meaning. The simple conclusion is that the crisis in the EU is not anymore about economic functioning of the Union. It is about its substance and character. The crisis has revealed the urgency for clarification of the links and mutual dependencies between monetary, fiscal and political integration in the Union. It has become clear that integration process in Europe has achieved such a point that there are ahead only two rational options. Either to continue with integration towards closer political Union, or to step back, allowing the loosening of the existing links inside the Union, and clearing the way for some members of the Eurozone to break away. This would be most likely followed by further

disintegration, accompanied by unpredicted economic difficulties, deepening of the crisis and political chaos.

The major challenge of the Union though is that the process of further political unification requires democratic legitimacy, which is in times of diminishing support of population in the Union missing. There is little desire for political union from the peoples of Europe and moves towards EU control over taxes, budgets and other core state competences. In a Pew Research Centre poll published last month, only one-third of respondents in the eight countries surveyed believed European economic integration had strengthened their country's economy. And in another study carried out by YouGov-Cambridge in March, 68% of Germans, 70% of French and 89% said that tax rates and national budgets should be controlled by national governments, not by the EU. What seems to be an economic and political necessity stands in such way in a clear opposition to the wishes of electorate.

To win peoples' minds and inspire them again for the European project seems now a matter of necessity more than ever. If European project has to continue, people need to be re-assured that in spite of justified doubts towards recent performance of political elites in Europe, in spite of many empty words and undelivered promises the European project deserves their trust and support.

In finding inspiration for it we should not limit our look on so often highlighted prosperity and competition as highest achievements of the integration process. Original aims of the Union have been formulated in different words, putting forward cooperation, peaceful and respectful coexistence and solidarity. Although cooperation is sometimes difficult and solidarity not unquestionable, they deserve to be pursued. Even if it is in the time of crisis and in the moments, when difficult decisions need to be taken.

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