BACHELOR THESIS

COSTS AND BENEFITS OF THE EURO IN SELECTED EMU COUNTRIES:

THEORY AND PRACTICE

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AJDA KOVAČ
AUTHORSHIP STATEMENT

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LIST OF ABBREVIATIONS

sl. - Slovene
ECB - (sl. Evropska centralna banka); European Central Bank
ECU - (sl. Evropska denarna enota); European Currency Unit
EMS - (sl. Evropski monetarni sistem); European Monetary System
EMU - (sl. Evropska ekonomska in monetarna unija); European Economic and Monetary Union
ERM - (sl. Evropski mehanizem deviznega tečaja); European Exchange Rate Mechanism
ESM - (sl. Evropski mehanizem za stabilnost); European Stability Mechanism
EU - (sl. Evropska unija); European Union
EZ - (sl. evroobmočje); Eurozone
IMF - (sl. Mednarodni denarni sklad); International Monetary Fund
UK - (sl. Združeno kraljestvo); United Kingdom
US - (sl. Združene države); United States
SGP - (sl. Pakt za stabilnost in rast); Stability and Growth Pact
INTRODUCTION: THE RESEARCHED ISSUE RELEVANCE, RESEARCH QUESTION, METHODOLOGY, AND HYPOTHESES

The focus point of the thesis is to examine the costs and the benefits of the monetary integration according to the specifics of the Eurozone (hereinafter: EZ) countries. The countries differ in historical, economic, political, and social aspects, and hence, different theories, rules, and expectations apply. Therefore, due to the respective differences in the nature of the EZ countries, different benefits from monetary integration are expected. The research question pertains to these benefits, and after having been identified, to whether they perform as well in reality vis-à-vis theoretically expected costs.

The topic is relevant from many angles. First, it has been discovered and academically confirmed by Ricardo’s Comparative Advantages Theory that the national income increases with trade. The benefits thereof have encouraged the countries to engage in trade and, soon after, international trade has emerged. However, especially with the fast-paced degree of global integration in the last 50 years, trading risks have become apparent, affecting various economic agents. One of the most prominent is the exchange rate risk. Second, obstacles to international trade, such as exchange rate risk, have in turn prompted the creation of ways that forgo the respective risk but keep the benefits. Therefore, exchange rate risk has acted as the leading, or at least the most apparent driver of the local monetary integration.

On the other hand, and third, this very solution has brought about other drawbacks that the facing countries need to juxtapose with its benefits in order to assess the profitability of integration. Clearly, monetary integration affects several major aspects of the countries seen as economic structures - such as their financial, borrowing, corporate, export and other standings - but also as political, social and historical entities. Hence, the question arises whether integration, given its drawbacks, is sufficiently beneficial. Namely, the underlying benefits of monetary integration are the driving engines of the European Union’s (EU) economic, political, and social integration. Finally, such questions are regularly addressed in the media, but seldom answered in a structured and justly argued way. Namely, only after the benefits are identified accordingly given the country specifics, along with realistic outcomes and hopes for the future, can political agents start to form opinions and expectations from the European monetary integration in the first place, and well-founded political interests for (dis)integration can begin to form.

Hence, the research question concerns country specifics and the expected benefits in theory vis-à-vis those displayed in practice. I hope to answer questions such as: “For the Netherlands and similar countries, do the benefits of being in the EZ outweigh the costs?” , “Is the rise of protectionist and nationalist political support based on fair arguments and can this potentially help shape a better Europe?” and “Given the economic (losing monetary and some fiscal independence), political (losing national autonomy), and social (brain-drain) costs, are the euro-associated gains sufficient to proceed with euro integration for the South EZ countries?” and similar.

To arrive at conclusions, I will consider the relevant monetary and exchange rate system theories. These will present the theoretical benefits and limitations of monetary integration, acknowledging its pertinence to several levels: economic, political, and social. Further, the integration is reviewed in the historical context to gain the perspective and comparative insight into the current international
monetary arrangement. Lastly, the theoretical part analyses the current European monetary integration, i.e. the European Economic and Monetary Union (EMU), using the theoretical framework and historical lessons for its multi-angled assessment.

The thesis gives greater weight to theoretical analysis, yet recognises the empirical urgency for policy conclusions. Thus, the study of Alessandro Gasparotti and Matthias Kulla from the Centre for European Policy (CEP), which was conducted in February 2019 and posed a nearly identical question of euro related gains and losses for EZ members, is employed in pursuit of evaluating theoretical expectations against the empirical reality in order to arrive at tangible conclusions for selected EMU countries, i.e. to verify whether theory complies with practice. However, it should be noted that the costs and benefits of the EZ are evaluated only through the relation between the realised GDP per capita vs its hypothetical non-EZ value. Therefore, this broad issue with substantial implications is analysed through a fairly narrow metric, which in addition to methodological critiques constitutes a shortcoming of the respective study. Finally, only countries with a satisfactorily long EU membership can be analysed in terms of the euro effect on prosperity for distinction purposes from the notably significant EU effect on growth, which in the case of post-2004 members still persists. Nevertheless, the final data should provide a clearer state of affairs.

Technically, qualitative and quantitative methodological approaches cover parallel complementary analyses. The following prevail: literature analysis, historical and normative analysis, data analysis, comparative insights, and the axiological method.

Furthermore, different members have different incentives for joining the EZ. Costs tend to be similar, but not every type of country benefits in the same way or equally. Hence, specific gains are investigated according to specific country characteristics, whereby a distinction is made between EZ South and West. Specifically, I formed the following hypotheses:

I. South EZ countries, such as Italy and Spain, benefit from the EZ more than they lose, since their economic perspectives are better as members. Lower expected inflation as monetary instruments are controlled by the credible European Central Bank (ECB), followed by lower interest rates and limited exchange rate risk, all contribute to higher economic growth.

II. West EZ countries, such as Germany and the Netherlands, benefit from the EZ more than they lose as a result of stimulated trade in the EZ area and thus increased exports into other member states, making their current accounts positive, along with increased savings and investment. However, this leads to discrepancies and tensions in the EZ as an economic, as well as in the EU as a political structure.

III. Political reasons, and not economic, are key to the admission of South EZ countries, such as Greece, into the European monetary integration along with the West countries; hence, economic discrepancies, such as country political risk, manifested in higher government bond interest rate, prevail even in the event of conditional economic convergence criteria.

Last, the thesis analyses monetary integration generally and specifically, a goal which is served through the following thesis structure: the first and second chapters are theoretical, whereby the former focuses on the general exchange rate theories, discerns the theoretical costs and benefits of specific monetary integrations, and evaluates them in a historical context. The latter presents the monetary status quo in Europe through an economic, political, and social dimension. Next, the third
chapter is empirical, delivering the results of the Gasparotti and Kullas (2019) study. Finally, the last chapter connects the theoretical expectations with empirical reality, assesses the hypotheses validity, and discusses the perspective research implications.

1 THEORIES OF MONETARY INTEGRATION: BENEFITS, LIMITATIONS, AND HISTORY

To evaluate the success of the EZ as a monetary integration, we must first define the theoretical basis within which it can be further analysed. In this way, we can discern the theoretical benefits and limitations, grasp the foundations on which it was built, and finally form fair expectations for its practical functionality. Thus, this chapter looks at monetary integration theories and associated benefits and limitations. It commences by reviewing the relevant theoretical framework to monetary integration research, such as the Robert Mundell’s Theory of Optimal Currency Areas and the Impossible Trinity. Further, as countries face a fixed exchange rate under the monetary union, its respective costs and benefits are analysed. Last, it reviews the history of monetary integration within the theoretical framework laid out in previous sections, creating the basis for a further analysis of the EZ as the current stage of integration.

1.1 The Optimal Currency Area

The essence of economic integration, which is the backbone of European integration but also connects nations politically, is its gradual deepening. According to Balassa (2013), the integration begins with the abolition of tariffs and customs, followed by their unification in relation to the rest of the world, and thus emerges the customs union. Next follows the common market, after which the integration reaches its last stage of an economic union with a common currency. However, entry is only worthwhile if there is evidence that the benefits of a membership in an economic monetary union outweigh the costs. For instance, full participation in a common market with minimum customs duties and a unified regulation, which acts as an international trade incentive, should outweigh the loss of part of the policy independence (Mundell, 1961). The costs of entry depend on how well the regional currency area coincides with the optimal currency area. In the respective theory, Mundell (1961) specifies that a prerequisite for the latter integration stage is deep harmonisation in several areas, particularly economic, political, social, and others, as only then external shocks are sufficiently correlated.

Furthermore, the second necessary mechanism of currency areas is a fiscal union (Cooper & Kempf, 2004). This component is necessary for the stability of a monetary union as it acts as its ‘back-up’ mechanism to facilitate the remaining economic and political discrepancies. Thus, the result is higher immunity to internal and external shocks which only a deeply integrated, coordinated, balanced, and converged union can overcome effectively. In other words, external shocks are symmetric (Rant & Fuhriman, 2017). Hence, political convergence is integral for economic functioning (Varoufakis, 2017).

However, the internal mechanics of an integration depends on its type, which in turn is determined by country priorities. Put differently, there are certain benefits and limitations deriving from the framework of a specific monetary integration. They are summarised by the impossible trinity.
1.2 The Impossible Trinity and its Implications

“The point is that you can’t have it all.”


The impossible trinity or the macroeconomic trilemma requires the countries to pick a combination of only two out of three generally desirable economic policies when forming their international monetary stance (Aizenman, 2010). The impossible three objectives are (1) monetary independence, (2) fixed exchange rate and finally (3) free movement of international capital (see diagram 1).

Diagram 1: The Impossible Trinity

Adapted from Pilbeam (2013).

It is impossible to pursue all three goals at once because of specific monetary mechanisms that take effect when already pursuing the other two (Aizenman, 2010). For instance, should a country already have monetary independence and free movement of capital, it cannot have a fixed exchange rate. Namely, any change in monetary policy will cause capital flows, which in turn will influence the exchange rate. Thus, it cannot be fixed. However, a country can impose capital controls i.e. sacrifice free movement of capital and thereby restrict capital flows, and the exchange rate remains fixed. Alternatively, it can give up monetary independence, thus obliging itself not to alter any variables which would make the exchange rate react to these shocks, such as the interest rate and currency in circulation.

To demonstrate the impossible trinity graphically, I employed the Mundell-Fleming model. This model builds on the Keynesian IS-LM Model by introducing the open economy dimension, summarised by a third balance of payments equilibrium (BP) curve (Obstfeld, 2001). Just like in the original Keynesian IS-LM Model, the model places interest rate on the vertical axis, and national income on the horizontal axis. The BP curve is used to depict the foreign exchange market or the balance of payments equilibrium, represented by the balance in its current account (Frenkel & Razin, 1987). This entails an economy is not undergoing any massive capital outflows, hence its exchange rate and international position are stable. Therefore, the model has three curves, where the IS curve depicts the goods market equilibrium, and the LM curve the money market equilibrium. Together, they represent the economy’s internal focus on its domestic goals, while the BP curve represents the
economy’s external focus in the international environment (Klaassen, 2018). The analysis is conducted for a small country with perfect capital mobility and fixed exchange rate, as are for instance the EZ member states. It should be noted that perfect capital mobility results in a horizontal BP line as the impossible trinity holds that any change in the domestic interest rate relative to the international interest rate results in massive capital flows and in order to restore equilibrium, national income would have to adjust infinitely (Pilbeam, 2013). In fact, the slope of the BP curve is a function of the degree of international capital mobility (Pilbeam, 2013). As a result, the interest rate of an economy with the above characteristics is equal to the international interest rate, as only this level of the domestic interest rate yields a balance of payments equilibrium.

Diagram 2: The Mundell-Fleming Model and the Impossible Trinity

Hence, the situation is as indicated by diagram 2. We assume the initial equilibria in all three markets. Consequently, the domestic interest rate equals the international interest rate (Klaassen, 2018). In order to demonstrate the country’s central bank monetary dependence, we assume that the central bank for example increases its money supply, which it is able to do in the case of monetary independence. The LM curve shifts to the right (arrow 1). This results in a short-term lower interest rate vis-à-vis the international level, and so results in capital outflows. In turn, this induces the domestic currency depreciation pressures. Since in a fixed exchange rate regime this is forbidden, the central bank must intervene so that it reduces the money supply by increasing the domestic currency demand, e.g. by selling domestic bonds. Hence, the LM curve returns to its initial position (arrow 2). Indeed, the central bank cannot manoeuvre the domestic monetary policy under combined fixed exchange rate regime and capital mobility (Mundell, 1961; Obstfeld, 2001), as illustrated in the above graph.

Clearly, the inability to pursue all three economic objectives has drastic economic policy implications (Obstfeld, 2001). Particularly, **monetary policy** is crucial for achieving macroeconomic goals such as inflation and economic growth (Pilbeam, 2013). Moreover, it is key for alleviating the degree of business cycles, the importance of which was acknowledged already when liberalism was only beginning to form in the 18th century with the ideas of the physiocrats, specifically Richard Cantillon, and later on fully developed by Joseph Schumpeter (Sušjan, 2006). Manipulating economic policies
in a sound and shrewd fashion results in facilitated recessions and prolonged prosperities, which means that it acts countercyclically (Hansen, 2003). In this way, recessions are restricted to spiral into depressions precisely due to the misuse of economic policies, as it occurred in the US in 1929 because of the then prevailing belief into the self-regulatory and self-equilibrating free market that was brought about by the marginalist revolution in the last quarter of the 19th century (Sušjan, 2006). Moreover, all the burden of this task now lies on fiscal policy only, and as the Tinbergen rule indicates, the number of economic tools must match the number of economic objectives, which can instantly become a problem when there are more of the latter, as is the case for every economy (Klaassen, 2018). Furthermore, as shown by Mundell (1962), monetary policy is best suited for external balance, while fiscal is best suited for internal balance. Lastly, not only can monetary dependence mean neutral monetary policy, it can also mean a monetary policy that works in contrast to the national economy aims. For example, the German reunification in 1990 signalled additional political risk to the financial markets, thereby increasing not only the German interest rate, but also the then common Exchange Rate Mechanism (ERM) rate for all members. However, for the UK which, at the time, was in recession, an increased interest rate was unapt (Klaassen, 2018).

Second, restrictions on capital flows are usually an omen sign to the financial markets and hence impede an economy’s access to capital and potential economic growth (Edwards, 2001). Undeniably, an investor is less likely to invest if there is high probability that he or she will not be able to collect the profit ceteris paribus. Finally, fixed exchange rate posits less uncertainty by excluding exchange rate variation from bond and stocks yields and thus signals stability to financial markets, along with involving central bank credibility benefits (Levy-Yeyati & Sturzenegger, 2001) and facilitating trade (Frenkel, 2003). These and further benefits, as well as costs (Flood & Rose, 1995; Obstfeld & Rogoff, 1995), are elaborated later on in the next chapter.

Moreover, the simultaneous pursuing of all three goals is linked to financial crises (Aizenman, 2010). The prime example is the Asian financial crisis in 1997 (Patnaik & Shah, 2010; see Aizenman, 2010 for more cases). Namely, the currencies of East Asian economies such as Thailand, Malaysia, Indonesia, and South Korea were pegged to the US Dollar, alongside allowing free capital mobility. However, their short-term interest rates were not coordinated to that of the US (Patnaik & Shah, 2010). As long as the US interest rates were lower, the capital inflows proceeded to boost their current account surpluses. However, as the interest rate ratio turned as a result of the increased US interest rate undertaken by the Federal Reserve at the outlook of the finishing early 1990s recession in order to supress the emerging US inflation, there were no barriers to stop massive capital outflows from the Asian countries (Moreno, 1998). The problem was exacerbated by the previously largely undetected problems of moral hazard and adverse selection that went unnoticed by the Asian financial intermediaries who amplified overinvestment, which resulted in the asset price bubble (Krugman, 1998). In the end, countries depleted their dollar foreign reserves in pursuit of defending their peg, and devaluations followed, the most notable of all being the collapse of the Thai baht in 1997, followed by many others, which depreciated to as low as 83% against the USD (Moreno, 1998). An essential argument in the large-scale bankruptcy declarations was that many short-term debt obligations of these countries were dollar denominated, which led to their substantial growth. In the end, the International Monetary Fund (IMF) interventions were required.

Emerging economies have resorted to pursuing all three goals at once in the aim to increase financial integration as well as maintain financial stability (Aizenman, 2010). However, as it turned out, only
two goals can be pursued. Thereupon, the question of the adequate combination for an economy arises. This depends on its characteristics and national objectives (Pilbeam, 2013). For instance, the EZ has monetary dependence and free movement of capital, but a floating exchange rate. Typically, most advanced economies will opt for these two, as well. Indeed, the combination is shared by the US, the UK, Japan, Switzerland, etc. (see diagram 1). In turn, the individual EZ member states do not have authority over their monetary policies, yet maintain fixed exchange rate and free movement of capital. Hong Kong is in the same position, whereby it pegs its Hong Kong Dollar rigidly to the USD and lets capital flow freely, together at the cost of monetary independence (Pilbeam, 2013). Further, China has a semi-pegged exchange rate and monetary independence, which requires it to impose capital controls (Hao, 2019). Moreover, as Pilbeam (2013) emphasises, the trilemma is particularly important for the developing countries, as already implied above. Therefore, they often peg their currency to some internationally stable currency in order to control inflation and ultimately keep currency value (Devarajan & Rodrik, 1991). Additionally, for long-term economic development, access to capital is crucial, thus they usually cannot afford to restrict capital flows. As a result, oftentimes they will give up their monetary independence. Examples of such economies in 2019 are, amongst others, Eritrea, Panama, and Cuba (Zucchi, 2019).

1.3 Costs and Benefits of a Fixed Exchange Rate

The exchange rate correlates with a vast array of variables, such as inflation, money growth, interest rates, and output (Flood & Rose, 1993). Therefore, the choice of an exchange rate regime is crucial for the functioning of an economy. The benefits and costs of a fixed exchange rate are examined in this section. In addition, it is worth bearing in mind that the extent to which costs and benefits manifest themselves in relation to each other is dependent on the characteristics of an economy, namely whether it is a developed, emerging, or a developing country (Husain, Mody & Rogoff, 2005).

First, fixed exchange rates promote international trade and investment (Frankel, 2003). As already implied above, floating exchange rate is seen as a source of instability, thereby discouraging international transactions and impeding economic growth ceteris paribus (Flood & Rose, 1993). However, Brada and Mendez (1988) offer evidence that greater risk associated with floating exchange rate is offset by the trade-reducing effects of restrictive commercial policies imposed by the countries with fixed exchange rates, and suggest that trade flows are higher between countries with floating exchange rates. In addition, Klaassen (2018) warns that while the exchange rate is fixed, real exchange rate remains unfixed. The latter is subject to inflation, which in turn is subject to other economic variables, such as money supply and inflation expectations, which is linked to central bank credibility. As such, competitiveness may still change and so the exchange rate risk persists. As summarised by Eun and Resnick (2007), a fixed exchange rate eliminates transactional exposure, but the operational exposure remains. Overall, however, the exchange rate risk is limited (Fratzscher, 2002). In addition, Pilbeam (2013) suggest that a fixed exchange rate regime necessities some degree of international coordination, which in turn should bring about benefits for all parties as it leads to a more stable environment for international trade and investment.

Similarly, in order to maintain the peg, other economic variables must be coordinated, one of them being inflation. Levy-Yeyati and Sturzenegger (2001) note that fixed exchange rates promote macroeconomic policy discipline via the increased credibility of policy makers, e.g. central banks.
Namely, by committing to the peg, national authorities are essentially binding themselves to lead a predictable and moderate monetary policy with convergent inflationary outcomes. In fact, the trade-off between disinflation and unemployment, as posited by the Phillips curve, decreases (de Grauwe, 1994). In other words, since the peg is usually to an internationally recognisable and stable currency, the domestic monetary policy is tied to that of the already established and credible central bank (Levy-Yeyati & Sturzenegger, 2001). Prior to the commitment, a nation is likely to follow an expansionary monetary policy since several cases exist for its desirability in the domestic economy. Pilbeam (2013) names elections and growth stimulation, and Mankiw (2016) and Romer (2012) the alleviation of the debt burden. However, after fixing the exchange rate, the authorities are incentivised to follow sound macroeconomic policy in order not to fail the peg and essentially inform the markets of their economic policy mismanagement.

On the other hand, Klaassen (2018) emphasises that in the case of the asymmetric shock, tied hands can promote too much rigidity, offer too few realignments, and just provide too little manoeuvre space for domestic economy operations. Therefore, pegs are more prone to banking and exchange rate crises (Husain, Mody & Rogoff, 2005). Moreover, Levy-Yeyati and Sturzenegger (2001) suggest that lower inflation comes at a cost of slower economic growth. Furthermore, they stress that in the light of increasingly global capital markets, floating exchange rate regimes offer more space for the necessary price adjustments and are thus better equipped to respond to external monetary and real shocks. On top of that, Obstfeld and Rodoff (1995) stress that the profound difficulty of maintaining the peg cast doubts as to its full use, and support their view with the 1992 Swedish and British crises and the 1994-95 Mexican collapse.

Finally, Pilbeam (2013) suggests that a floating exchange rate may yield a suboptimal level of an exchange rate. This can originate from generally two processes: ‘irrational’ speculation and uncertainty measures. First, by acknowledging some market inefficiency in the forex market (see Shiller, 1981 for stock market inefficiency), one realises that there may exist excessive risk aversion to hold certain currencies beyond the relevant fundamentals. Investors may exhibit biases by relying on past price information even though proven uninformative of future performance (Kendall, 1953). As a result, there may be inefficiency-justified risk premium on some currencies, or in other words, some currencies may be unjustifiably weaker or stronger (Pilbeam, 2013).

However, even rational speculators can produce an unfitting exchange rate based on the available information due to exchange rate uncertainty (Dornbusch, 1983). Namely, they can base their expectations on a defective model of price determination, which in turn creates a faulty exchange rate. Alternatively, the latter can be produced via the so-called Peso problem, which essentially holds that the formation of the exchange rate is influenced not only by the economic fundamentals, but also by their expected future estimates (Veronesi, 2002). Because of their upcoming nature, they can be inaccurate and set the exchange rate based on events that do not materialise, thus impeding the macroeconomic stability (Rietz, 1988). Third, the ‘rational bubble’ phenomenon can emerge (Blanchard, 1979). Essentially, even if investors realise the overvaluation of the held currency, they consider it will continue to appreciate so that they can realise capital gains of selling such an overvalued currency. With doing so, they hinder currency readjustment to a fair and efficient level, thereby aggravating the macroeconomic costs associated with it (Assnes & Liew, 2014).

On the other hand, free market proponents will instantly contend upon the above arguments that all facts considered, the market eventually determines the price more efficiently than the policymakers.
Indeed, there are many cases of exchange rate set at a rate suiting national interests as opposed to how fairly trading operations would have it (Economist, 2005). In fact, even if the policymakers’ interest is to have the exchange rate reflecting the relevant economic fundamentals, these can change over time, while the exchange rate remains fixed (Pilbeam, 2013).

1.4 Historical Overview: Search for Stability and Flexibility

In order to deem the current state of affairs in Europe lucid, one ought to review the factors that led to the formation of the EZ system. Namely, with perfect capital flows, monetary independence, and fixed exchange rate all simultaneously being favourable characteristics of an economy, I examine the factors that prompted the EZ to abandon the latter. In the past, however, that combination did not appear optimal in the region; yet, sensible reasons persist for the EZ to finally adopt the current combination. Additionally, it should be noted that in reality, using the Mundell-Fleming terminology, countries might not be capable of pursing internal and external balance at once. As such, countries prioritise only one, switching from the search for stability to flexibility (Klaassen, 2018). These are both desirable in the international monetary context, yet once again cannot be achieved simultaneously to their full extent. Thus, countries adjust their international monetary standing based on current economic reality to capture an apt balance between the two. With the above taken into consideration, brief history is presented in this section, as many international monetary reforms were proposed to address past monetary system issues (Pilbeam, 2013). Only after that can one fully understand the EZ systematically.

1.4.1 Monetary Arrangements until the Second World War: Gold Standard and Gold Exchange Standard

As trade revealed its benefits in the form of increased national income in the mercantilist and later classical economic eras from around 1600 to 1875 (Sušjan, 2006), grounds for a structured international monetary system emerged. Its establishment was facilitated by some important international monetary concepts already emerging in mercantilism such as terms of trade and balance of payments, the latter notably conceived by Thomas Mun and later upgraded by David Hume with his “specie-flow mechanism” (Obstfeld, 2001), and the “Cantillon effect” by Richard Cantillon (Sušjan, 2006). Despite that, the need for an integrated cross-country systematic arrangement was only formalised with the construction of the Gold Standard in 1870 (Eichengreen & Flandreau, 1997). The system demanded prices were fixed to gold quantity, which served as national reserves and provided stability both internally for controlled inflation and externally for international trade. However, the system smothered flexibility by limiting monetary expansion to support economic growth (Eichengreen & Flandreau, 1997). The latter became problematic in light of the First World War where monetisation was urgent to finance military, as well as the subsequent reconstruction, and thus provided substantial grounds for countries to prioritise flexibility over stability (Klaassen, 2018). With that, the 1914 to early 1920s war period was characterised by overall exchange rate instability and trade controls (Eichengreen & Flandreau, 1997).

In the 1920s, the Gold Exchange Standard prevailed, which was prompted by the need to stabilise the inflation that emerged from reckless monetary expansion due to the war period (Klaassen, 2018). The possibility to hold foreign exchange reserves alongside gold reserves was encouraged and
institutionalised for easier monetary expansion in order to accommodate economic growth (Eichengreen, 1987). However, upon the Great Depression in 1929, countries required liquidity and flexibility in order to address internal balance issues, such as unemployment, and events like competitive devaluations and trade restrictions effectively produced floating exchange rates and thus marked the end of the Gold Exchange System (Eichengreen, 1987). Again, countries prioritised internal balance, particularly battling widespread unemployment, over external balance. Instability and disintegration persisted throughout the Second World War, economically and politically.

1.4.2 Monetary Arrangement from the Second World War until 1973: The Bretton Woods System

“It has been our task to find a common measure, a common standard, a common rule acceptable to each and not irksome to any.”

Source: John Maynard Keynes (1944); Sivramkrishna (2016).

These recurrent focus switches necessitated a monetary system that managed to maintain both internal and external balance. Indeed, policymakers produced the Bretton Woods system, which was to ensure stability and flexibility through the following three mechanisms (Mrak, 2002): (1) fixed but adjustable exchange rates, thereby promoting discipline with some degree of flexibility, and the establishment of (2) the International Monetary Fund (IMF) and (3) the International Bank for Reconstruction and Development, which later became one of the five pillars of the World Bank. The exchange rates of 44 allied nations were fixed to the USD with a +/- 1% band, and the USD in turn was fixed to gold with USD 35 per ounce gold, introducing the confidence in the system (“the dollar was as good as gold”, Eichengreen, 2010). Additionally, the IMF was to aid in the case of temporary balance of payments disequilibria, and if permanent, there was the possibility of a re- or devaluation (Mrak, 2002).

In this way, the Bretton Woods system was asymmetric, whereby it positioned the USD at the centre of the system and so the US stability at the centre of the system stability (Eichengreen, 2010). Indeed, asymmetry proved problematic as the US began experiencing persistent budget deficits from the 1950s, leading to large dollar reserves held by foreign central banks which gradually started to exceed the US gold reserves (Triffin, 1960). The perceived dollar overvaluation was exacerbated by the expansionary monetary policy led to finance the Vietnam War in the 1960s and other fiscal spendings (Noël, 2019). Dollar speculation attacks followed, an answer to which materialised in 1971, when the US president Richard Nixon announced two measures: the suspension of dollar-gold convertibility and a 10% tariff on US imports (Noël, 2019). In response to these protectionist measures, the Smithsonian agreement was reached in the same year to abide by market pressures. It held devaluating the dollar against gold at USD 38 per ounce gold; revaluing other currencies by an average of 8%; and increasing the fluctuation margin to +/- 2.25% (Garber, 1993). These measures were aimed at restoring the US competitiveness, but proved “too little too late” (Pilbeam, 2013). Indeed, the US balance of payments further deteriorated, and the European currencies began to adopt the Snake in the Tunnel regime, gradually abandoning the USD peg by 1973 (Higgins, 1993). This stood in stark contrast to the Bretton Woods system and effectively ended it.

The Bretton Woods demise can be boiled down to two problems: (1) the liquidity vs confidence trade-off, and (2) the lack of an adequate adjustment mechanism (Garber, 1993). Robert Triffin identified the fundamental issue to the gold-dollar convertibility already in 1947, which later became
known as the ‘Triffin dilemma’, and presented it to the Joint Economic Committee in Washington in 1959 (Triffin, 1947; Triffin, 1978; Triffin, 1960). He argued that gradually increased international trade entailed equally increased international reserves needs i.e. dollars (Triffin, 1978; Triffin, 1960). The US deficits were thus necessary to support liquidity needs, but simultaneously reflected themselves in the USD devaluation pressures, eventually undermining the confidence in the dollar and so in the system itself (Garber, 1993). In other words, there was a trade-off to either dollar quantity or quality (Klaassen, 2018). Second, despite the de-jure possibility to resolve balance of payments disequilibria, there existed de-facto several disincentives to variable adjustments which would lead to equilibria reestablishment (Pilbeam, 2013). First, the USD devaluation would undermine confidence in the system, and other currencies devaluation would signal government weakness. Additionally, deficit countries were reluctant to adopt contractionary policies for fears of unemployment. On the other hand, surplus countries proved reluctant to revalue their currencies for fears of potential economic growth loss. On top of that, expansionary policies that could yield balance of payments equilibria were feared for inflationary consequences. In other words, internal balance focus overweighed external balance. Therefore, with none of the countries’ willingness to adjust either their economic policies or exchange rates, the question of how to maintain fixed exchange parities in the face of persistent imbalances in the balance of payments remained open (Pilbeam, 2013). Additionally, the then French finance minister Valery Giscard d’Estaing under Charles de Gaulle coalition exposed yet another ‘seigniorage’ problem, namely that the dollar pivotal role translated to ‘exorbitant privilege’ granted to the US, i.e. the system asymmetry (Eichengreen, 2010).

2 MONETARY INTEGRATION IN EUROPE: HISTORY AND PRESENT, THEORY AND PRACTICE, POLITICAL AND SOCIAL IMPLICATIONS

The theoretical framework discussed in the previous chapters is applied to the principal monetary integration of this paper, the EZ. I review facts and factors that characterised its emergence; the costs and benefits of its membership for specific countries; and finally, its political, and social implications, whereby theoretical expectations are challenged by some practical developments.

2.1 Emergence Facts and Factors

As the Bretton Woods era ended in 1971–73 the European Economic Community (EEC) countries advanced from the Snake in the Tunnel to the European Monetary System (EMS) by 1979 (Mrak, 2002). The latter encompassed three essential arrangements: the European Exchange Rate Mechanism (ERM), the European Currency Unit (ECU), the weighted average of the 12 European currencies, and the European Monetary Cooperation Fund, institutionalised for financial assistance (Pilbeam, 2013). The EMS was designed to erode exchange rate volatility in order to inhibit it from undermining trade stability by means of competitiveness changes (Higgins, 1993), accompanied by the longer-term aspiration for a fully-fledged economic and monetary union (Wittich & Shiratori, 1973), the latter notably originating from the Werner Report in 1972. The fixed exchange rate regime was materialised by setting up a grid of bilateral exchange rate bands, with each currency being allowed a narrow band of +/– 2.25% (Germany, the Netherlands, Belgium, France, Luxembourg, Denmark) or a broader band of +/– 6% (Italy, Spain, Portugal, UK) (Mrak, 2002).
Although the EMS experienced a crisis in 1992–93 that ultimately led to its downfall, there existed two benefits to joining: currency stability and a credible anti-inflation zone (Pilbeam, 2013). The first benefit, external balance, was widely associated to arise only at the expense of internal stability, which proved true in the early 1990s. The most significant economic shock was the German reunification, which pushed up interest rates not only for Germany, but also for the entire EMS in order to preserve their exchange rate parities (Pilbeam, 2013). However, with countries like the UK battling recession at the time, the need for contrasting economic policies arose (Davis, 2002). This built up market pressure and induced massive speculation attacks on most notably pound sterling and lira, which ultimately ensued their ERM suspension (Budd, 2005). In an attempt to keep other currencies in the ERM, bands were widened to +/- 15% in 1993, effectively marking the end of the fixed exchange rate regime (Mrak, 2002).

In the years before the crisis, currency stability was successfully maintained. Artis and Taylor (1994) find that greater nominal exchange rate stability was accompanied by greater real exchange rate stability, indicating some convergence of inflation and short-term interest rates. However, as Higgins (1993) and Rogoff (1985) note, exchange rate stability was supported by capital controls. With their abandonment by the early 1990s, fixed exchange rates could no longer be sustained without a perfectly coordinated monetary policy towards low inflation. In other words, the simultaneous newly free capital mobility and fixed exchange rates necessitated the loss of monetary independence. With the lost instrument, the Tinbergen rule shed light to the dilemma between domestic policy objectives and stable exchange rates, which was consequently marked ‘The Unstable EMS’ by Eichenbergen and Wyplosz (Higgins, 1993) as it led to its crisis in 1992–93.

**Graph 1: Inflation Rates in EMS Countries**

![Graph 1: Inflation Rates in EMS Countries](source: Higgins (1993).

Nonetheless, the convergence of inflation rates took place in 1980s (see graph 1), making the second benefit of the EMS a less painful disinflation process for weak currency countries (de Grauwe, 1994). The low inflation in the EMS was anchored by the German Bundesbank. With first-hand experience of hyperinflation in the 1920s making the Germans extremely inflation-averse ever since, the Bundesbank was granted independence in 1957 with the intent of promoting price stability (Pilbeam, 2013). Therefore, the credibility of the Bundesbank created an environment where the process of disinflation for relatively high inflation countries, such as Italy and France, could be conducted more rapidly, substantially, and at a lower cost (Giavazzi & Pagano, 1988; Melitz, 1988). Specifically, this came about by means of incentives for authorities and private economic agents (Pilbeam, 2013).
Namely, with the condition of peg maintenance, economic indicators such as inflation and interest rates must be aligned in order to preserve international competitiveness. Thus, a peg to a credible low-inflation currency translated into a more effective signal of commitment to an anti-inflation strategy for financial domestic and international markets than otherwise, tamed expectations better and resulted in less painful anti-inflation costs (notably the unemployment according to the Phillips curve, see Wen Wan, 2001). In this way, Italy and France effectively gained some of the German anti-inflation credibility, ultimately resulting in a greater degree of convergence in the EMS (Giavazzi & Pagano, 1988). It should be noted, however, that countries were willing to commit to the system discipline only after the second oil shock was over in 1982 (Pilbeam, 2013).

Further, Melitz (1988) argues that Germany’s international competitiveness increased as other countries were tied to fewer devaluations by committing to anti-inflation measures. In essence, by participating in the EMS, internal and external balance could hypothetically be achieved concurrently. However, although there was no anchor currency determined technically, German inflation and interest rates dictated EMS rates, and so the Deutsche Mark established itself as the centre of the EMS (Wyplosz, 1989). Hence, asymmetry emerged despite the bilateral exchange rate grid, which proved fatal as economic divergences came into light (Haldane, 1991).

As the euro superseded the ECU in 1999, ERM II replaced ERM (European Commission, 2019). The system demands that a currency is pegged to the euro with either a narrow margin of +/- 2.25% or a broad margin of +/-15% (European Commission, 2019). In 2019, the only country in ERM II is Denmark that pegs its Danish krone within the narrow margin, along with certain transition countries that are obliged to join the system for two years as one of the conditions under the convergence Maastricht criteria to join the European Economic and Monetary Union (EMU) (European Commission, 2019).

Thus, it became apparent that certain aspects of the European monetary integration framework needed to be addressed to sustain its functionality. First, given that the asymmetry of Bretton Woods and ERM resulted in these systems’ failure, the EZ is (Klaassen, 2018). Second, the impossible trinity limitations were reconsidered. At the EZ supranational level, the fixed exchange rate regime was abandoned for monetary independence and free capital mobility. This was accompanied by the fear of greater competitiveness fluctuations and thus trade instability, but on the other hand relaxed the exchange rate as a variable, thus providing for more readjustment mechanisms in the case of market pressures. Further, at the national level, the fixed exchange rate was preserved in the form of a hard peg, i.e. a monetary union. That way, free capital flows were maintained at the expense of monetary authority (Mrak, 2002). The ECB was established with the task of considering the EZ as a whole, and as opposed to the ECU, the euro is used as a medium of exchange in the entire EZ.

The euro era was initiated by notably two reports. Ever since the Treaty of Rome in 1957, it had been envisaged that the degree of integration would eventually reach a monetary dimension. However, it was only with the Werner Report in 1972 that the setting up of a monetary union was laid out in detail, as the focus of the Treaty of Rome was the customs union and so its mentioning of a monetary union did not exceed motivation. The Werner Report was the result of the Hague summit of 1969 and anticipated that the monetary union of the EEC would be established by 1980. Further, it argued in favour of the free movement of production factors (Werner, 1970). Next, it predicted the conduct of monetary and fiscal policy at the community level by community institutions, with monetary policy to manage the external relations with the non-EEC currencies, and fiscal policy to ensure
economic stability and growth (Werner, 1970). Finally, it foresaw the need for regional and structural policies to contribute to the balanced development within the community (Werner, 1970). However, the only tangible immediate result of the Werner Report was the Snake in the Tunnel. Pilbeam (2013) argues that the project was over-ambitious since it demanded that the countries give up their macroeconomic control in pursuit of convergent inflation rates to achieve parities, for which at the time of the oil crisis there was no political will.

It was only in 1989 that the specifics of monetary union realisation were outlined in the Delors Report. At the time, many incentives to the single currency existed. First, consequent to the European Single Act of 1986 it was seen that a single market would be best served by a single currency (Deschamps, 2016; Pilbeam, 2013). Second, a single currency would make the transition to the monetary union more effective due to its irreversibility (Pilbeam, 2013). Further, it would facilitate monetary management by diminishing transaction costs (Pilbeam, 2013). Hence, the Delors Report foresaw the establishment of a single European Central Bank to operate monetary and credit rate policy in order to avoid the potentially lumpish central bank coordination (Higgins, 1993). In this way, it was clear that the convergence of monetary and fiscal policy would ensue (Delors, 1989). The report determined three stages to the EMU realisation (Pilbeam, 2013): the convergence, the transition, and the euro stage, and assigned each the start and the finish dates. Stage 1 was initiated on 1 July 1990, Stage 2 on 1 January 1994, and Stage 3 on 1 January 1999, with euros circulating the EZ on 1 January 2002.

Thus, the EMU is broader than the EZ, which is the last stage of the EMU only. The conditions to join the EMU were delineated in the Maastricht Treaty in 1993 (Article 140 in ECB, 2019). By pertaining to five key economic indicators, they aim at their convergence (hence, ‘convergence criteria’), and at the facilitation of the functioning of the monetary union. Particularly, the inflation rate cannot exceed that of the lowest inflation countries by more than 1.5%. Further, budget deficit cannot exceed 3% of GDP and public debt 60% of GDP. Next, long-term interest rates cannot exceed that of the lowest long-term interest rates countries by more than 2%. Finally, to demonstrate exchange rate stability, a country must join ERM II for at least two consecutive years, which implies effectively pegging its currency to the euro. However, a permanent derogation was granted to the UK and Denmark in the EMU, permitting them an ‘opt-out’ of the third euro stage (Piekutowska & Kużelewska, 2015). Sweden likewise has a de-facto ‘opt-out’ since it never fulfilled the Maastricht convergence criteria. On the other hand, all other EU members have a temporary derogation, tying them to the eventual EZ entrance (Piekutowska & Kużelewska, 2015). Moreover, Greece joined in 2001 without complying with the criteria. All the above led Piekutowska and Kużelewska (2015) to consider the EMU a differentiated integration.

### 2.2 Economic, Social, and Political Costs and Benefits of the Eurozone

“When goods don’t cross borders, soldiers will.”

*Source: Frédéric Bastiat (19th century); Snow (2010).*

The EU was the result of a long-term European project proposed after the Second World War to preserve peace in Europe, executed notably by Jean Monnet (Garten, 2017). The underlying motivation was for the economic integration (of particularly Germany) to disincentivise any political
and military interventions, and to base geopolitical relations on economic cooperation and prosperity (Garten, 2017).

In relation to that, the single market was introduced in 1986 (Deschamps, 2016). As argued above, accompanied by a single currency, it further diminishes trade barriers such as exchange rate risk and transaction costs, thereby acting as a stimulus to intra-EU trade (Fratzscher, 2002; Camarero, Gómez & Tamarit, 2014; Rose, 2000; Frankel & Rose, 2002; Lane, 2006; Bun & Klaassen, 2002). In addition, that does not come at the expense of flexibility, given that euro value is determined through market mechanisms, making it less prone to speculative attacks and crises. First, EZ membership limits exchange rate risk (Fratzscher, 2002; Bun & Klaassen, 2002). While there are means to hedge against short-term exchange rate risk, such as financial derivatives markets, no such means exist in the medium to long-term, which places an adverse effect on long-term international trade (Peree and Steinherr, 1989). The EZ, on the other hand, ensures long-term exchange rate stability by being by default a long-term concept, and reduces short-term hedging related financial and administrative costs, such as exchange risk exposure strategy financing and monitoring (Pilbeam, 2013).

Second, single currency adoption eliminates transaction costs that were previously related to conversion fees, time, premiums etc., which the European Commission assessed to amount to 0.4% of the EU GDP per annum (Pilbeam, 2013). Pilbeam (2013) uses the term ‘economies of scale’ to signify the degree to which single currency affects the operations of businesses, banks, and individuals. Hence, by reducing trade costs, trade incentives increase (Bun & Klaassen, 2002). Indeed, Micco, Stein and Ordonez (2003) found that the euro increased trade in the region by 8-16%. Furthermore, not only does euro increase intra-EU trade, it also increases extra-EU trade (Pilbeam, 2013). Euro has namely claimed the Deutschmark characteristics of being an international currency backed by a credible central bank. In addition, Micco, Stein and Ordonez (2003) find that the euro increased trade already a year prior to its introduction, emphasising the significance of expectations. On the other hand, whether higher trade translates into higher economic growth remains inconclusive. Ehigiamusoe and Lean (2018) find that while economic integration yields positive effects on growth through trade, capital accumulation, and productivity growth, financial integration is not necessarily linked to higher economic growth, albeit it increases trade.

Further, the euro affects financial markets drastically by (1) eliminating currency risk and (2) providing greater liquidity for national members (Lane, 2006). First, currency risk encompasses inflation risk and exchange rate risk, the former being dependant on domestic and foreign inflation, and the latter on exchange rate volatility, which together with the inflation differential affect the real exchange rate (Klaassen, 2018). By adopting single currency both components of currency risk are eliminated as common inflation must be sustained in light of capital mobility as one of the four pillars of freedom in the EU (Mrak, 2002). Therefore, euro denominated debt offers lower interest rates i.e. cheaper source of financing for governments and businesses, as neither inflation nor exchange rate volatility premium is attached (Lane, 2006; Cette, John & Benoit, 2016). Thus, borrowers enjoy lower interest rates, and lenders lower risk. This argument extends to international borrowing where, despite some currency risk, such is limited by the credible ECB whose low inflation target fuels the reputation of the euro as an internationally strong and stable currency. However, as the case of the Greek debt revealed, euro denominated debt does not decrease political and fiscal risk (Klaassen, 2018). In sum, as far as currency risk is concerned, euro denominated debt is cheaper nationally and internationally.
The next benefit of euro is greater liquidity on the EZ and international levels (Lane, 2006; Portes & Rey, 1997). Higher liquidity is associated with lower transaction costs, which again reduces the cost of financing (Portes & Rey, 1997). On the EZ level, it is a natural consequence of further market integration, and on the international level of the euro’s reputation as an internationally stable and thus relatively desirable currency. Pilbeam (2013) argues that the euro, even though allowed to fluctuate, will likely fluctuate less than any individual EU currencies would due to the balancing out of the performances of their economies. In addition, not only is the EZ a net recipient of liquidity benefits, it also provides liquidity for international trade since the EZ covers a market of 332 million people, larger even than the 310 million US market (Portes & Rey, 1997). By challenging the dollar position of a key international reserve currency, which lingers still from the Bretton Woods times, it thus alleviates the world’s seignorage problem (Portes & Rey, 1997). As a currency granted the exorbitant privilege by other countries’ willingness to hold euro reserves, it brings down financing costs (Portes & Rey, 1997; Pilbeam (2013) lists the study of Cohen and Wyplosz (1989) who estimate the related savings to amount to 0.75% of the EU gross national product). Hence, borrowing and lending in the EZ and internationally is easier (Lane, 2006).

Moreover, as common currency entails common inflation, common inflation encourages greater price transparency (Barrell et al., 2008). This stimulates competition by eliminating price-related distortions across markets. As price differentials prove more difficult to maintain, greater inflation convergence ensues.

Last, Pilbeam (2013) points to a more efficient allocation of production factors within the EU. Namely, despite the free movement of capital and labour already established as one of the four freedoms of the EU, the euro pushed to their full realisation (Barrell et al., 2008). In particular, the factor will seek high marginal productivity areas, which prior to the euro remained discentivised in fields where currency was significant, e.g. conversion premiums, fees, wage denominations, price differences and other restrictions and distortions that persisted in the face of full freedoms. That said, regional disparities with unfavourable social effects may arise as a consequence of factor movement (Meardi, 2012). Put differently, the efficiency of the EZ as a whole can come at the expense of its structure within. Indeed, the EZ was criticised for failing to translate economic efficiency to better development, whereby free movement of labour induces large-scale brain drain, and free movement of capital drains investment and job opportunities (Varoufakis, 2017; Meardi, 2012). In this environment, East European countries resorted to lowering income taxes to attract capital in an attempt to paint their regions as favourable (Čok, 2018), and cases of labour exploitation are known (Meardi, 2012). However, whether the EMU has caused or merely fostered the stagnation of certain regions remains an open issue, but one that entails the use of corrective EU regional policy (Pilbeam, 2013).

On the other hand, the most profound and restrictive cost of the EZ is the loss of monetary authority (Beetsma & Giuliodori, 2010). In a monetary union, economic convergence is key. As economies diverge, the conduct of a common monetary policy is inevitably inadequate for certain economies (Esposito, 2014). For instance, a typical response to a booming economy is the raising of short-term interest rates to stifle inflationary pressures, while to a sluggish economy a typical response is the lowering of interest rates to stimulate credits, investments, and consumption (Mankiw, 2016). Additionally, should a country pursue several macroeconomic objectives simultaneously, fiscal policy alone cannot suffice according to the Tinbergen rule; what is more, even fiscal policy must be
harmonised for the proper functioning of the union (Beetsma & Giuliodori, 2010; Eijffinger & de Haan, 2000; Cooper & Kampf, 2004).

Similarly, a country’s short-term trade-off between inflation and unemployment is summarised by the Phillips curve (Samuelson & Solow, 1960). For countries whose macroeconomic balance between these two targets differs from that of the EZ, a common inflation rate turns out to be suboptimal (Pilbeam, 2013). Namely, countries that prioritise lower unemployment over higher inflation might suffer higher unemployment than nationally desired; on the other hand, countries with the opposite goals might suffer higher inflation than nationally desired. However, when the goal is the process of disinflation for relatively high inflation countries, they can do so bearing lower costs of unemployment by claiming the credible announcement policy which effectively reduces inflation expectations (Blanchard, 1997). By joining the EMU, they are effectively reducing inflation according to the common EZ Phillips curve instead of their national one (de Grauwe, 1994). Therefore, the Phillips curve coordination at the EZ level may both exacerbate the pursuit of macroeconomic objectives for countries whose objectives are not aligned with that of the EZ, and alleviate the pursuit of macroeconomic objectives for those whose are.

Another phenomenon that cuts both ways is the spillover effect, as integration makes countries more susceptible to both positive and negative effects (i.e. spillovers) from other countries in the union. In particular, economic prosperity in one country could easily translate into the growth of exports in another country if they are integrated, as less barriers to trade exist. On the other hand, so can crises. Fernández-Rodríguez, Gómez-Puig and Sosvilla-Rivero (2015) and Antonakakis and Vergos (2013) remind of the Greek debt crisis as an example. Negative spillovers in monetary unions spread with ease as confidence in the entire system is affected, whereby market expectations, namely the fear of contagion, play a key role (Constâncio, 2012; Fernández-Rodríguez, Gómez-Puig & Sosvilla-Rivero, 2015; Rant & Fuhriman, 2017).

Finally, EMU membership comes at a loss of the exchange rate instrument, the implications of which are parallel to that of the loss of monetary policy (Beetsma & Giuliodori, 2010). Namely, a country is no longer free to manipulate this instrument in order to produce nationally desirable economic results (Lane, 2006; Beetsma & Giuliodori, 2010). Specifically, the competitiveness of South European countries could no longer come about by devaluations (Toussaint, 2013; Beetsma & Giuliodori, 2010). Rather, in order to achieve the same competitiveness level, they must adhere to low inflation, which in turn ties hands as to the policy use (Lane, 2006; Beetsma & Giuliodori, 2010). Furthermore, in the early stages of the EZ, low interest rates accompanied by low inflation rates were associated with low investment and high (over)consumption in Spain, which was reflected in trade imbalances and increasing debt obligations (Toussaint, 2013; Esposito, 2014; Lane, 2006). Therefore, although the euro is adjusted so that the EZ balance of payments is in equilibrium, the national balances of payments are not. Graph 2 shows the current account balances of individual member states and reveals persistent deficits and surpluses of specific countries, which reflects the overall EZ trade imbalances.
Lastly, Mundell (1961), according to his Optimal Currency Area theory, argues that benefits outweigh the costs if member states are sufficiently convergent. Moreover, the economic convergence ought to be accompanied by a political one (Cooper & Kampf, 2004). Hence, the Maastricht criteria and the subsequent Stability and Growth Pact (SGP) strive for convergence (Beetsma & Giuliodori, 2010). Yet, if they are not adhered to, as Piekutowska and Kużelewksa (2015) maintain, there is no basis to contend that the EZ is an optimal currency area according to Mundell’s theory. However, the convergence criteria were subject to some criticism, which makes it dubious to assess what would be optimal: their strict following or being open to compromises, and if so, concerning which criteria and to what extent.

Nevertheless, it is precisely due to internal discrepancies that were to be avoided through convergence criteria that Rant and Fuhriman (2017) argue the EZ was susceptible to external shocks as its ‘back-up’ mechanisms were not established and imbalances prevailed, resulting in the 2008 financial and economic crisis inducing asymmetric effects across the union. In this way, the crisis was reflected in increased social friction and thus political demands for leaders that point to power imbalances and fuel Euroscepticism. At the same time, most remain unconstructive in their demands for the potential change in the EU, and so act harmful to a long-term establishment of the EZ which must be supported by trusted institutions for its future functioning.

2.3 Political Implications for the EMU and its Individual Member States

The EMU admission process was criticised for permitting candidates in without enforcing their strict complying with the convergence criteria (Piekutowska & Kużelewksa, 2015). In particular, Piekutowska and Kużelewksa (2015) point out that the 60% debt of GDP criterion was largely overlooked in the name of the debt ratio merely approaching the reference value, and the situation was akin to the 3% deficit of GDP criterion. The most notable case of admission to the EMU on grounds of only promised ex-post convergence was Greece, which was admitted in 2001 despite its deficit ratio of 4.4% of GDP and debt ratio of 103.7% of GDP (Provopoulos, 2013). Piekutowska and Kużelewksa (2015) conclude that based on economic incompliance and divergences, it were political reasons that were key for the admittance of Greece and the EMU establishment as a whole.
This later turned out to be severely problematic despite the ‘no-bail-out’ clause, as due to spillover effects the debt crisis spread to other countries, evoked the political turmoil, and largely undermined the confidence in the euro system and the euro itself (Fernández-Rodríguez, Gómez-Puig & Sosvilla-Rivero, 2015; Antonakakis & Vergos, 2013; Constâncio, 2012; Rant & Fuhriman, 2017).

On the other hand, the convergence criteria were criticised for being set at arbitrarily prescribed levels (Pilbeam, 2013). In addition, they were criticised for their exclusive focus on financial indicators, disregarding real economic components such as economic growth, balance of payments and the unemployment rate. Pilbeam (2013) notes that in order to comply with the criteria, some countries often sacrificed real economic components by imposing fiscal austerity. Further, de Grauwe (1996) argues that complying with the fiscal criteria would be more sensible only after joining the EMU, as the elimination of inflation risk would erode inflation risk premiums that were built in the debt interest rates. In turn, lower financing costs would decrease their fiscal deficits and ultimately their national debts. Next, the Maastricht Treaty contained the ‘no-bail-out’ clause with the legal implication of EMU members not being held accountable for the debt obligations of their fellow members (Pilbeam, 2013). However, as implied above, this only disguised the threat of fiscal spillovers (Lane, 2006; Beetsma & Giuliodori, 2010).

Finally, the lack of the follow up obligations to the Maastricht reference values was criticised (Pilbeam, 2013). The criteria evoked incentives for prior prudence, but secured none for its continuation. Therefore, to ensure the continued fiscal responsibility, Germany proposed the Stability and Growth Pact (SGP) to supplement the criteria. The Pact strove to disable fiscal laxity to undermine confidence in the euro by obliging members to follow up to the deficit and the debt targets (Huart, 2002; Beetsma & Giuliodori, 2010). This way, the role of the SGP was to compensate for the bias in the ‘before’ focus of the Maastricht criteria and for the compromising of its fiscal components in the EMU admission process. However, the SGP also was subject to much criticism as the most intense advocators of the SGP, Germany and France, failed to adhere to it shortly after its passing (Pilbeam, 2013). The fact that no fines ensued revealed the political bias towards the ‘big’ members of the EMU. Others criticised it for failing to acknowledge economic cycles. In 2002, the European Commission President Romano Prodi called the pact “stupid”. In response, the SGP underwent two reforms in 2005 and 2011, but along with other Maastricht criteria failed to converge EMU members to the level that would make them crisis-unsusceptible (Sklias & Maris, 2016; see graph 3 for government debt ratios across the EZ).

![Graph 3: Government Debt as the Ratio of GDP in the EZ](image-url)

*Source: Robert Schuman Foundation (2017).*
Indeed, the 2008 crisis unveiled the divergences that prevailed in the EZ in several fields (Rant & Fuhriman, 2017). Graph 4 exhibits government yields which reveal country risk premiums, which can be discerned due to currency risk absence. Finally, social divergences constitute another issue for the EZ (Esposito, 2014; see graph 5 for unemployment rates).

*Graph 4: Long-Term Government Bond Yields of EZ Members*

![Graph 4](source: Spitzl (2017).)

*Graph 5: Unemployment Rates in the EZ vs Germany in Percentages*

![Graph 5](source: Bernanke (2015).)

As a response to the 2008 crisis, integration tightened with the establishment of a banking and fiscal union, along with the mechanisms such as the European Stability Mechanism (ESM) to introduce crises-immunity in the system, which further synchronises the operations of member states. Namely, the lack of ‘back-up’ mechanisms prior to the crisis was largely criticised (Rant & Fuhriman, 2017). Further, the supremacy of EU law entails that national legislation and legal institutions are subject to EU law and the European Court of Justice (Craig & de Búrca, 2011).

By monetary unification and fiscal harmonisation, both macroeconomic policies are effectively relinquished to the EU level. Hence, economic integration entails a political and an institutional one. The respective sacrifices were, however, presented already in the 1972 Werner Report.
3 IMPLICATIONS OF THE EURO ON GDP OF INDIVIDUAL EZ MEMBER STATES: AN EMPIRICAL ANALYSIS

The posed theoretical basis demands some empirical verification. Specifically, I employed the study of Gasparotti and Kullas (2019) from the Centre for European Policy (CEP) in pursuit of evaluating theoretical expectations against the empirical reality to arrive at tangible conclusions for selected EMU countries.

The study aims to determine the welfare brought about by the EZ by comparing the GDP per capita with the hypothetrical GDP per capita as obtained by the synthetic control method, and ultimately reveal the so called ‘winners and losers’ of the EZ (Gasparotti & Kullas, 2019). They point out the necessity of evaluating the prosperity of the euro in a wholesome manner as indicated by the GDP per capita and average national consumption rates, and transcend from the previously largely focused on trade promotion (in for instance the studies of Camarero, Gómez & Tamarit, 2014; Rose, 2000; Frankel & Rose, 2002; Micco, Stein & Ordonez, 2003; Lane, 2006; and Bun & Klaassen, 2002). In addition, Gasparotti and Kullas (2019) argue that the disadvantage of the devaluation limits and the associated divergent competitiveness issue is overlooked when analysing trade promotion only, and warn that it does not paint a broader picture in the final assessment of the EZ reality (the same issue is risen by the studies of Toussaint, 2013; Beetsma & Giuliodori, 2010; and Lane, 2006). Last, they only include eight long-term EU member states, Germany, the Netherlands, Greece, Spain, Belgium, Portugal, France, and Italy, as the analysis of the more recent EU member states would pose the indiscernible issue of the notably substantial EU effect on growth vis-à-vis the euro effect.

The empirical evidence provided by the study of Gasparotti and Kullas (2019) reveals that only two out of the eight EZ countries studied benefited from the euro as indicated by their GDPs per capita in 2017, namely Germany and the Netherlands. The GDP of Germany was higher by EUR 280 billion by participating in the EZ, which corresponds to EUR 3,390 of GDP per capita (see graph 6 and 9). Likewise, that of the Netherlands was higher by EUR 19 billion, which is equivalent to EUR 1,116 of GDP per capita.

Graph 6: The GDP Per Capita of Germany With and Without Euro (in EUR)

Source: Gasparotti & Kullas (2019).
The GDPs of the other six countries were found to be relatively lower to their hypothetical non-EZ values, whereby Italy lost the most, with its hypothetical GDP higher by EUR 530 billion or EUR 8,756 of GDP per capita had it remained out of the EZ as indicated by graphs 7 and 10. The figures for Greece reveal the same trend with its GDP lower by EUR 41 billion to that of its hypothetical non-EZ value, which amounts to EUR 3,850 of GDP per capita as exhibited by graphs 8 and 11.

Second, Gasparotti and Kullas (2019) assess the impact of the introduction of the euro on prosperity by summing the annual GDP per capita euro surpluses or deficits and multiplying them by the related average national consumption rates along with adjusting to the population growth in the 1999-2017 period, thereby arriving at the cumulative prosperity euro effect which considers the consumption rates. Similarly to its GDP trends, the study yielded positive figures for Germany and the Netherlands, whereby summing the GDP per capita euro surpluses for Germany and multiplying them with its consumption rate of 77.83% revealed EUR 1,893 billion or EUR 23,116 per capita (see annual GDP surpluses exhibited by graph 9) and for the Netherlands EUR 346 billion or EUR 21,003 of prosperity per capita with the Dutch consumption rate of 72.52%.

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**Graph 7: The GDP Per Capita of Italy With and Without Euro (in EUR)**

![Graph 7](image1.png)

*Source: Gasparotti & Kullas (2019).*

**Graph 8: The GDP Per Capita of Greece With and Without Euro (in EUR)**

![Graph 8](image2.png)

*Source: Gasparotti & Kullas (2019).*

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However, they were not the only ones with positive figures. The study also revealed positive figures for Greece of EUR 2 billion of overall prosperity or EUR 190 per capita using the consumption rate of 81.88% (see graph 10). Continually to the GDP figures, Italy lost the most from the euro, with an overall loss of prosperity of EUR 4,325 billion or EUR 73,605 per capita using its consumption rate of 77.59% (see graph 11), followed by France with the consumption rate of 77.86%, whose loss of prosperity of EUR 3,591 billion or EUR 55,996 per capita remains nowhere near negligible.
CONCLUSION

The Gasparotti and Kullas (2019) study concludes that Germany gained the most from the euro, while Italy lost the most. However, they fail to elaborate the concrete plausible causes that led to these results in an exhaustive and comprehensive multi-angled manner. Theory suggests that in the early years of the euro introduction, the competitiveness of Germany increased relatively to that of most EZ countries that were still battling higher inflation (Melitz, 1988), and were simultaneously unable to compensate for the loss of competitiveness by currency devaluations (Toussaint, 2013; Beetsma & Giuliodori, 2010; Esposito, 2014; Lane, 2006; Gasparotti & Kullas, 2019). As Toussaint (2013) adds, the situation in the South of the EZ was exacerbated by the overconsumption and underinvestment in Spain, further feeding the housing bubble that emerged in that area thereafter. Essentially, the increased relative competitiveness of Germany had a positive effect on its current account that resulted from the positive effect on its exports, which persists until today. This trend continues because it is facilitated by the notably relatively high German propensity to save, a case similar to that of the Netherlands.

While positive for individual countries, this is negative for the cohesiveness of the EZ as a whole. Indeed, the EZ was criticised for punishing current account negative imbalances in a more determined manner than positive ones, albeit all imbalances cause union disparity (Mrak, 2019). As Esposito (2014) notes, the euro fuelled the divergent current account levels, and thus an increasingly divergent rather than increasingly convergent EZ. This led to its susceptibility to potential crises, reflecting its most apparent vulnerability in the 2008 global recession (Rant & Fuhriman, 2017).

Indeed, Italy seemed to be the most negatively affected by the euro through the loss of the exchange rate policy instrument. Its competitiveness appeared to have remained uncompensated by the benefits suggested by theory, namely that of the central bank credibility inducing lower public debt rates. This positive effect was arguably offset by the contagion that spread from the Greek debt crisis shortly after the euro introduction, infecting the deficit account countries by restricting to renew their lower euro associated bond yields which they had been facing until then (Lane, 2006), and eventually forcing them into restructuring programs.

The most notorious case was Greece (Fernández-Rodriguez, Gómez-Puig & Sosvilla-Rivero, 2015; Antonakakis & Vergos, 2013; Constâncio, 2012; Rant & Fuhriman, 2017). The study clearly reveals how the euro shifted from producing gains to producing costs for the Greek economy as its public debt struggles began threatening its international financial market position in roughly 2011, followed by the undermined trust in the entire EMU and the euro as contagion spread to other members (graph 4 demonstrates how that was reflected in the long-term government bond market). Whether the blame was entirely on the euro questions Pilbeam (2013), who notes that national problems are hardly straightforward due to monetary union, albeit he recognises their interconnectedness, which is in itself difficult to assess. Further, we can argue that the ‘no-bail-out’ Maastricht clause did little to prevent fiscal laxity from transcending the national issues. Moreover, it distracted from the risk of spillovers (Beetsma & Giuliodori, 2010; Fernández-Rodriguez, Gómez-Puig & Sosvilla-Rivero, 2015; Antonakakis & Vergos, 2013; Constâncio, 2012; Lane, 2006; Rant & Fuhriman, 2017), essentially making it counterproductive in that it incentivised lenient compliance with the Maastricht criteria as evidenced in the EMU admission process, thereby revealing the prioritising of other incentives of potentially political nature, which was suggested by Piekutowska...
and Kużelewkska (2015). However, it is difficult to judge the process of EMU admission as overly tolerant for not abiding by the convergence criteria in a disciplined fashion, as other economic and political reasons existed to support the criteria opposition (de Grauwe, 1996; Pilbeam, 2013). Hence, to evaluate whether persistent divergences are to be addressed prior or post EMU acceptance remains an open question, as both may lead to undesirable outcomes.

In order to foster economic convergence, promote the overall union balance, re-establish sound monetary and fiscal policy, and manage to continue to sell the EMU idea to the progressively sceptical public, the EMU authorities have set up several ‘back-up’ mechanisms. The European Stability Mechanism (ESM) and the reformed Stability and Growth Pact are the most notable ones, designed to maintain a resilient and convergent EMU and EU. Nevertheless, no solution is single-dimensional when forming economic policies where interconnectedness prevails, and ESM was subject to criticism for incentivising reckless euro bond risk assessing as the mechanism essentially promises to repay even the higher risk bonds should the country default on its debt obligations. Indeed, there exist several economic objectives and few instruments, as reminded by the Tinbergen rule.

On top of that, these measures fuel political unrest and the term two-tier Europe emerged to signify the contrasting rules in Europe on several levels: the traditional members vs the post-2004; the euro vs non-euro; the Schengen vs non-Schengen EU members. This was exacerbated by the recent memory of the aforementioned restructuring programmes that followed the shooting up of the borrowing costs for most EZ members at the sight of the crisis (see graph 4 for long-term government bond yields). These encompassed austerity measures, which were introduced to relieve the deficits. However, in the face of prevailing economic and social divergences, this laid the path for the currently observed rise of the nationalist political parties across Europe (Varoufakis, 2017; Meardi, 2012).

Therefore, the current situation of current account surpluses might be concealing the lost welfare that accompanied the restructuring paths, as suggested by Mrak (2019). The lost prosperity was evidenced in the Gasparotti and Kullas (2019) study, which identified Italy as the most affected even in the pre-crisis area. Nevertheless, to reveal a more detailed analysis, it would have been valuable had the study focused on several indicators along with GDP per capita and the prosperity linked consumption, for instance inflation, balance of payments, and public debt yields, which would make it easier to link causes and consequences for euro-associated cost and benefits. Essentially, the assessment of several indicators would fit the specific-benefits-for-specific-countries narrative better, and help identify the winners according to various criteria.

Altogether, this questions the suitability of EMU members to be monetarily integrated given that they hardly adhere to the convergence necessitated by the Mundell’s Optimal Currency Area (1961). Furthermore, it turns out that oftentimes, the costs and benefits originate from the same phenomenon – they are merely viewed differently from the standpoint of specific country objectives and values. For instance, the common Phillips Curve (de Grauwe, 1994) is viewed in a positive manner should the country’s goal be the reducing of inflation, yet, it becomes undesirably binding should the goal be the reducing of unemployment through now unattainable inflationary policy. In other words, the unifying of the Phillips Curve can be a pro or a con, depending on (current) country targets. This calls for not only static economic convergence, but also for a dynamic alignment of objectives.
In this regard, my hypotheses aimed to illustrate that despite the apparent costs that EZ membership entails, there exist tangible, albeit different benefits for different countries. The first two hypotheses that dealt with this issue are listed below along with the third hypothesis that gauged the EMU admission process and related widespread divergence:

I. South EZ countries, such as Italy and Spain, benefit from the EZ more than they lose, since their economic perspectives are better as members. Lower expected inflation as monetary instruments are controlled by the credible ECB, followed by lower interest rates and limited exchange rate risk, all contribute to higher economic growth.

II. West EZ countries, such as Germany and the Netherlands, benefit from the EZ more than they lose as a result of stimulated trade in the EZ area and thus increased exports into other member states, making their current accounts positive, along with increased savings and investment. However, this leads to discrepancies and tensions in the EZ as an economic, as well as in the EU as a political structure.

III. Political reasons, and not economic, are key to the admission of South EZ countries, such as Greece, into the European monetary integration along with the West countries; hence, economic discrepancies, such as country political risk, manifested in higher government bond interest rate, prevail even in the event of conditional economic convergence criteria.

Based on the results of the study by Gasparotti and Kullas (2019), I reject the first hypothesis. It appears that albeit the benefits of lower expected inflation and lower government bond yields exist, they fail to overweight the costs, namely lower economic growth and not higher, as predicted by the hypothesis. In fact, according to the study, the economy of Italy performed the worst out of eight analysed countries due to the euro. However, in order to determine the links between these indicators with higher accuracy and practical implications for economic policies, the importance of assessing several economic factors emerges, as suggested above.

Furthermore, given the results of the Gasparotti and Kullas (2019) research, I confirm the second hypothesis. Indeed, the euro amplified their positive accounts due to intra-EZ stimulated trade, which turned out to be expedient as their relative competitiveness was higher, accompanied by other factors such as higher propensity to save. It is further confirmed that the discrepancies cause socially undesirable outcomes, such as qualified labour force concentration in the West of the EU, as brought about by brain-drain and criticised most notably by Varoufakis (2017). It is undeniable that this is linked to political turmoil observed in the recent European history.

Yet, whether the EZ divergences are a product of EMU admission or would have persisted regardless, and whether these led political interests to prevail over economic ones, is more difficult to evaluate. However, based on the theoretical analysis, particularly that of Piekutowska and Kuźlewska (2015), the respective issue appears to be more present than not, which leads me to lastly confirm the third hypothesis. This coincides with the study of Faber (2006), who calls for the deepening rather than widening of the European integration.

Nevertheless, we must allow for a sound judgement of the results obtained by the study of Gasparotti and Kullas (2019). As Hans-Werner Sinn, the former director of the Ifo Institute for Economic Research emphasises, there have been some methodological dubieties (Kenda, 2019). Mrak (2002) equally warns of the ‘hypothetical’ methodology use for comparison. Yet, despite its methodological
shortcomings, Sinn remains certain the study will be misused for political reasons related to the EU fiscal budget distribution and other political interests (Kenda, 2019). Therefore, the possibility of a different outcome must not be denied at the occurrence of a more accurate insight with various indicators and less dubious methodology.

Finally, my study serves to remind of the necessity for consistently applied, reviewed, and linked factors of EMU integration to finally clarify the issue of euro-associated specific costs and benefits for specific countries, and accordingly provide accurate and practical economic policy guidelines. Therefore, the thesis evaluated the costs and benefits of the euro while considering that different country characteristics entail different country benefits. The analysis acknowledged the respective research question by paying specific attention to benefit division and tying its origins meticulously to the country characteristics. Not surprisingly, Italy can expect different benefits from European monetary integration than Germany. In turn, the European monetary integration was reviewed in the historical context to arrive at a full comprehension of the current monetary arrangements in Europe. At the centre of my research was the question whether integration ultimately serves the national members with specific benefits outweighing the potentially more apparent and frequently exposed costs. In order to limit the political misuse and present theoretically fair and empirically supported data, the issue covered by the thesis demonstrates the appreciation of academic research via its application to and the shaping of economic and political reality.

REFERENCE LIST


Appendix 1: Povzetek (Summary in Slovene language)

Diplomsko delo obravnava problematiko specifičnih korist in stroškov za specifične države. Države so si različne iz zgodovinskih, ekonomskih, političnih in socialnih vidikov. Razlikovanje med državami je ključno, saj se glede na njihove karakteristike za posamezne države aplikirajo drugačni stroški in koristi in le na podlagi teh teoretično realističnih koristi lahko ocenimo njihove realizirane vrednosti. Povedano drugače, zaradi razlik v naravi držav je ustrezno pričakovati, da bodo zaradi evroobmočja deležne različnih koristi.

Problematica je relevantna iz več razlogov. Prvič, v okviru globalizacije in povečanega trgovanja med državami monetarna integracija prinaša zmanjševanje transakcijskih stroškov in omejevanje valutnega tveganja. A vendar ta prinaša tudi signifikantne stroške, ki jih morajo posamezne države oceniti glede na svoje koristi. Šele potem je integracija smotra. Slednje je povezano tudi z vzponom populističnih strank, ki zahtevajo deintegracijo v imenu večinoma bolj očitnih stroškov. Drugič, natančna proučitev specifičnih korist in stroškov za specifične države je pomembna, da stroški ne bi bili politično izrabljeni in da bi bile koristi, ki jih lahko posamezne države pričakujejo, deležne enake pozornosti. Namreč, šele po tem, ko se ugotovijo koristi glede na posebnosti držav članic evroobmočja, se jih lahko primerja z njihovim dejanskim stanjem ter se lahko začnejo oblikovati mnenja in pričakovanja od evropske monetarne integracije kot podlaga za (de)integracijo.

Tako sem si zastavila tri hipoteze:

I. Južne države evroobmočja, npr. Italija in Španija, imajo od njega več koristi kot stroškov, saj so v primeru članstva v evroobmočju njihove gospodarske perspektive boljše. Pričakovani nižji inflacij zaradi monetarne politike pod nadzorom kredibilne ECB sledijo nižje obrestne mere in omejeno valutno tveganje. Vse to prispeva k višji gospodarski rasti.

II. Zahodne države evroobmočja, npr. Nemčija in Nizozemska, imajo zaradi trgovinskih spodbud na evroobmočju več koristi kot stroškov, zaradi česar beležijo večji izvoz, kar se preliva v njihove pozitivne tekoče račune, pa tudi varčevanja in investicije. Vendar to vodi do neskladij in napetosti ne le v evroobmočju kot gospodarski, ampak tudi v EU kot politični strukturi.

III. Politični razlogi, in ne ekonomski, so ključni za sprejem južnih držav evroobmočja, npr. Grčije, v evropsko monetarno integracijo skupaj z zahodnimi državami; zato gospodarske razlike, kot je politično tveganje države, ki se kaže v višji obrestni meri državnih obveznic, prevladujejo tudi nad pogoji ekonomske konvergencije.


Trikotnik nekonsistentnosti je osrednja teorija monetarnih integracij, ki jasno riše njihove omejitve. Zapoveduje namreč, da je od treh relativno zaželenih ekonomskih ciljev, torej monetarné neodvisnosti, fiksnega deviznega tečaja in prostih kapitalskih tokov, simultano možno doseči le dva. Zato se to teorijo v literaturi imenuje tudi makroekonomska trilema. Podam tudi primere neuposkodovanje teh zapovedi, ki so se odrazili v krizi, med katerimi sta najbolj znana primera Vzhodne Azije in Evropskega monetarnega sistema (EMS). Poleg tega se države evroobmočja soočajo s stroški in koristi fiksnih deviznih tečajev. Glavni strošek je odpoved monetarni samostojnosti v okviru prostih kapitalskih tokov, kot to zapoveduje triotnik nekonsistentnosti, katerega mehanizem analiziram skozi teoretski okvir modela Mundell-Fleming.

Poleg tega države izgubijo instrument deviznega tečaja, ki je lahko ključen za odziv na tržne interne gospodarske razmere in tudi plačilnobilančno prilagajanje. Vsaka izguba instrumenta pomeni manjšo odzivno moč za dosego makroekonomskih ciljev, razmerje med katerimi opisuje Tinbergenovo pravilo: država potrebuje toliko instrumentov, kolikor ima ciljev. Prav tako je za kontinuiran fiksen in stabilen tečaj treba upravljati druge temeljne ekonomske indikatorje, npr. inflacijo. V primeru fiksnega tečaja, ki je značilen za države v monetarni uniji, se kompromis med dezinflačijo in nezaposlenostjo, ki ga opisuje Phillipsova krivulja, dejansko zmanjša (Grauwe, 1994). Po drugi strani pa je glavna korist višja ekonomska stabilnost in tako boljše okolje za mednarodno poslovanje in investicije. Omeniti je treba tudi povečano disciplino in tako kredibilnost nacionalne centralne banke za izpolnjevanje zastavljene monetarne politike, saj efektivno prevzame kredibilnost centralne banke, katere valuta je osnova za vezavo nacionalne. Ta je izmenoma povezana z drugimi pomembnimi ekonomskimi indikatorji, kot so obrestne mere za javno zadolževanje (Lane, 2006). Države članice današnega evroobmočja so se skozi zgodovino srečevale z vsemi omenjenimi koristi in omejitvami.

Nadalje pretekle monetarne integracije ovrednotim skozi proučeni teoretični okvir. Uvidim, da se je skozi zgodovino menjaval fokus na notranje in zunanjé makroekonomske cilje, tj. fleksibilnost in stabilnost, in temu primereno denarni sistem. Tako analiziram zlati standard in zlati devizni standard, ki sta bili denarni ureditvi do druge svetovne vojne, in zatem povojno Brettonwoodska ureditev. Sistema sta propadla zaradi drugačnih razlogov, katerih proučitev in razumevanje sta ključna za uspešno gradnjo prihodnjega sistema. V naslednjem poglavju raziskujem korake k današnji evropski
denarni integraciji. Tako ugotovim, da je asimetričnost sistemov iz 20. stoletja spodbudila nadaljnje asimetrično gradnjo sistema proti koncu stoletja.

Evropska integracija je od nekdaj stremela k njeni tesnejši obliki, kot to predvideva Balassova teorija (Balassa, 2013). Svetovni vojni 20. stoletja sta delovali kot glavna razloga za povezovanje, začenši s skupnim nadzorom nad proizvodnjo jekla in premoga, rezultat tega pa je bila tudi vse višja ekonomska prosperiteta. Tako je bil po Kači v tuneli ustanovljen EMS, ki sta ga odražali dve koristi: (1) stabilnost valute, pomembna zato, ker volatilnost deviznih tečajev ovira stabilnost trgovanja preko sprememb konkurenčnosti (Higgins, 1993), in (2) verodostojno anti-inflačijsko območje, kjer so lahko države s šibkejšimi valutami znižale svoje inflacije z manjšimi stroški, saj je nemška Deutsche Bank delovala kot sidro območja, katere valuta, obrestne mere, ter ugled usmerjajo ostale (Wyplosz, 1989). Kljub temu torej, da je bil EMS zasnovan s ciljem simetričnosti preko bilateralnih mrež vezanih valut v Evropskem mehanizmu deviznega tečaja (ERM), se je izkazal za asimetričnega (Haldane, 1991). Zaradi tega, pa tudi zaradi vodenja različnih monetarnih politik kljub ukinitvi kapitalskih kontrol konec osemdesetih let, saj Velika Britanija zaradi recesije, torej internega fokusa, ni bila pripravljena povečati obrestnih mer, ki jih je za celotno območje narekovala ponovna nemška združitev, tj. nespoštovanja omejitev trikotnika nekosistentnosti, je EMS leta 1992–93 razpadel.


Obstaja veliko spodbud za vstop v EMU. Prvič, skupni trg, ki ga spremlja enota valuta, signifikantno zmanjšuje ovire za mednarodno trgovanje, kot sta valutno tveganje in transakcijski stroški, in tako deluje kot spodbuda za trgovino znotraj EU (Fratzscher, 2002; Camarero, Gómez & Tamarit, 2014; Frankel & Rose, 2002; Lane, 2006; Bun & Klaassen, 2002). Poleg tega to ne gre na račun prožnosti, saj je vrednost evra določena preko tržnih mehanizmov. Evro torej močno vpliva na finančne trge z (1) odpravo valutnega tveganja in (2) zagotavljanjem večje likvidnosti za članice (Lane, 2006). Namreč, dolg, denominiran v evrih, ponuja nižje obrestne mere, tj. cenejši vir financiranja za privatne in javne ekonomske subjekte, saj obrestni meri ni pripisana niti inflačijska premija niti premija za valutno tveganje (Lane, 2006; Cete, John & Benoit, 2016).


Nadalje, največja slabost EMU je torej poleg izgube monetarne oblasti tudi izguba instrumenta deviznega tečaja. Kot že opisano v splošnem teoretičnem delu, ga država ne more več uporabiti za dosego nacionalno začlenjenih gospodarskih rezultatov. Vključeno na Evropo, konvergenčnost južneoevropskih držav ne more več izhajati iz konkurenčnih devalvacij (Toussaint, 2013; Beetsma & Giuliodori, 2010). Da bi dosegli enako stopnjo konkurenčnosti, se morajo države na zelo nizke inflacije, ki deluje omejujo na diskrecijsko uporabo politik (Lane, 2006; Beetsma & Giuliodori, 2010). Zato kljub temu, da je evo fleksibilen na nivoju evroobmočja in preko tečajnega prilagajanja doseže plačilnobilancen evo ravnovežje, to lahko ne odraža, in celo prikrije, ker je znotraj unije. To je odražala EMU, zaradi česar je bila posebej po finančni krizi iz leta 2008 deležna veliko kritik (Rant & Fuhriman, 2017), saj so jo prav notranja neravnotežja naredila ranljivo za zunanje šoke. Kot odziv na krizo sta bili vzpostavljeni bančna in fiskalna unija, skupaj z mehanizmi, ki večajo odpornost unije na krizne razmere, kot sta Evropski mehanizem za stabilnost (ESM) preko stremenja k bolj sinhroniziranemu delovanju držav članic in Pakt za stabilnost in rast (SGP) preko večjega fiskalnega nadzora. Ti torej kompenzirajo za predhodno nedosledno upoštevanje konvergenčnih kriterijev, ki je ogrozilo stopnjo konvergencije EMU, dezintegriranost pa se je v zameno odrazila v političnih in socialnih trenjih, vzponu nacionalističnih političnih strank in trendu bega možganov v jugovzhodu na severozahod evroobmočja.


Rezultate lahko pojasnimo s tem, da je bila v prvih letih uvedbe evra konkurenčnost Nemčije relativno višja v primerjavi z večino držav evroobmočja, ki so se še vedno spopadale z višjo inflacijo (Melitz, 1988), hkrati pa izgube konkurenčnosti niso mogle nadomestiti z devalvacijami (Toussaint, 2013; Beetsma & Giuliodori, 2010; Esposito, 2014; Lane, 2006; Gasparotti & Kullas, 2019). Večja relativna konkurenčnost Nemčije je pozitivno vplivala na njen tekoči račun. A čeprav pozitivno za posamezne države, je to negativno za kohezivnost evroobmočja kot celote. Ta kontinuiran proces je

Tako bi bilo za podrobnejšo analizo smotro analizirati več kazalnikov, npr. skupaj z BDP tudi inflacijo, plačilno balanco, donose javnega dolga ipd., kar bi omogočilo lažjo povezavo med vzroki in posledicami stroškov in koristi evra. Dejansko bi takšna obravnava več kazalnikov bolje odražala namen diplomskega dela, namreč specifičnih koristi za posamezne države, in pomagala opredeliti zmagovalce po različnih merilih. Zato ne zanikamo možnosti drugačnega izida koristi in stroškov evra pri bolj natančnem vpogledu preko različnih kazalnikov in manj dvomljivi metodologiji.


Nazadnje, moja študija opominja na pomembnost dosledno proučenih dejavnikov monetarne integracije, da bi končno razjasnili vprašanje specifičnih stroškov in koristi evra za določene države. Tako sem pregledala teoretično realistične stroške in koristi, ki jih lahko pričakuje posamična država glede na svoje karakteristike, ter jih umestila v zgodovinski kontekst. Potrebno pa je te oceniti še empirično preko kriterijev več kraljev, da bi lahko zagotovili natančne in praktične smernice za ekonomsko politiko. Kljub temu moje diplomsko delo predstavlja strukturiran okvir za razmislko o evropski integraciji, ki zadeva številne aspekte delovanja različnih subjektov, tako ekonomsko in politično kot socialno.