

The crisis revisited: will divergence tear the Eurozone apart?

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Completing Economic and Monetary Union

Panel on Economic Union: convergence in the euro area – a pious wish?

What does convergence mean?

- Convergence within or between countries?
- Convergence in policies or in outcomes?
- Convergence to the same level or compliance with rules?
- Absolute convergence or business cycle synchronisation?
- Convergence on what – fiscal, competitiveness, growth and jobs?
- Economic or political divergence?

Does convergence matter for the Eurozone?

- Accumulation of imbalances and long term divergent prospects → implications for investment, banks, growth/jobs & public finances
- Endogeneous crisis?
- Exogeneous shocks and resilience
- Painful adjustments (internal devaluation)
- Lack of positive spill-overs
- Political consequences

Policy response: the Five Presidents' Report

- Stage 1:

“boosting competitiveness and structural convergence”

“a renewed effort for all to converge towards the best performance and practices in Europe, building upon and further strengthening the current governance framework”

- Stage 2:

“the convergence process would be made more binding through a set of commonly agreed benchmarks for convergence that could be given a legal nature. Significant progress towards these standards – and continued adherence to them once they are reached – would be among the conditions for each euro area Member State to participate in a shock absorption mechanism for the euro area”

“common standards should focus primarily on labour markets, competitiveness, business environment and public administrations, as well as certain aspects of tax policy”

- Final Stage:

“once all the steps are fully in place, a deep and genuine EMU would provide a stable and prosperous place for all citizens of the EU Member States that share the single currency”

Is the policy response adequate?

- Is it fast enough?
- What is the buy-in at member state level?
- Will we see implementation of politically tricky policies e.g. fiscal capacity?
- What political momentum is there for further EMU reform?
- Will the current adjustments achieve greater compliance with the rules?
- Is compliance a good thing? Does the Eurozone pursue the right goals?
- Do CSRs change the relative competitiveness or economic behaviour of countries?
- Beyond a legal framework: what are the political and economic incentives?

Why is progress stalled?

- Poly-crisis
- Not bad enough (ECB etc.) – next crisis?
- No clear distinction between can't and won't
- Distrust: member states & institutions
- No common narrative on causes of and routes out of crisis
- Allegiance to (legalistic) rules and political aims rather than economic rationale
- Political legitimacy/accountability vs. need for stronger coordination

What can be done in economic governance?

- Focus on growth-enhancing structural reforms rather than public finance
- Invest to save
- Golden Rule for Public and Social Investments
- Measuring real returns
- A fiscal capacity to overcome limitations of fiscal space
- Contractual arrangements – Investment and Reform Pact

EMU rebooted?

- Political economy problem persists – legitimacy vs. coordination
- Fiscal capacity/contractual arrangements might break the current deadlock
- Does not create genuine EMU by itself but is a stepping stone on the way
- A positive step in the right direction, resulting in more investment
- A step to rebuild trust, showing that Europe cares for its citizens
- A turning point in the current political crisis?

Thank you

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