The Dysfunctional Nature of the Economic and Monetary Union

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Causes of the euro crisis

- The basic proposition that:
  - On-going euro crisis has not fundamentally arisen from ‘bad behaviour’ nor profligate governments;
  - The crisis is closely related to ‘design faults’ of the Economic and Monetary Union;
Design faults of EMU

- Design faults reflected in the ‘convergence criteria’.
- Failure to consider convergence of real variables (unemployment, business cycle).
- Failure to consider current account imbalances.
- Failure to consider inflation mechanisms and experiences.
Monetary policy and the ECB

- Inflation targeting and the ‘one size fits all’ problem
- National differences in labour market institutional arrangements
- The ECB and the role of lender of last resort
- The ECB and support of national governments’ fiscal policies
Fiscal policy

- The deflationary nature of fiscal policy under the Stability and Growth Pact
- The ‘one size fits all’ problem again with common budget deficit requirements
- The lack of fiscal transfers within EMU
The necessary reforms

- Addressing current account imbalances between EMU countries.
- Policies to resolve those imbalances without resort to deflation.
- Co-ordination of prices and wages across countries
The necessary reforms

- The development of a substantial Federal fiscal policy with tax raising powers, expenditure decisions.
- Substantial could entail Federal tax revenues of order of say 10 per cent of EMU GDP
- Fiscal policy operated on ‘functional finance’ lines, not balanced budgets
The necessary reforms

- European Central Bank to be democratically accountable in a framework of policy co-ordination
- ECB reconstituted to be fully supportive of the fiscal policies of EMU and national governments
Getting there

- Constraints from need to revise Treaty of Lisbon
- Constraints from the neo-liberal agenda of the EMU project
- Constraints from ‘starting from here’