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ON THE NEW ECONOMIC PHILOSOPHY OF CRISIS MANAGEMENT IN THE EUROPEAN UNION

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Abstract

This essay attempts to go beyond presenting the bits and pieces of – still ongoing – crisis management in the EU. Instead it attempts at finding the 'red thread' behind a series of politcally improvized decisions. Our fundamental research question asks, if basic economic lessons learned in the 1970s are still valid. Namely that crises that emanate either from structural or regulatory weaknesses can and should not be remedied by demand management. Our second research question is the following. Can a lacking internal committment and conviction in any member-state be replaced or substituted by external pressure or formalized procedures and sanctions? Under those angles we analyze the project on establishing a fiscal and banking union in the EU, as approved by the December, 2012 Council.

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On the New Economic Philosophy of Crisis Management in the European Union

With the management of the crisis 2012 has brought perhaps more far reaching innovations in the actual workings of the European Union than anything since the adoption of the Maastricht Treaty in 1992. Most important changes, that bear – potentially or actually – of systemic significance include, a/ a fiscal union, meaning the obligatory ccordination and real time control of national fiscal plans? b/ banking union, implying a unified supervisory organ within ECB, with far-reaching competences to act even pre-emtivelény, and without prior consent of national authorities: c/ setting up the permanent bailout mechanism, the European Stability Mechanism, managing over 750 bn euros worth of assets and last but not least d/ bond purcheses of the ECB, including direct buying of obligations of indebted governments, and accepting thsoe as full worth collateral for issuing new credit. The latter implies a quasi-fiscal activity, at the end of the day, monetizing debt, prohibited by the statutes of the ECB.

It is hard to oversee that the strict and far-reaching supervision of banks by the ECB, complementing the European Supervisory Agency, implies a resolute step away from inter-governmentalism and towards supranationalist arrangements. While British and Czech resistance has been open and vocal, other countries may join these in calling for referenda on each or some of the four items listed above. For the present inquiry we still presuppose that all the innovations will materialize, sooner or later, in line with the original intentions. Thus we analyze, what all this is to imply for the architecture and workings of the European Monetary Union, and how current non-members will be able to join in.

We may set out from the premise, broadly documented in our previous writings on the subject, that one of the very few uncontested success stories of European integration has been the introduction of the single currency. It has been complementing the single market, relfecting and also driving the 'ever closer union' in political, symbolic, economic and consumer terms. This success has built on the experience of unilateral peegging of the currencies of small corporatist states to the D-Mark, and later to the conversion of large continental EU members – France, Spain and Italy – to 'monetary orthodoxy', allowing for sustaining their pegs to the D-Mark for a decade and longer. In other cases, as Finland and Austria, the peg actually survived several decades, not just one, before the merging in the euro.

This development has not been built on any specific economic theory, school, or ideology. This holds particularly to the frequently invoked 'neoliberalism' of the arrangement. As it is known, fixing – even more unilaterally pegging – the exchange rate has long been an anathema to the monetarists, dominating the American universities/Friedman, 1953/. Political neoliberalism, triumphing on the ruins of the Soviet Empire, also has could not be instrumental. If for no other reason, that the project had been launched much earlier, and basically by Christian Democrats and Socialists, both coming from the Franco-German statist tradition, and acting through the backdoor of sectoral policies, top-down arrangements as the European Steel and Coal Community and Common Agricultural Policy. As in so many other instances in history, the reslut wasn't an outcome of specific and targeted constructivist projects, but one of social learning, via trials and errors, even if it involved a fair amount of diplomacy and a plethora of compromises/extensively in: Dyson-Featherstone, eds, 1999/.

From the economic perspective it is axiomatic, that if currencies are exchanged on the same rate for decades, the difference among them becomes nominal, notional, restricted to national symbolism rather than any financial substance. The only important difference of a currency union is the irrevocability of fixing. In broader terms it also means that the central monetary authority – the ECB – being exempt – and institutionally insulated – from national political and fiscal pressures – may and do create money and credit, irrespective of the fiscal stance, and irrespective of the business cícle in individual regions.

In so doing the ECB imitates national central banks, which do not conduct monetary policies specifically directed to, say, California or Baden Würtenberg. Thereby the disciplined conduct of solid and sustainable public finance becomes a side-condition not only for price stability, but of overall financial health. If this is more than a postulate, national current accounts become nominal, the same way the export-import balance of Reggio Emilia or Andalusia do not matter for the assessment of public finance of Italy and Spain. Contrary to frequent claims, level of development differences in terms of per capita GDP do not necessarily translate into disintegration, at the past century of Russian, Chinese or US development indicates. Or if it does, it is a complementary – additional, dependent – variable, rather than the fundamental cause.

True, establishing monetary integration prior to – rather than following – political union has been singular to EMU. But at the time of its evolution – which lasted for decades – nothing cautioned against this step, built on decades of trial and error, and decades of successful currenc pegging. Most member-states – except for the notorious trespassers - did introduce structural reforms, did introduce fiscal discipline,did manage to control the expansion of public debt. While these efforts were perhaps more resolute in the 90s, also in 2001 to 2008 debt/GDP ratios stabilized. From the ratio of 68.3 pc in 2001 in 2008 this indicator grew to 70.1 pc only, despite tha major massive bank bailouts performed already in the second half of 2008. By contrast, the failure of later crisis management is best summarized in the explosion of public debt since: by the middle of 2012 the ratio jumped to 89.1 pc. This limit is known to show the limit to where public debt becomes a danger for economic growth .

With the benefit of hindsight one may well ask, how legitimate it was for us, economists, treat political actors as rational agents following the maxims of exconomic theory, largely built on rational expectations hypothesis. While in general terms it was just as much of a phallacy as taking homo oeconomicus at face value, especially pertaining to players of financial markets, who are known to follow herd behavior in most cases. On the other hand, it is hard to deny that a politician, fighting for re-election, is confronted with at least a minimum need of being able to deliver in economic terms in growingly materialistic European societies. This holds all the more so, when – unlike in the UK and USA – the elction system does allow for the entry of new, protest movements in legislation, and even in governmental positions /cf recent advances by Vlaams Blok and of the True Finns/.In other words, politics ceased to be a closed shop and non-performers are being voted down.

Therefore one may not even consider, that some players – behaving strategically – deteriorated economic performance on purpose. On the other hand, it is a novelty of the first decade of the new millennium that at least in some countries, successive governments did shy away from any major restructuring. While this is in line with the ruling paradigm of rational choice in political science, it is very unlike the experience of the entire 1945-2000 period, when major transformations have taken place both in the East and West of Europe. In terms of EMU it is hard to forget that monetary union was in fact a toll collected from Germany in exchange for agreeing to the project of political union/in Germany and EU alike/. Also the track record of the nineties made pledges, commitments to improving fiscal sustainability through welfare reforms sounded credible, plausible and doable in the medium to long run, not least owing to the incentives of an open political system based on exit and entry of new paries/political forces, as this has already occurred in the 1980s and led to governmental participation in case of some former outcasts, as the Greens in France and Germany during the 1990s. This is very unlike the Anglo-Saxon tradition of bipartisan rule on which msot political science models of rational choice are based, thus we cannot claim that incentives for change were non-existent from the very outset.

A Flawed Architecture or a Flawed Implementastion?

In a considerable part of the literature/e.g Daianu, 2012? Mayer, 2012/ the opinion is voiced that the EMU failed because it has ben built on sand. On the other hand, not only our introduction above contrasts with this view. The fact , that fixed exchange rates could co-exist for severtasl decades, is itself an indication, that the foundations are solid, workable, unless major trespassing occurs. In other words, there is no need for the complex surveillance and enforcement mechanisms, which have developed in the Treaties of Maastricht, Amsterdam, Nice and Lisbon, to ensure fiscal compliance. As the detailed description of the system shows/de Haan et al, 2010/ if fiscal prudence – as a form of selfish behavior – prevails, compliance is ensured even in the lack of surveillance and sanctions. And conversely: if there is no committment, if there is no conviction of the inhertent uses and value of behaving well, trespassing will be the rule. The more rigid rules emerge to punish non-compliance, the bigger deviations – and the stronger the incentive to non-abide – will be. If a country does not want to relapse in the inflationary policies of the 1970s, it will avoid, on its own, and without any external disciplining, the explosion of debts, public and privat, in order to forestall the inflationary outcome, which is in the medium run inevitable in all economic theories.

Furthermore it also follows – especially in the resurfacing Keynesian framework of thinking – that governemnts may spend themselves out of recession only under two severe conditions. 1. There are a number of underutilized and competitive capacities, which are quick to be used once effective demand allows for that. In other words, recession is cyíclical, rather than structural. It is hard to believe, that say, the car industry in germany or the real estate market in Spain was under such conditions in 2008-09. 2. There is sufficient elbow room, created by the debt reduction strategies – results rather than proclamations – in the preceeding period.

As we have seen above , in 2001-2008 next to no improvement happened at the Eurozone level, despite improvement in some small economies. Founding fathers of the euro therefore wondered, if all the necessary structural reforms will indeed be realized in the weaker countries, in order to pre-empt fiscal derailment/Issing et al, 2004/. And they were quite right, and were saying so before.. However the non-reform scenario – which did happen in the South – was not replicated in the North, not even in the poor Baltic states.

What has added to recieved wisdom, as summed up above, the study of ongoing crisis management in the euro-zone? Without re-stating earlier accounts/Palánkai, 2012; Csaba, 2012/ we may advance, that some countries fared pretty well. These were the ones which did follow – not only preached – rules-based fiscal policies, which did attain price stability – not only in statistical terms of headline inflation but also in terms of underlying factors - and ones which did care about the stability and solidity of the banking sector, even if the latter falls outside the scope of public finance, regulated by the Stability and Growth Pact and other EU level fiscal arrangements.

In short, these countries – including Slovakia, Estonia, Luxemburg, Austria and the Netherlands – avoided the minimalist approach that reigned in the problem countries. By the same token it did not require additional efforts – over and above the one taen on their own initiatives – to deliver and meet all conditions laid down in the Treaties. Let us be explicit: those who survived the crisi in good shape were not the ones who adhered to EU rules of the game. They tended to outperform, on their own, the commandments of stability and sound conduct of public finance and banking supervision. It is known that for instance Belgium and Germany regularly missed the debt criterion of SGP, without heading for trouble. By contrast, Ireland, estonia and Spain, while being excellent pupils in terms of fiscal stringency, did all suffer from the tremors of 2008-2012 period.

We may observe, already at this early stage, that the escalation of the previously hidden crisis of public debt in the EU can and should, by no menas directly related to the concept or the architecture of EMU. It also does not allow for those wide ranging generalizations, which emanate mostly from the British daily press – traditionallly hostile to EMU – that the whole project were ’unworkable’ or ’hostile to realities’ or followed a ’flawed design’. As we have seen, countries at various levels of development, various cultural backgrounds and various political orientations managed to live quite well with this ’crazy arrangement’.

Therefore we cannot subscribe to the view, expressed by respectable authors/Laski-Podkaminer, 2012/ which declare the very criteria, rather than their application, to be infeasible and unpracticable. We also do not see any proof for the classical claim by Feldstein/1997/ that regions with uneven levels of development and unlike economic structures were unfit for a currency union. The latter statement is simply ahistoric, as the examples of the Austro-Hungarian Monarchy or the Ottoman Empire demonstrate. None have seen any convergence in terms of regional per capita GDP, and none of them collapsed for this reason. On the contrary, both of them flourished for several decades, until a lost World War One led to their partition, the same way the Holy Roman-German Empire was dismembered in 1806 by Napoleonic conquest.

In fact, economic history cautions us from buying in the claims of neoclassical models in terms of convergence, as it tended to be the exception rather than the rule/cf China, Russia, or the USA proper/. In historical statistics what is observable is not convergence in the long run, but an ongoing change of relative positions of countries, with some – but very few – maing big advances, others – also a few – lagging behind, and a large number remaining in unchanged relative positions/cf more recently Acemoglou and Robinson, 2012/. This book also invokes the long forgotten insight about the relevance of historic conditions, quality of institutions and social value sets in explaining the outcomes, against factor endowments and other mechanistic variables. If we do not expect convegence, a rare event in history, to repeat itself, than a non-convegence per se has no message for the EU, its crisis management, or even the global economy’s prospects.

In our case it is easy to see: invoking level of development differences is though intuitively strong, it is still a fallacy. Estonia, which is about Hungary’s level of development in terms of per capita income, managed to overcome the crisis at the cost of one single year’s recession, and growth resumed in 2010-12. The country did join EMU in 2011. By contrast, much wealthier old EMU states, like Italy, Spain and Ireland, have still been suffering from repercussions of the crisis at the time of writing. In sum, the reference to level of development as a major explanatory factors imply does not hold, no matter how widely held a claim it is. The factors other than the ’flawed EMU architecture’, ie the much cited ’one-size-fits-all’ proposition needs to be revised.

Common currency and structural reforms: which way goes causality?

There are two complemenntary insights emanating from the every growing industry of crisis explanations, produced by international agencies and think tanks alike. On the one hand these support the original propositions formulated at the time of launching the EMU project. These suggested, that joining in a currency union has though overwhelming benefits for the overwhelming part of players, however it also entails risks. Should countries not be able or willing to persue price stability as an organic outcome of macroeconomic interplay, and thus should they be unable to sustain what used to be the unilateral peg of their national money, might run into trouble. All the more so, if they do not make up for the loss of monetary and exchange rate policy instruments for targeted fiscal policy intervention, structural policy and liberalization of labor markets, as well as rendering welfare arrangements sustainable financially, the de-railment is no longer an if, but a when.The SGP, the Broad Economic Policy Guidelines, the convergence and stability programs, as well as the more recent innovations as the Fiscal compact and the newly launched project of a fiscal union all point in thsi very direction.

The basic counter-argument may go as follows/cf eg Muraközy, 2012/. The size and modalities of the welfare state, and expectations for the state to provide welfare services on citizens' rights, have long been built into the preferences of most of the elctorate. Thus welfare states represent revealed preferences of the majority, thus any attempt to cut them back radically is likely to founder. However, as the same article documents at great length, structural changes in expenditure patterns and incremental changes towards more fiscal sustainability of welfare provision have already made ways in the years preceeding the financial turmoil, in old and new member-states alike. It is equally important that labor makrets have started to become more flexible and provision of social benefit becoming targeted, often means – tested – the German Harz IV and the Dutch polder model being perhaps the best known, together with flexicurity, the Danish concept elevated to the level of EU polices/van Rie and Mary, 2012/.

As a second, distinct group we may list those countries, where teachings of basic marco-economic textbooks were taken perhaps too much at face value. At the level of financial theory, the efficient markets hypotheses/Fama, 1970/, at the level of policy practice, the conduct of low interest rate policiey at good times and bad, and the avoidance of any burst of any bubbles, as practised consciously by Alan Greenspan/2008/, shaped much of the outcomes. However, opportunism – or simply following intellectual and political fashions – does not follow from the original monetary model of integratiomn. On the contrary, at the abstract level both fiscal and monetary policies should have been focused on medium to long term events, asaging or implications of the debt overhang, or ramifications of exploding private debt, be tht in construction or banking. Thus we are less than surprised to note that staunchest critics of EMU emerged from the libertarian camp, as Milton Friedman, Václáv Klaus or Martin Feldstein, all calling any rules-based policy – and especially the irrevocability of exchange rate peg – as the triumph of politics over economics.

While analyses on the de-railment of Greece and Italy abound, to which we may add only new data or anecdotal evidence, there is much less attention devoted to the second group. This includes in our reading Spain, Ireland, Romania and Estonia. The common feature of those economies is that stringency and regulation applied to the public sector only, therefore their fiscal accounts looked OK at the time of eruption of the crisis. By contrast, the private sector – which accounts for a considerably larger part of GDP in all European economies – remained largely unregulated. This was particularly noticalbe in the financial and banking sectors – the latter two overlapping to a considerable degree. The staff of Irish financial regulatory agency added up to three professionals, symbolizing the largely ideological fear of the Irish government from any reguilatory intervention in financial markets/more on that in: Connor and O'Kelly, 2012/. This was perhaps a case of taking the non-interventionist stance of contemporary mainstream economics too much at face value, even when deciding over practical matters.

But it would be wrong to invoke, as usually, the 'too big to fail' argument. In the case of Spain the regulation was truly meticulous, covering the ministry of finance, the central bank, the supervisory authority, regional governments, savings' banks and also large transnationalized banks, following international accounting standards closely. With reference to these arrangement the Zapatero government repeatedly announced during 2009-2010 that finances of both the autonomous regions and of the savings' banks, financing those and much of the population, have been solidified and sound. This claim was barely credible, given the structure of Spanish boom of the 2000-2008 period. The latter was based largely on tourism and the construction industry, with banks lavishly financing both, in line with the Zeitgeist. This was only exacerbated by the interbank operations, largely unrelated to financing the real economy, which rendered the formally strict national regulation hollow. Local savings' banks were though tightly under governmental control. However their supervision was often void of elementary professional skills, let alone personal integrity, as these were intimately intertwined with the ruling class/Garciano, 2012/. Thus the tremors triggered by the spillover of global financial crisis should not have been surprising at all.

The situation was in many ways comparable also in Romania and Estonia. In both countries one could observed a large degree of overheating in 1999-2008, including the non-applying of available brakes for cooling the economy, combined with very liberal application of regulations, if at all. As a consequence, prudent fiscal policies proved insufficient to forestall macro-economic de-railment, compromising the performance of the entire decade. According to the statistics of the ECB, Romanian public debt in 2008 stood at the low of only 13.4 per cent, on par with the traditional champ, Luxembourg. In Estonia virtue was even more pronounced, with public debt running at 4.5 per cent of GDP in 2008, which must be a world record of the year. Thus the situation of the two NMS is comparable more to Ireland than to Spain or Italy. This parallel implies, that troubles accumulated in the private, rather than in the public, sector, with economic policy/ideology leading to a hands off stance – something we may term a new brand of macroeconomic populism.

Without getting into the nitty-gritty of individual stories we may well ask at this point: if the pattern of crisis is similar by the countries, is it not an immediate proof of the failed construction of EMU? Is it not that the limited focus – on public sector finances only – is at the root of subsequent troubles, that resurfaced in the private sector?

This suggestion does carry a modicum of truth. However it seems to neglect salient features of the EU. In short, especially following the ratification of the Lisbon Treaty in all the 27 MS, the EU has become even more intergovernmentalist, than before. Final decisions rest ultimately with the respective national legislations, not with any of the common organs/with the proverbial exceptions of ECB and in some cases the European Court of Justice, passing directly applicable rulings/. In order to pre-empt fiscal trespassing, therefore one option is to adopt national fiscal rules, mirroing SGP/Benczes, 2011/, as later stipulated by the Fiscal Compact of March, 2012. Or alternatively, we acknowledge, that national an EU level legislations co-exist, and any joint legislation must be anchored in inter-governmental agreements, open and explicit transfer of sovereignty, which remains the exception rather than the rule/more on that in Vörös, 2012/. The comparison of Spanish to Irish cases warn of the threats inherent in both under- and over-regulation, especially in the financial sector, as well as of the landmines of too cosy relaionships between the financial sector and its regulators, which may lead to conflict of intereest situations more often, than postulated in integration theory.

This of course means that setting up a joint supranational supervisory agency over all major European banks in the framework of the ECB, is going to be a formidable task, with a series of regulatory competences, procedures and other practicalities to be settled. The fine print is likely to matter more than the general declarations of intent. The compromise of December, 2012 consists in the following: a/ only about 100 'systemically important' banks will be under direct ECB supervision; b/ thus most of tthe rest of the 6000 units in question remain under national supervision c/ as a rule, bail-outs must be fundd from national coffers and d/ there is a cap on the use of ESM funds and serious pre-conditions for their use . True. The 'unlimited liquidity provision' of ECB may render all the brakes illusory, at least in the medium run.

Let us underscore: supervising banks, with cross-border authority, and the right of pre-emprive action is anything but a technical matter, as suggested by the working documents of the Commission in their various editions in June-December, 2012. The arrangement, to be elaborated and implemented by January, 2014 is about competences, about ways of overcoming collkusions across national legislations, about ways of managing drifts between EU and national arrangements, and not least about hundreds of billions euro worth of assets and the way these are manged. If all these were to be vested with the second leg of the ECB, and empowered with the exceptional jurisdiction of the ECJ, allowing for immediate validity without proper instances to appeal against them, these steps would transfer an exceptional degree of sovereignity to un-elected supranational organs.

Let us note: already the bailout fund – ESM – of 750 bn euros, and the fact that since the December 2012 Council the ECB may directly intervene in troubled banks, with its money transfer not showing up in the accounts on national public debt, the transfer of sovereignty, way above the curernt 132 bn euro or 1 pc of GNI, has already materialized. Further sovereignty transfers would require elaboration of the fine print, as formulated above, and perhaps, in several countries, a referendum or decisions of the Constitutional court on the legality of the arrangement and on the proper ways of inserting these steps in national legislation. Not only the UK, but the Czech Republic, the German Constitutional Court and a number of smaller countries, including Slovakia have already voiced their concerns. The fear of smaller states to be run over is palpable and legitimate. Poland and Sweden have already voiced the view that non euro-zone memmbers should have voting rights in all matters pertaining banking.

This concern is rooted in the fact that banking is already de facto transnationalized, thus any measure pertaining to eurozone members are of direct concern to the rest. For instance in January, 2009 when Ireland unilaterally declared a general deposit insurance by the state, irrespective of the size of the holdings, this had to be genertalized in hours rather than days, irrespective of the weighty moral hazard considerations that could have cautioned against such a step. By contrast, the one country-one vote principle may create situations where Cyprus or Latvia could veto a complex deal hammered out by others via a series of tough compromises, for reasons that may or may not relate to the substance of the deal. In the opposite case the 'one money, one market' principle, with supranational regulation, may simply pre-empt basic features of national sovereignty in fiscal matters, but also – in banking – for the private sector.

On the changing role of the ECB

Financial market analysts and policy-makers tend to be positive about the change brought about by the new, Italian President of the ECB. His predecessor, Jean Claude Trichet was mocked by his critics to be „more German as the Germans" because of his committment to the independence of the ECB and the single-minded focus on preserving price stability – while avoiding deflation – which he in fact succeeded. Defying the spirit of the ECB being an „augmented Buba" as well as the letters of its statutes, the ECB has gradually relapsed into a seires of quasi-fiscal activities. Emulating the practices of the FED rather than the Bundesbank, the ECB first purchased debt obligations of troubled eurozone members on the secondary market.

It also instituted a series of liquidity enhancing measures. Since September 2012 it has been actively involved in buying government bonds on the primary market and providing 'unlimited amounts of liquidity' to save toe single currency. The December, 2012 Council approved the practice of buying directly assets of troubled banks, thus 'saving' on the published gross deficit numbers of the home country. While the latter is good news for money markets, bad news for anyone concerned about basic principles of proper and sound accounting, at micro and macro levels alike. As one observer put it aptly, the ECB has never been so powerful in terms of market standing, and never been so weak in terms of independence from the daily political considerations – in theoretical terms its independence has become a fiction/Schnaas, 2012/.

On the more abstract level of economic theory, it has never been seriously questioned since the late 1970s, that the Keynesian type of demand management is meant to remedy cyclical ills only. By contrast structural and reguatory weknesses and the troublées emanating from these can, neither in theory nor in practice, be cured by easy money. Not onyl the experience of western Europe, but also of Japan in the 1990s vouch warranty for the validity of this insight. And we argued in the previous section, that over- and underregulation, as well as structural flaws and policy blunders, not external shocks were behing the recession of 2009 in the EU. This situation is only exacerbated by the fact, that public debt continues to grow, basically in all three major poles of the global economy- that is not just in the EU, but in the USA and Japan alike. While EU debt is to peak with 90 pc of GDP, the USA figure is around 105 pc and that of Japan 240 pc.

True, we do have excellent students in class of the EU, such as Luxembourg, Estonia and Slovakia, but these regrettably do not include any of the four major economies. Moreover public debt continued to increqase in 2010-2012, when the global financial crisis was already over. While IMF data show an increase of global output in the range of 3 to 5 per cent per annum, there is no sign of the – in theory concommittant – declining debt rates in any of the three amjor locomotioves of the global economy. Governemnts have long forgotten the maxim of Lord Keynes on the symmetry of fiscal policy, let alone the even stinger maxims of the Austrian school or of monetarists.

This is quite a problem insofar we accept the compelling arguments why global imbalances tend to be managed by the surplus of one region counterbalanced by the deficit of the other/Feldstein,2008/. As the above cited article proves convinclingly, aiming at a global 'general equilibrium' in any point of time would automatically trigger a world-wide recession, with both surplus and deficit countries suffering in an unnecessary manner.

What is indeed a major source of trouble that in most of the global economy it is not only the government, but also the two other principal agentd of the macro-economy which run structural deficits- i.e households and corporations alike. In short, the textbook identity on the overall balancing act across the three major holders of income. This is a problem, as long as we have relatively few countries like Saudi Arabia, running a structural surplus in savings, against many countrries like the USA, where deficits of all three major players are structural.

It is hard to question that if there is not sufficient voluntary savings at the global level, financial intermediation has nothing to channel. If this phenomenon is structural, emmission of credit and money may help only in the short run, and the ramifications already in the medium run are devatating.

For the time being we are entering in a paradoxical situation. While IMF statistics show an annual growth rate between 3 and 5 per cent, which is quite considerable in historical standards, both fiscal and monetary policies continue to be lax and expansionary in all the three major centers of global economy. One may comment, that this at least avoids the unhelythy mix of the early 1980s, which lead the US to a recession at the time. But this is a cheap argument. If both legs of economic polices continue to be expansive at times of growth, the revival of inflation is just a matter of time, not a matter of 'if'. Furthermore if the economic lull is due to overextension of household and corporate debt, or of weak innovation, or other structural factors, including the non-caclculability of overall economic condiitons, weak supply may co-exist and supplant extensive availability of money and credit. And this is precisely the established recepie for stagflation, known form the 1970s. This danger is so imminent, that – following the clasical Lucas Critique/1976/ all holders of money and income are well advised to refrain from sopending- which turns into drying up of money markets.

Thus it is hardly surprising that in his Nobel lecture the renown financial economist Thomas Sargent/2012/ draws a parallel to the current state of EU with the pre-civil war, confederative USA. The parallel is established on the grounds of the US confederative budget accounting for about 1 pc of GDP, i.e comparable to that of current EU. The basic difference to history is that the US of the day was by no means a welfare state, unlike most of EU states today. His conclusion is thatz an efficient solution to the debt problem is by and large the opposite to what we observe in the EU today. Instead of providing unlimited liquidity the solution is the ensuring of the no bailout clause – the single, non-replicable experience of a bailout, just the opposite tot what we observe in Greece and other indebted nations. By contrast the US has never bailed out any member-state, irrespective of its political ramifications.

It is less than trivial, if the German-inspired practice of trying to offset the dire consequences of the policy of easy money can be countervailed by the unification and more rigid application of EU level rules and regulations. The underlying factor is not just the different debt dynamics of the EU member-states, but also their divergent social and welfare models. For this reason both the pattern and dynamics of public spending is unlikely to be liable to joint, unified handling, let alone their union.

The latter observation holds also for the Unites States of America. As it is known, individual states have different social and fiscal practices, with federal level welfare initiatives surfacing only during the Obama administration/perhaps not at the best concievabvle point of time/. As long as the political union iin the EU is still a very long way from anything comparable to even a weak federal state, thus outsourcing fiscal responsibilities to technocratic agencies, as suggested by many, is not a realistic option. Therefore EU organs, be that DG EcFin or the often propsed budget tzar, can and should not act, as if they were representing a supranational authority, where it is the packaging of intervention which matters, not its size or justification.

As long as different countries exhibit different preferences in terms of public spending and related public provision of services, it is difficult to support the idea of a fiscal union, aimed at improving the cosmetics of public finances in well defined group of countries. The preliminary agreement of June, 2012 pointed to this direction, while the compromise in December, 2012 have actually prolongued its implementation to undefined later periods of time.Thus the sustaining differences in the pattern of both spending and revenue generation limit the unification of procedures and even more of standardizing major items on the Union level. This holds irrespective of the motives behind unification, also in the future.

On the Drivers of Money Markets: Fundamentals, Appearences and Beliefs

Analysts of real –as against modelled – money markets have long tried to supersede the world of simple, non-testable axioms. They based their views on actual observations of mass behavior in empirical psychology and adopted behavioral finance approaches. Following Ludwig von Mises they took herd behavior – rather than unlimited rationality – as the basic feature of workings of money markets. This translates into the focal role of perceptions, beliefs and expectations – phenomena which are testable and observable on the ground, thus are in no need of being assumed or assumed away.

The crisis of 2008-2009 has revived the old question: what is the point of elaborating 'iron laws' that apply to computer displays or paper only? For one, the assumption of efficient markets was that markets do react 'instantenously' and punish ruthlessly each and every trespassing. This logic did work in the minds of the founding fathers of the EMU, who presupposed: it is rational for policy-makers to reform rather than risk the storm of global capital markets. The example of Greece and other EMU de-railments implicate: this was a conceivable but by no means compelling argumentation. Could have worked, but has not worked on the ground. One may wonder, for how long may – at least some high profile – economist boast of economics NOT being an experimental science? How long may the pre-occupation with coherence at the expense of reelvance- testability – susrvive as the supreme academic maxim?

Thus it would be difficult to over-rate the explanatory power of socio-psychological/soft/ factors in the interpretation of fianncial market outcomes in real world economies. It is well established – at least since the 1920s – that appearences and perceptions matter more than fundamentals in triggering actions –especially mass reactions – on the financial markets. Crashes on the stock exchange invariably follow gossips and panics, rumors and misinformation, sometimes spread on purpose, sometimes just correcting preceeding 'safe bets',a s was the case on the burst of the dotcom bubble in the early 2000s/but also in the old times of the tulip craze/. It is also recieved wisdom that fluctuations follwing from information asymmetries are inherent features of the market economy, as long as we follow the old distinction between calculable risks and unforseeable, thus uncalculable uncertainty. The latter is a basic feature of money markets, and negating this feature – by attempts to calculate, quantify and thus exclude all potebntial uncertainty – has surely been one of the falalcies of financial economists over the past four decades. Appreciating this feature would make us rather cautious on the possible applications of the 'macroprudential approach' thet recently dominates thinking on global financial regulation.

In short, the substance of the macro-prudential approach/Hanson- Kashyap-Stern, 2011/ is the extnesion of provisions for solid banking behavior including the responsibility structures, to the macro-economy, and in theory the global economy. The attempt at creating the banking union in the EU, discussed in the preceding section, is a case in point. The underlying idea is the belief that such arrangements may, and indeed will, pre-empt the recurrance of global financial crises. It would be wrong to deny that appropriate precaution and provisions limiting excessive risk-taking in banking may and do contribute to ex post damage control. Still it would be naive to theorize that any regulator could, even in theory/let alone in actual practice/ pre-empt the problem of fundamental uncertainty and resulting lack of foresight at the systemic level. All the less so, that informational asymmetries and imperfections tend to accumulate, with informational noise and misperceptions adding to a series of negative synergies, which render actual foresight highly imperfect in any real world situation.

If this insight holds, even in part, in line with the insights of Austrian economics, but also in line with empirical studies on financial crises, than the attempt to overcome the contagion of fianncial crises in Europe through the centralization of supervision is likely to prove a dead alley. While it is re-assuring to find that the Council of December, 2012 rejected the over-ambitious idea to create a single supervision for over six thousand banls, it is hard to oversee that the compromise is based on concessions to the UK rather than theoretical insights. Also the need to accomodate the German taxpayer against his fears of a snowball of bank bailouts, rather than the basic acceptance of limitations on centralized controls which shaped the decision to constrain ECB oversight to a mere 100 financial institutions 'of systemic relevance'. By contrast, recent literature/Dürr and Elsig, 2012/ strongly emphasized the relevance of principal-agent problems and theuir accumulation in EU policies, even in areas where much less money and power is at stake.

In a political economy approach thus we should not disregard the agency problem, nor the issues of political conflict and lack of professional and personal integrity, issues that usually fall outside the scope of technical econometric analyses of EMU troubles. The role of the latter are quite obvious in the case of successive Greek governments/Visvizi, 2012/ but we have already indicated the relevance of those items in the Spanish and Irish cases in terms of difficulties, and in the Estonian and Slovak cases as favorable feedbacks, stemming from credible committment of lacal governments over a single electoral cycle.

And this leads us to the fundamental question. As long as the EU falls short of being a supranational body, how far its stipulations may go in delivering good performance, when domestic committment of actors is lacking, on a number of grounds? As detailed analyses/Győrffy, 2013/ explain, in cases when social and professional consensus translates into high levels of committment, lacking formal fiscal institutions have not compromised prudent macroeconomic policies, as in Slovakia and Estonia. In the contrarian case existence of formal institutions, sanctions and meticulously elaborated procedures could not forestall degradation- not only in Greece, but also in Italy, and as more recent warnings indicate, also in France.

Following the logic of German ordoliberalism we may offer a solution is the proper sequencing of individual measures. Thus orchestrating professional and social consensus should come first, and policy committment, later institutiolaizing the latter comes as second and third. Else the cart is put in front of the donkey. For instance, the United States of America has one of g the eldest independent fiscal control organ, the Congressional Budget Office, set up in 1974 in reaction to the first global crisis. Likewise in Germany debt ceilings and corrective rules are anchored in the Constitution. The availability of watchdogs, however, could not prevent the explosion of public debt, reaching 105 pc of GDP in the USA and over 90 pc in Germany. By contrast, in Luxembourg and Estonia lacking institutions have not translated into fiscal de-railment. Similarly Latvia and Slovakia acted in a resolute manner and attained a quick recovery in 2010-12 period.

From this line of reasoining it follows, that efficiency of economic policies is much more contingent upon societal anchoring and professional consensus than the reference to one or other school of economic ideas. However, this claim is non-reversible: wrong or too abstract – and thus non-applicable – theorems never breed economic success. Reference to lack of effective demand at times when regulatory failures strenghten structural weaknesses is a case in point. Likewise the unwillingness to bear the burden of mistaken decisions by the shareholders is always a policy blunder in a non-socialist economy.

As we have seen, the longer the unhealthy twins of lax fiscal cum lax monetary policies prevail, the deeper is the suspicion of private markets on the ability and willingness of governemnts to manage their debts. Therefore the doubt, if private and public debts can be parallely managed is also gain in relevance.And this is not only because of the exceeding of the historical limit of 90 pc of debt/GDP ratios/Reinhart and Rogoff, 2011/. The deteriorating quality of Japanese, French and American debt also exacerbates the problem.The downgades that reached not only major US banks, but also the EFSF and ESM, as well as of France are already warning signs for this.

This only underscores the relevance of psychological factors in both creating and solving the crisis. Without acknowledging the problem there is no remedy- Greece, Italy and Portugal are excellent examples for this insight. On the other hand, chronic fear may also lame action, as the cases of France and Hungary may illustrate. We may only reach, through trial and error, where the optimal level of crisis consciousness emerges, which is a state of mind which mobilizes rather than freezes action.

This insight is reversible. No matter how much fundamentals improve, if this is not appreciated by society at large, the government maanging the process is likely to be lost. Improving actual performance is thus a necessary, but by no means a sufficient condition, for sustainable sound economic policies. This is bad news insofar as adjustment measures initiated in southern Europe and in the large member states have already triggered a series of protest all across Europe. While economics has become non-accessible – owing to its over-emphasis on formalization – the demand for populist suggestions, offering single measure once for all solutions is on the increase. Reviving bad – and mostly failed – theories are unlikely to help, as is the case with the usual practice of ongoing policy improvisation in most of the EU states.

One of the concievable conslusion of ourt analysis may go as follows. On the base of empirical observations and of established, testable theories, it is possible to develop an economics which is perhaps less elegant than the mainstream, but is more relevant to solving the crisis of the EU. This applies to both to the level of interpretations and policy recommendations, or more simply, to the descriptive and normative planes. This new approach may be, what the German proverb calls, identical with the long forgotten old one, a systemic approach or Ordoliberalism.

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