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An historic view over the current European economic troubles

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Abstract: The financial crisis sparked after the Lehman Brothers bankruptcy has caused havoc in the international economic system. Although, since then, the vast majority of the world has recovered, wide parts of the European Union are underperforming. The aim of this research is to tackle the issue of poor economic performances in Southern Europe, with a focus on Italy, disclosing many topics that are not well known by a not academic audience. In the research, I am first going to describe the political process of the post-war period, then it is proposed an overview over the following decades. Finally, two trends are described as critical sources of the crisis that hit the PIIGS. I conclude drawing the attention upon the political reasons that might have led the Euro project to take place.

Key words: Euro, current account asymmetries, Optimum currency area

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Summary

Introduction – Motivation

This research aims to investigate the economic trends of the last years in Europe emphasizing the outcomes of the single currency in the continent. The motivation behind this study is mainly to be related to the poor quality of the mainstream debating that is taking place in Southern Europe countries. So far, policymakers, journalists and a certain degree of analysts have claimed that the real drivers of the poor economic performances of the last years are due to cultural and structural problems.

However, the nature itself of the current monetary experiment appears to be less discussed in newspapers and talk-shows. Already in the past, many academics warned Europeans politicians about the scientific doubts that a European single currency rose during the post-war period. *"If there was ever a bad idea, EMU it is"*. With these words, Rudiger Dornbusch *(1996, p.124)* stated his thoughts about the Euro project. Writing in 1996, he described the process of monetary union that took place during the 90s. Although the European countries undertook the unification project to achieve more stable relations, the last years have seen a progressive destabilization within the union. During the turmoil in the international economy during the crisis in 2008 and 2010-11, in an unhappy definition, the international mass media labelled the underperforming countries PIIGS –Portugal, Italy, Ireland, Greece, Spain. The description of these population as historically weak and lazy could be translated into specific economic terms, whereas European institutions and core economies blamed low levels of productivity, high public debts and structural problems as actual reasons of the difficulties in Southern Europe *(Bagnai, 2012)*.

However, it would be misleading to pretend that these are the only causes of the economic troubles. Indeed, researchers rose doubts about the single currency project since the very beginning. A countless number of well-known academics professed their worries about it. Not only Rudiger Dornbusch, but also several others published scientific works opposing the introduction of a single currency in Europe. Krugman *(1998),* Feldestein *(1997)* and Salvatore *(1997)* are some of the most famous amid the ample range of critics. They analyzed the features of European economies and the option, for economies that differ, such as European ones, in labor markets, fiscal rules and taxation systems, to adopt one single currency. Krugman immediately recognized the danger that Europe approached: *"But EMU wasn't designed to make everyone*

happy. It was designed to keep Germany happy - to provide the kind of stern anti-inflationary discipline that everyone knew Germany had always wanted and would always want in future" (Krugman, 1998). The historical German unwillingness to inflate is the principal problem of the Euro sustainability. Surplus countries, to maintain a neutral - neither positive nor negative - balance of payments and to keep the financial stability of the area, should inflate. On the other side deficit countries rely on the inflation of surplus countries in order to achieve growth and full employment *(Mundell, 1961).*

Productivity disparity amid countries is one of the main issue is often debated. The comparison between Germany and the Netherlands with the rest of the continent, and particularly with Mediterranean countries, reports an overwhelming advantage and better performances of core economies. Those that sustain the Euro struggle, or refuse, to implement the effects of the single currency into their analyses.

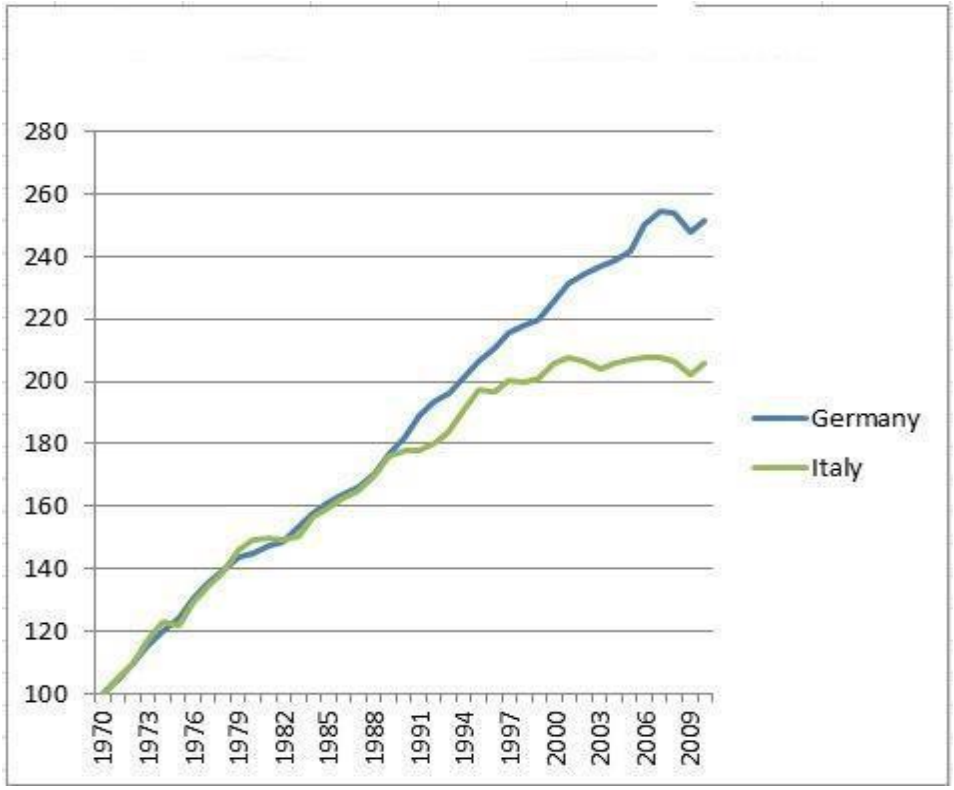

Figure 1. Labor average productivity in Italy and Germany from 1970 to 2009, Source: Labor productivity index, OECD

Figure 1 shows part of the issue. As can be seen, the productivity trends of Germany and Italy followed an identical development for most of the post - Bretton Woods years, from 1971 to the end of the 1980s. Only from the start of the 1990s the two lines have different tendencies. Unfortunately, this figure is not well known at the big audience and as it seems by Giordano et al. *(2015)* who argue that inefficiencies in public governance are one of the main sources of poor productivity performances. Although they are correct in underlining Italy as a very inefficient state, with a huge waste of public money and resources, they forgot to show the broader figure. Indeed, in their main tables, they only report data from 1998, when Italy began to underperform if compared to other developed countries.

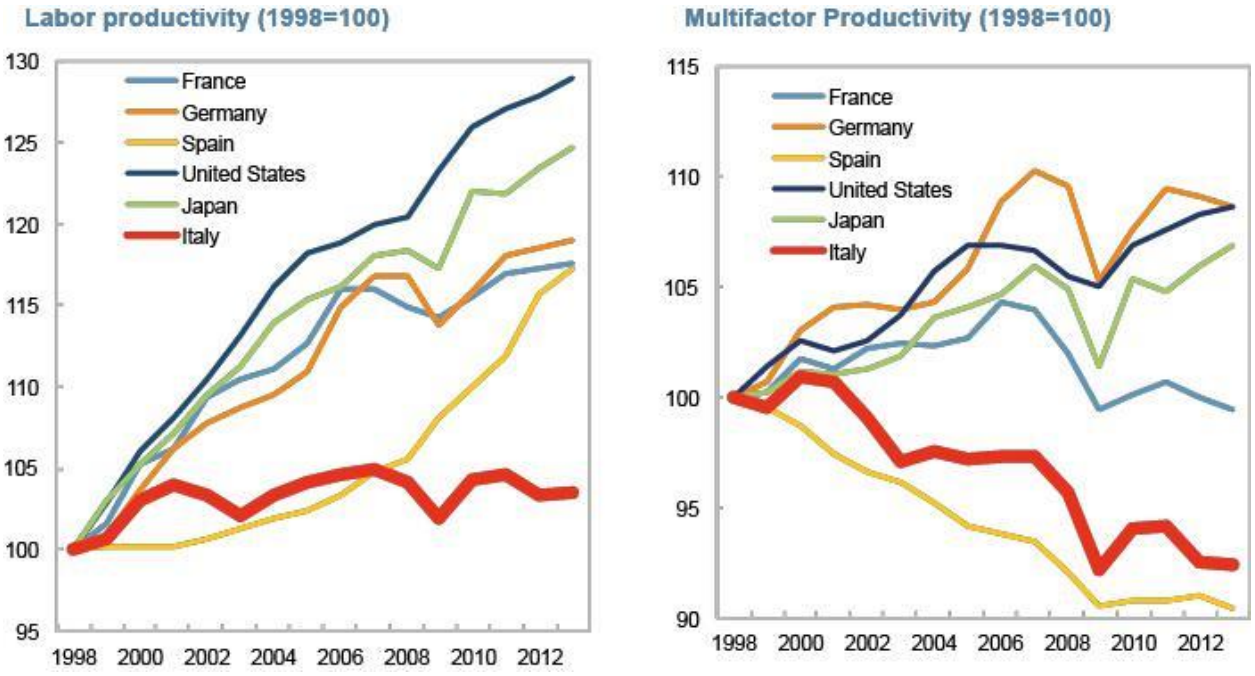

Figure 2. Labor and multifactor productivity, from Giordano et al., 2015

Figure 2 is the main point of the article published by the researchers. As just said, it presents many weaknesses (and it appears to be biased as well). As widely known, Italy has never been a virtuous state. Clientelistic ways of doing business and a nepotistic political system have always distinguished the country. Furthermore, since the unification of the 19th century, a marked difference between the northern and the southern part has featured a nation that has in this dichotomy the central element of backwardness. However, the fragility of their argumentation stands out once the fiscal situation is more deeply analyzed. During the 1980s, under Craxi and Andreotti governments, the public debt skyrocketed from 50% to 100% of the GDP and the

public expenditure rose from the 4% in 1965 to 12,5% in 1985 *(Sapelli, 2012, p 123)*. Even though inefficiencies in public governance and an incredible waste of public money were the daily routine in those years (the decade ended in the scandal of *Mani Pulite*, which swept out several of the old political parties), figure 1 illustrates an extremely positive development. Thus, someone may wonder, why if these features have always characterized the Italian economy, only in these last decades the productivity growth, and the economy more broadly, is experiencing a slowdown. Italians did not become corrupted or lazy at the turn of the last decade of the 20th century. They were not the most virtuous country in the previous time neither.

A further main argument that is widely proposed as one the crucial structural problems is the issue of public debts in Southern Europe, which is probably the most criticized aspect by European institutions. Even though it is doubtless that the public debt of some countries skyrocketed, as Bilbow underlines *(2013)*, if compared with the rest of the world the European financial situation does not look to have especially bad shapes. The Fiscal Sustainability Report, published in 2015 by the European Commission, conclusion might seem surprising to many. Figure 3 derives from a study carried on upon few determinants of fiscal positions, public expenditures correlated with projections of population ageing issues. It can be easily seen that Italy is the only country in Europe with both sustainable long-term projections and with the favorable initial fiscal position. Thus, it appears that some measures adopted by politicians, and partly imposed by international institutions, do not find approval into this research. Moreover, the very same report states: *"there is only one country (Ireland) facing short-term challenge to fiscal sustainability stemming from the financial-competitiveness side, and another one (United Kingdom) facing short-term challenges stemming from the fiscal side" (Fiscal Sustainability Report, 2015, p. 65).* Thus, high levels of public debt do not worry the European Commission. Further evidences come from Japan. Its economy, indeed, has always been featured by highly competitive firms and by low unemployment rates. However, the public debt is the highest amid developed economies *(Graph 1, Appendix)*, which, despite all, has compromised the well-being of neither the country nor the Japanese population. The determinant, thus, seems to lay in other factors.

Even though it does not raise any doubts that few countries in Europe present issues for their amount of public debt, this introduction meant to draw the attention upon the fact that there is not agreement on the critics moved in the last years towards the tendency of Southern Europe to rely

on excessive public expenditures. Eminent papers like that one reported by the European Commission reflects the thought of analysts, academics and researchers who do not see the primary cause of the difficulties of the last years in the lack of *"virtuous"* spirits within the *Res Publica* in the Mediterranean area.

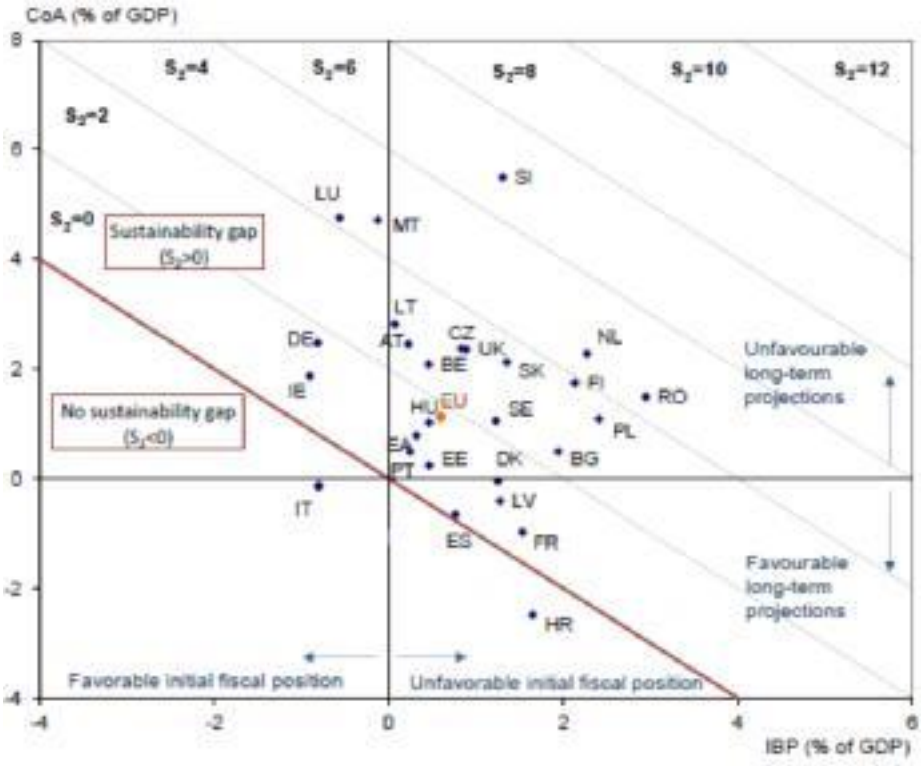

Figure 3, Sustainability of current fiscal position on the long-run, Source Fiscal Sustainability Report, 2015, European Commission

2. Research question

In the last decades, since the single currency has been introduced in Europe, the European Union has been characterized by different economic trends that have clustered the continent in what has been labelled as a core-periphery dual system. In this structure, few countries have had better economic performances that led these nation economies to sustain growth and development in the long-run. On the other hand, economic data of the last period highlight a divergence that undermines the European Union project. Many indicators of economies status show a clear situation in which periphery countries lag behind the more dynamic German and Dutch economies. These primary indicators mainly point at increasing unemployment rates, public deficits and expenditures, lack of investments and low levels of R&D. However, the chronic troubles of Italy and Spain in productivity have attracted the more attention from newspaper, policymakers and European and international institutions, since it erodes the competitiveness of the firms in these countries. As it is daily reported by international mass media, the last years have marked a turning point amid Germany and the periphery due to the difference in productivity growth. Moreover, the 2008 financial crisis has brought the situation of the overall economies at unsustainable levels. The crisis, sparked after the bankruptcy of the American investment bank *Lehman Brothers*, stressed some aspects of the European situation that could not be handled with the right financial means, as predicted by Mundell back in the 60s *(Mundell, 1961).*

Previously briefly described some evidences of the current debate concerning European economy troubles, the aim of this research is to tackle the issue of Italian poor economic performance through a historical analysis of monetary policies and international agreements. The focus will be put upon the several financial arrangements that determined the exchange rates amid European currencies. Looking back at the financial and monetary history, I will be able to individuate few different periods when a direct correlation between monetary system and economic performances defined the well-being of countries and population. The historical evidence will result useful in parallel with the experience of the single currency of nowadays. Whereas the history of Europe has mainly seen floating exchange rates, although, with numerous attempts to find a framework of fixed exchange rates, the final question that I am going to

inquiry is the role that floating exchange rates and then the Euro played in determining the outcomes of economies. It will be given particular attention at the past periods since they represent the opposite experience of the situation that took place with the introduction of a single currency in 2002.

3. Methodology

"Those who cannot remember the past are condemned to repeat it" George Santayana[1]

Having a background as a historian I did not feel familiar enough with many of the quantitative methods that have been used in several studies. Thus, for this research, I chose to conduct a qualitative analysis. I found this approach extremely useful and helpful to investigate the events that featured the Eurozone in the last decades. Nevertheless, the nature of the Euro project itself constitutes, in some extents, a further issue that should be considered. A historical perspective must, nevertheless, take in account that there are not experiences like the current monetary experiment. The previous currency unions that took place in Europe, whereas similar, differed in many senses *(Bordo and Jonung, 1999).* However, an overview over the entire post-war period can underline the main features of European economies. Therefore, I will emphasize the trends and policies that allowed the continent to sustain a balanced economic growth.
Reading through Keynes *The Economic Consequences of Mr. Churchill (1925)* the surprise derives from the features that the period, in which the great economist wrote, shares with our times. Writing between the two world wars, he assessed the choice to readopt the Gold Standard. This extremely rigid monetary system in some extents reminds the current situation in the Euro Area *(Ljungberg, 2004, p.139).* In both cases, different countries committed themselves to a fixed exchange rate system. Describing the trade imbalances, he stated: *"our problem is to reduce money wages and, through them, the cost of living, with the idea that, when the circle is complete, real wages will be as high as before. By what modus operandi does credit restriction*

[1] Vol. I, Reason in Common Sense, 1905-6

attain this result? In no other way than by deliberate intensification of unemployment […] the policy can only attain its end by intensifying unemployment without limit until the workers are ready to accept the necessary reduction of money wages under the pressure of hard facts" (Keynes, 1932, p.257). These few lines must sound very familiar to academics and researchers that nowadays study the status of Euro experiment. The broad number of papers, works, theories and books that has been published during the years before and after the monetary union is so wide that allows any researcher to develop its own perspective of the economic drivers and the political decisions that led Europe towards the single currency. Furthermore, a multitude of esteemed academics expressed their thoughts regarding a single currency in Europe since the first post-war period.

Economic theories have been developed since the 60s and 70s when the way was paved by the milestone of Mundell's Optimum Currency Area (OCA) theory. Using the OCA as starting point, this research aims to take into account all the debates that questioned if European countries constituted or not an OCA. Furthermore, as we will see in the following sections, attention will be put upon some critics that were moved to the OCA theory that made academics and economists to wonder if this theory was valid for Europe. I found that a qualitative approach could fit this intent since I benefited from the historic outlook. Several papers that moved critics to the classic approach of the OCA, have missed to forecast few of the events that instead, as Mundell theorized, were already predicted in the 60s and 70s.

A qualitative approach allowed this research to have a broader view upon many of the main variables that produced the outcomes of the monetary union. I do believe that conducting a quantitative analysis of just few aspects of the issue might be misleading. For instance, an analysis limited to only some aspects, productivity and investments, would lack other determinants. Exchange rates, public expenditures, wages, exports and imports, national current accounts, industrial production, inflation are only few on those economic parameters that should be analyzed as well, but that are often very tricky to correlate with each other since, in the eurozone case, they are influenced by so many other factors that make assessments difficult and partly incomplete. Thus, for having that wide view that I believe is more complete, I will carry on an overview over several data, reports, interviews concerning the introduction of the Euro as unique currency in Europe.

As Cooper *(2010)* suggested, I am going to take advantage of the literature review to highlight

the central issues within the topic trying to connect different aspects that result to be a central aspect of this research. Furthermore, since there already are dozens of studies and researches I opted for conducting a study that relies upon what I consider the most representative works concerning the chosen topic.

In order to discuss this wide argument, I plan to report the results of analysis, which examine different economic trends that being profoundly influenced by single European currency, show the real status of this monetary experiment. Focusing on Italy, I am going to report several data from the Bank of Italy and other data centers –ISTAT, IMF, World Bank, EUROSTAT. Throughout the research, the findings of the Italian think-tank *"Asimmetrie"*, which since the years of the 2010-11 crisis leads the debate in Italy and in Europe, will support the narrative adopted for emphasizing the most important points of this research.

A main argument that will be tackled is the turning point embodied by the period 1997-2002 when European countries adopted fixed exchange rates that constituted the final step towards the Euro. As it will be discussed, the economic landscape of Europe began to drastically change since those years. Moreover, I will do a parallel with the main economies, Italy, Germany, France, Spain and the Netherlands, which will underline the main asymmetries that undermine that stability of the EU.

4. Literature review – Theoretical framework

In this section, I am going to discuss few of the countless number of scientific works, books articles and papers that have been written about the issue of flexible exchange rates and OCA. I consider these two aspects the most important elements that should be considered in any analysis of the European Union and its currency. The ample amount of studies that have been conducted on the argument span all the aspects that concern the argument of this research. However, I decided to report only those that I considered the most representative ones. Furthermore, I will outline some aspects of the theories that will then be discussed once I will engage in the body of the argumentation.

The subject of this study captured the attention of academics since the very beginning of economic studies peaking during the period of German reparations during after the First World War when a shattered Gold Standard was attempted to put back in business by the Allies. John Maynard Keynes was at the time one of the few to recognize that not only the reparations, imposed on Germany during the peace conference in Versailles were impossible to afford for the defeated country, but also that a restoration of a financial system based on gold would have been a straitjacket to the international economy. Keynes at that time was a pioneer in the study of inflation and deflation, of monetary policies and their social impacts. He saw inflation as mean to achieve economic growth through investments, while a lack of investments would undermine economic growth leading to unemployment *(Keynes, 2016, p. 124)*. Furthermore, his worries concerning the restoration of the Pound to his former value sound similar to some of the critics that were moved to the Euro and its system of fixed exchange rates *(Keynes, 1925).* Thus, he expressed his doubts that the Gold Standard could not supply international trades with the right monetary framework taking from monetary institutions the means to adopt the proper policies in case of recession or economic expansion. After Keynes, Friedman was one of the leading economists to tackle the argument of flexile exchange rates. Being widely in favor of unrestricted commerce, he saw flexible exchange rates as essential way through which obtaining the best possible framework for trading: *"…a system of flexible or floating exchange rates is absolutely essential for the fulfilment of our basic objective: the achievement and maintenance of a free and prosperous world community engaging in unrestricted multilateral trade" (Friedman, 1953, p.157).* However, recognizing that it was likely that flexible exchange could be perceived as an extremely unstable environment, he underlined that flexibility does not mean instability. To validate this thesis, he argued that once fixed exchange rates are put in place the adjustments to economic difficulties would only more difficult to adopt in absence of floating rates *(Friedman, 1953, p.158).* In their view of the EMS, Gros and Thygesen *(1998)* seem to agree with him. In their ample description of the European monetary integration, they face many of the problems that European countries met towards a more integrated common market. Nevertheless, their assessment of the EMS during the 80s reflects Friedman´s theories. However, a first reading upon their work can be misleading. Indeed, they widely argue in favor of fixed exchange rates claiming that they would not bring unemployment and those asymmetric shocks that are feared by different academics. Their book fiercely contrasts the traditional idea of Mundell's Optimum

Currency Area theory. They questioned two of the main points that are proposed in the OCA theory. Firstly, they disagree with the central role that flexible exchange rates have in Mundell's view. Secondly, they do not share the typical description of the lower European labor mobility when compared to the United States. Their main point highlights how European countries are featured by very low labor mobility at an interregional level within countries. Thus, they assess the low international labor mobility as a distinctive characteristic of Europe (*Gros and Thygesen, 1998).* Under a trade perspective, de Grauwe *(1987)* seemed to support their view. He found that exchange-rate variability had a limited impact on trades during the 1980s.

Nevertheless, there is a wide literature which defends what was proposed by Mundell and his OCA theory.

As starting point let me briefly report the discussion carried on by Mundell and its main implications. His analysis focused on two hypothetic countries A and B in a status of full employment and equilibrium in their balance-of-payments. When a shift of demand happens from B to A it causes rising unemployment in B and inflation pressures on A. However, if A does not allow inflation to take place, adjustments must be implemented in B through a decrease in output and employment: *"The policy of surplus countries in restraining prices therefore imparts a recessive tendency to the world economy on fixed exchange rates" (Mundell, 1961).* For recovering from this disequilibrium Mundell proposed three ways. Wage flexibility, labor mobility or fiscal policies. These variables are confirmed by the study conducted by Bayoumi and Eichengreen *(1998),* who tried to empirically demonstrate the possible interventions just mentioned. Following the way paved by these two authors, Alesina and Barro *(2002)* studied changes in prices and output and how a country decision to join a currency union should depend upon these two variables.

A further work from Bayoumi and Eichengreen *(1993)* sparked a new debate within OCA and monetary unions. Indeed, they found as more suitable for adopting a common currency those countries that nowadays are known as the core of the Eurozone. Germany, the Netherlands, Austria, Belgium and France appeared, in their study, to have similar economic features that made more likely to pursue a monetary union between these countries. This inspired a vivid discussion about what was at that time labelled as a "two-speed-approach", which meant the formation of a first block of countries that would eventually have been followed by the rest of the continent once it would have fixed some parameters (Maastricht criteria). James Tobin

(2001) and Dominik Salvatore *(1997)* had similar worries. They both argued that lack of labor mobility and inadequate fiscal reallocation would have led the union to the collapse if hit by an external shock.

Most recently, an interesting paper has been proposed by Johansson and Ljungberg *(2013).* They questioned the policy adopted by the ECB and by the EMU of "one-size-fits-all". In their paper, they criticize the assumption that a central bank, such the ECB, could not adopt different policies for different economies. Indeed, they underlined how at the same time the ECB allowed *"bubble economies"* to grow while others were put under deflationary pressures. Secondly, they find how periphery countries saw their competitiveness gravely undermined by the new currency. They particularly emphasized this latter aspect. Indeed, they show how, since the introduction of the Euro, only few core countries benefited in terms of productivity. Furthermore, they do not miss to notice that Germany could take the lead in the euro-12 only through policies aimed to contract wages *(Johansson and Ljungberg, 2013)*. Their work seems to oppose the view that some expressed at the beginning of the Euro experience[2] *(Issing, 2005).* The two authors could benefit from a complete historic experience, since they were able to analyze the outcomes of the Euro and its effects on European economies after the 2008 and 2010-11 crises. Their aim was to describe how the single currency stressed the asymmetries within the Eurozone, which perfectly fits the fears expressed in Mundell's model *(Johansson and Ljungberg, 2013)*. Bibow's *(2012)* moved a similar critique. In his paper, he approaches the OCA theory comparing it with the current situation and with the role of Germany in spreading the imbalances amid countries. He particularly emphasized the unwillingness of Germany to commit herself to a common inflation rate, which he defined as *"golden rule of a monetary union".* Furthermore, he agrees with Johansson and Ljungberg view of the wage restriction policies of the end of the 1990s as the real drivers of German higher competitiveness *(Bibow, 2012).* This point, outlined by Bibow, embodied the country A in Mundell's theory. Indeed, Germany, refusing to inflate its economy, leaves the burden of adjustments upon the periphery countries, or as international mass media sadly marked them, the PIIGS (Portugal, Italy, Ireland, Greece, Spain).

These recent works have been extremely severe in their assessment of German policies because academics recognize the correlation between inflation and employment since the 1960s. The

[2] Speech by Otmar Issing, Member of the Executive Board of the ECB, International Research Forum, Frankfurt am Main, 20 May 2005

most influential work is the research of Phelps *(1967)* who theorized the well-known Phillips curve, which positively associates inflation and employment. Higher inflation rates cause decreases in unemployment. A further support to the imbalances thesis is the three-countries model proposed by di Mauro and Pappadà *(2014),* who confirm that Italy and Spain need a drastic exchange rate depreciation in order to pursue external rebalancing.

A final topic, faced by Mundell, is imbalances in current accounts. David Hume *(1752)* price–specie flow mechanism was the first to argue against countries running mercantilist trade surpluses. During the post - war period debate, alongside Mundell's proposal, Meade *(1957)* had at the core of his analysis balance-of-payments equilibriums seeing in the lack of labor mobility a possible asymmetry. Sachs and Sala-i-Martin studied this aspect of monetary unions as well *(1991)*. In their paper, they agreed with the view of international imbalances. However, they mainly focused on the point of fiscal policies, whereas they concluded that without proper means of fiscal redistribution the future of the Euro might have already been doomed before even taking place *(Sachs and Sala-i-Martin, 1991)*. The current account issue is central in the view of Bibow as well *(Bibow, 2012)*.

Current account and flexible exchange rates were the two mechanisms that could realign imbalances amid Europe. When a country runs a surplus, it means that this country's products are widely required in foreigner markets. Thus, in order to purchase these goods, the currency appreciates whereas it is strongly required by international markets. Albeit with some backlashes, the Dutch experience of the 1970s, when the sudden exports of gas made skyrocketing the Dutch guilder, illustrate the mechanism. An overvalued Guilder undermined the nation broader economy *(Eichengreen, 2008, p. 293)*. The mechanism is valid on the other way around. In this way, deficit economies take advantage of increases in value of foreign currencies to foster competitiveness through more advantageous positions in exchange markets. Needless to say, the introduction of the Euro has removed this automatic mechanism that always allowed realignments in current accounts.

5. An historic no-sense

The recent crisis has taken place in a unique situation. The European countries, indeed, have embarked themselves in an economic experiment that seems to contrast the trend that the rest of the world is experiencing in our times. Whereas the vast majority of economies followed a tendency towards adopting floating or less fixed exchange rates, the European countries preferred the opposite direction *(Calvo, 2000).* Alesina studied a similar topic. He finds that since the end of the Second World War the number of independent states increased from 74 in 1946 to 191. Furthermore, he concluded that smaller economies tend to perform better the big ones, with the USA the only exception (Norway, the Netherlands, Sweden, Singapore) *(Ljungberg, 2004, p.39).* Thus, someone might pose the question of why European countries want to obtain a political and economic union. Trying to unify so many countries, with their different cultures, languages, economies and social fabrics, is a task that challenges politicians and the historical differences that feature Europe since ever. These differences have been often pointed as a unique element in the international environment that allowed Europe to overcome the other parts of the world towards industrialization and economic success. Indeed, during the decisive 17^{th}-18^{th} centuries, the Old Continent was clustered in a countless number of national and city states, which competitive spirit drove Europeans to develop revolutionary military technologies and to improve manufactures that, through a synergy of different elements, evolved in the Industrial Revolution. Even though some economic historians see in the high degree of competition the determinant for the European success, others underline the cultural and geographical elements as real drivers of the development that took place from the mid-18^{th} century (*Findlay et al., 2007).* However, describing the debate concerning the causes of the drastic change that has gradually shaped the continent is behind the means of this paper. Nevertheless, I found extremely interesting reporting this view since under this prespective the current experiment seems moving towards an opposite direction in respect of the history of European countries and their success. A political union would mean to remove the intra-national competition. Moreover, as I will describe, the current situation gives artificial advantages to few countries that, exploiting a dysfunctional monetary system, have outperformed the rest of the European Union in terms of economic fortune.

6. Brief historical background 1950s-1970s

The European Union is the most important political and economic experiment of nowadays. Such revolutionary political project has its roots in a generally shared shock embodied in two world wars, fought in less than fifty years. The degree of destruction and loss of human capital have led intellectuals, politicians and economic elites to wonder how to pursue wealth through a peaceful future. Furthermore, a looming communist invasion, threatened by the Warsaw Pact countries, brought the European countries even closer. Being able to have a broader view on the evolution of the European dream, Martin Feldstein admits that the basis of the unification process is mainly to be searched in the political sphere instead than in the economic ones. He defines the Euro as part of the creation of what he labels as *"sense of European community" (Feldstein, 2012).* For achieving this goal, the population of the first six founder countries, or at least their ruling classes, committed themselves to abandon any project of continental supremacy aiming towards cooperation and shared decisions. From the ECSC *(European Coal and Steel Community)* of 1951, numerous treaties progressively decreased tariffs allowing free movement of goods, capitals and people. On the long-run the aim was a unique free European market. However, since the first years of this experiment, a clear dualism emerged within the decision-making process that regulated the newborn European Union. Taking place in the immediate afterwards of the most deadly and catastrophic war recorded in human history, many authors recognize that this project can be reconducted to the American will to tie together France and Germany to prevent these two countries to bring the world into another war *(Eichengreen, 1998, p.150).* The international economy could not afford a further conflict, whereas in less than seventy years these two nations fought three times (Franco-Prussian War, 1870-71, First World War, 1914-18, Second World War, 1939-45) destroying wide parts of European infrastructures, economies and population. Moreover, as already said, the Soviet nuclear threat was the determinant stimulus for finding a peaceful solution to the historical issues that had divided the two countries until that time.

Thus, the unification project of the continent was carried on by this intention. It seems perfectly natural that German and French policy-makers took immediately a central role in the political

and economic institutions and being the two most populated and biggest economies gave to these countries the leading role in Europe. The institutional framework that was born during the 50s and 60s deeply depended upon the French desire to regain independence in foreign policy from the United States, while Germany saw in the European Community (EC) the channel through which moving forward leaving behind an, for using a euphemism, "uncomfortable" past. Alongside German interests, the Benelux found itself closely integrated with the Germany economy. Therefore, already in these first years of the European Union, these countries began to compose the core of European economy forming a dualism amid the core and the periphery. The latter put together those countries that since the very beginning had worse economic trends and that mainly relied either on international aids, Marshall Plan or upon extremely high public expenditures. Therefore, they contrasted the first free trade agreements adopting independent economic policies, which rose tariffs to protect domestic markets *(Eichengreen, 2008)*.

A country that perfectly fits these traits is Italy. Even though it was invaded by both the Nazis and the Allies, the core of the industrial fabric, located in the "Triangle" between Milan, Turin and Genoa, slightly suffered tangible damages from the fights that took mainly place in the Southern part. Once the war ended, Italy was geographically placed at the frontline of the Cold War. Moreover, the widespread support of the communist ideologies pervaded vast parts of the population allowing the Party to achieve stunning results during the national elections of the 50s and 60s. Thus, the financial aids of the Marshall Plan were primarily aimed to contain the Soviet influence into the political system and to build enough wealth that could prevent a revolution *(Sapelli, 2012, p.64)*. Through these means, tariffs and free trades limitation were put in place, despite the initial liberal spirit that characterized the first steps of the economic unification of the continent *(Sapelli. 2012, p.13)*.

As economies were, slowly but surely, getting closer and merging into each other, their financial systems tried to follow as well. Few monetary arrangements were designed that imitated the financial institutions that the USA created at the end of the war, the IMF and the WB (*Eichengreen, 1998, p.104).* The European Payments Union (EPU) started to operate in 1950 and it was only the first of a series of several settlements. There is no wonder in discovering that Germany and Austria immediately benefited from this arrangement. Eichengreen *(2008, p.82)* shows how exports of these two countries skyrocketed in 1951. This is primarily due to the main goal of the EPU. Since the Marshall Plan aimed to restore trades and current-account

convertibility, states running deficit balance of payments were allowed to access credits provided by American aids. In this way, core economies that always relied upon intra-European trades could grow through exports that were directed towards Denmark, the Netherlands and Italy, which all deeply depended upon German exports *(Eichengreen, 2008, p.81).* These measures adopted by the USA constituted the proper framework that allowed Europe to recover from the destruction of the Second World War achieving stunning economic performances in those years that are now remembered as Golden Age. Trades and investments were the determinants of economic growth that has not experiences to compare with. An extremely high range of new technologies was commercialized, productivity rose in most of the countries, outperforming the US. This was achieved also through *social contracts* stipulated amid industries and workers' unions. Employees limited their requests in order to ease investments and full employment policies. This agreement was made possible by the institutionalization of an extensive and inclusive welfare state that mitigated the lack of any abrupt wage increase during the first post-war period *(Rhode and Toniolo, 2006).*

5.1 *The historical German attitude*

"The welfare of member countries is always affected by supply and demand shocks emanating from the leading country[3]*"*

Heinz-Peter Spahn

I felt the need to shortly describe the role of Germany in the post-war economic life of Europe because it has always constituted the determinant in most of the decisions that shaped the continent since the unification of the multitude city-states at the end of the 19th century. The policies, implemented within its borders, have affected its surrounding countries at a level that many struggles to recognize. The size of the German economy is so decisive that its neighbor European states depend upon its well-being. However, despite the doubtless central role that Germany plays in Europe, its elites have failed, or have refused, to assume the lead in the

[3] Spahn, 2001, p. 167

European Union. The lack of any substantial coordinated policy has its focus upon the aversion to inflation economic policies.

Since the end of the Second World War, Germany was featured by the Ordoliberismus, an economic school that, contrary to what is professed by Keynes, sees in the markets the best way to achieve full employment and a welfare state. This, translated in more practical and direct terms, means that German economy and workers had to commit to an export-led economic growth. In order to achieve this goal, Germany economic fabric, composed of all the characters that have a role in the outcomes of a country economy, from worker unions, to central bank, through employers and the federal state, chose, or were forced, to pursue a sterilization of salary increases for bringing advantages to German companies *(Cesaratto and Stirati, 2010).* The decision to adopt a conservative salary policy forced the rest of the continent to implement currency devaluations in order to face the German competitiveness.

Cesaratto *(2010)* well portraits the German economic behavior since the end of the war:

> *"…taking advantage of fixed exchange rates by pursuing a domestic inflation rate lower than competitors to foster exports; (ii) relying on other countries stimuli to aggregate demand and taking advantage of their ensuing inflationary bias; (iii) compensating with conservative domestic fiscal (and monetary) policy any possible labor market overheating, maintaining the external competitive hedge; (iv) replying to foreign criticism with moralistic tones by blaming their indiscipline and proposing itself as a model"*[4].

The issue of the Euro is understood in the quote here reported. Whereas Europe has always had a monetary system that, even though were put in place for bringing stability within exchange rates, had countless "realignments", the Euro has brought an exceptionally rigid environment that does not allow single countries to adjust their economies or to proper react to external shocks. The policies left to the Eurozone countries are very limited. The widely adopted one, after the 2008 financial crisis, has been a spread deflation. Furthermore, the ECB is a *super partes* institution that does not have the required means to tackle national problems, but it only can battle

[4] Cesaratto and Stirati, 2010

economic shocks at an overall level. Thus, once the crisis hit periphery countries were doomed to follow a policy of salary restriction.

"We are gaining better position in competitiveness because of the structural reforms. We are actually destroying domestic demand through fiscal consolidation. Hence, there has to be a consolidation of the demand throughout Europe"[5].

This sentence perfectly illustrates the situation that occurred in the afterwards of the 2008 and 2010-11 crisis. A series of structural reforms mainly focused on labor markets, welfare states and public expenditures, were the recipe proposed by the European Union. In spite of this, Germany did not want to assume the role of leading economy in Europe. Indeed, the expected inflation rates and rise in domestic expenditures that were required, for recovering European economies from the crisis, did not occur.

[5] Mario Monti, former Italian Prime minister 2011-13, CNN interview May, 2012,

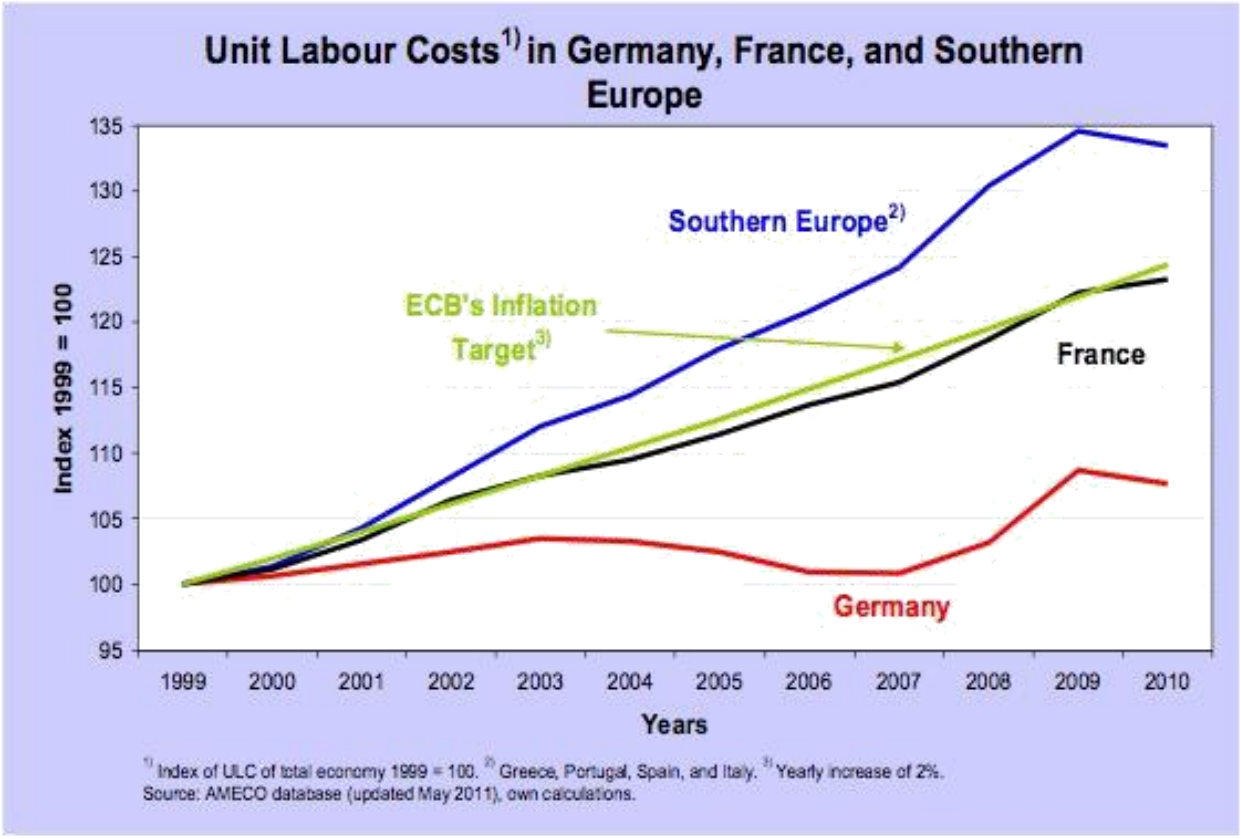

Figure 4. unit labor costs in Germany, France and Southern Europe from 1999 to 2010, Source AMECO

6. Discussion of the issue

I embarked myself in a description of the main events of the first post-war period since I believe that having a proper historic background is a fundamental part of our understanding of the shapes that European economies and societies are assuming. Even though, at a first reading, the previous part might seem to lack useful information, the themes slightly presented will be now deeper discussed. In the following argumentation, I am going to discuss the evolution of the European Union, the Euro and its main protagonists.

The 1970s and the oil shocks

The monetary integration of European economies has its turning point during the 70s. The international financial system, at that time, was still regulated by the Bretton Woods arrangement, agreed by the leading industrialized countries in 1944. It had at the center of its functioning framework the American dollar which embodied the fundamental role of the US economy in the international economic scheme. The US currency was designed to function as an element, alongside gold, to refer for adopting fixed exchange rates. However, the high military expenditure required by the American intervention in Indochina and rumors concerning the will of France and England to convert their dollar reserves into gold led Nixon to cease the convertibility of dollars into gold on August 13, 1971. The system, which ruled international capital movements since 1958, came to an end leaving many open doors to further uncertain times (*Eichengreen, 1998).*

The decade following the break-up of Bretton Woods was featured by what, already at the time, was defined as *"Snake in the Tunnel",* whereas European currencies were free to float within a range of 2,5± on the dollar. However, the life of this new monetary system that characterized the continent from 1972 to 1978 was inconstant in the sense that various times countries withdrew from this narrow band. Yet, the Snake failed for several reasons. An overall assessment should point at the synergy between global energy shocks, which made *"unpropitious for efforts to peg exchange rates" (Eichengreen, 1998, p. 154),* and Germany decision to avoid inflation.

For a deeper view, a first approach reveals the numbers concerning inflation rates in the key countries considered for this research. France, Italy and Spain witnessed high inflation rates, which primarily derived from the international oil crises of the 1970s. The price stability chose by German authorities allowed the other currencies to have a broader fluctuation range *(Eichengreen, 1998, p.153).*

	74-80	***81-85***	***86-90***	***91-95***	***96-00***	***01-05***	***06-10***	***11-15***
France	*11,13*	*9,6*	*3,08*	*2,23*	*1,2*	*1,9*	*1,5*	*1,09*
Germany				*3,5*	*1,26*	*1,5*	*1,5*	*1,3*
Italy	*16,9*	*13,7*	*5,6*	*5,03*	*2,4*	*2,4*	*1,9*	*1,4*
Netherlands	*7,1*	*4,1*	*0,75*	*2,7*	*2,1*	*2,4*	*1,5*	*1,7*
Spain	*17,9*	*12,2*	*6,4*	*5,16*	*2,6*	*3,2*	*2,3*	*1,2*

Table 4. Percentage average of inflation in consumer prices, source OECD.stat

The oil crises that occurred in the 1973 and 1979 represented a point of no return in the history of European economies. Firstly, because of the stagflation, which defines an unexpected weak growth despite high inflation. Secondly, low-cost source of energies allowed policies of mainly full employment for two decades. However, as oil prices skyrocketed, European countries found themselves in an unprecedented situation. Unemployment rose in all developed countries as higher expenditures for input factors compressed companies' profitability. Furthermore, the cost of labor increased due to higher inflation *(Eichengreen, 2008, p.263).*

In a situation of flexible exchange rate countries opted for either devaluating their currencies or taking advantage of the German March revaluation *(Gros and Thygesen, 1998).* Even though the 1970s-monetary experience might look deeply unstable, the data about growth and trades still showed positive trends *(Sapelli, 2012, Gros and Thygesen, 1998).* Table 3 in the appendix supports this statement. Focusing on Italy, even though the inflation reached its highest point in 1980, the country performed an astonishing 25% of household saving rate during the very same year *(Bagnai, 2012)* and, despite all, a relatively low unemployment rate *(Sapelli, 2012, p.71).* Despite the fact that the international situation did not appear to recover in the short-run to these shocks, the industrial fabric could rely on significant monetary policies that were implemented by the Bank of Italy. In those years a consistent amount of industries took place in the north-east. The widely studied and admired Italian industrial districts assert themselves during this troubled period *(Sapelli, 2012, p.71).*

Regarding the stagflation, which was the distinctive characteristic of that decade, a study proposed that a sudden increase in import expenditures might have caused negative correlation between inflation and employment. Unemployment was a problem that all Western countries faced and that continued to be a trait of Europe also in the following years *(Eichengreen, 2008, p.263).*

The 1980s and the EMS

"The system broke down because other countries were unwilling to go along with the policies of the center country"

Michael Bordo[6]

Thus, European economies, after a first period of struggles, could start to grow again, although during the first years of the 1980s *(table 3, Appendix)* the way back to development found many obstacles in the lack of international cooperation, productivity slowdown and current account imbalances *(James, 1996, p.409, Eichengreen, 2008, p.290).* Disinflation policies featured the first half of the 80s, which brought back inflation rates to lower levels. The more conservative monetary policies had the effect to curb growth in Europe. In this economic framework, Germany emerged as a center of stability. Its policymakers strictly followed the indications that came from the IMF: *"increased attention might be given in this regard to the use of incomes policy – as a supplement to sound fiscal and monetary policies, but not as a substitute for them"*[7]. On the other side, Italy reacted these years of turmoil through intervention in exchange markets. As James *(1996, p.285)* admits, the process *"was highly successful quite quickly".* As Bagnai *(2012)* and Eichengreen *(1998, p.161)* report, Italy joined the EMS in 1979, but already a few years later a European currency realignment took place. Figure 1 is extremely meaningful in regard of the deep correlation between Italian economy and its devaluation policies. As can be seen, Italian productivity looks interconnected with the feature of its currency and the monetary framework, the European Monetary System (EMS), which replaced the Snake in 1978. Germany and France were the two main actors in the decision making. They set an Exchange Rate Mechanism (ERM) that had a fluctuating range of 2,25± (Italy obtained a more flexible rate of 6% due to its high inflation rates), towards the Deutsche Mark that assumed a central role into the new system, very similar to that one that the dollar played in the Bretton Woods system (*Eichengreen, 1998, p. 160)*. However, even though the EMS was supposed to bring stable exchange rates, it experienced a more troubled life.

[6] Michael Bordo, 1993, p. 181

[7] International Monetary Fund, Annual Report, 1976, p.18

	Belgian Franc	*Danish Krone*	*French Franc*	*Dutch Guilder*	*Irish Pound*	*Italian Lira*
Mark "revaluation" (1979-90)	*31.2*	*35.2*	*45.2*	*4*	*41.4*	*63.5*

Table 1. Overall revaluation of Deutsche Mark against other European currencies, data expressed in percentage, from Gros and Thygesen, 1998, p. 69

However, the stabilization policies implemented by the Bundesbank led the EMS to collapse. German instability embodied a series of rigorous conservative actions that were meant to contain price increases: *"...key currency should be characterized by a stable price level to provide a nominal anchor for the monetary system as a whole: the key currency country should never be in a position to need to employ restrictive interest policies in order to achieve price stability at home" (Spahn, 2001, p.160)*. The result of this attitude towards inflation developed in a progressive increase of current account surpluses from 1983 *(Spahn, 2001, p.150).* Further evidences of moderate salaries policies come from Franzese and Hall who confirm what is displayed in figure 1 in the appendix: "*The metalworking sector, which produces the lead bargain in most years, has a high export concentration. In itself, this induces lower settlements because wage bargainers in export sectors are especially concerned with maintaining unit labor costs at internationally competitive levels. Actors in such sectors are also especially sensitive to signals from the central bank, however, because the restrictive monetary policies that the bank wields not only depress the level of economic activity but also tend to appreciate the exchange rate, thereby threatening export sectors especially severely by rendering their products more expensive in world markets*[8]*."*

The rest of Europe, however, could not, as France and Italy, or did not follow the German policies. France and Italy had to sustain high public expenditure. To contain the communist parties, employment policies were fostered through the public sectors of the two states (in 1984 the Italian communist party was the first choice by the voters, by a narrow margin though). Thus, EMS countries reacted to the conservative German policies with higher inflation rates and

[8] Franzese and Hall, 2000, p. 182-3

intervention in exchange markets.

The situation worsened after 1987 when currency devaluations stopped to be a tool that central banks could use in case of needs. Therefore, the second half of the 1980s was labelled "hard-EMS" when in addition to the removal of currency depreciation, controls on short-term financial movements were abolished causing a wave of capital inflows in countries with higher interest rates and inflation – Spain, the UK and Italy.

For the latter joining the EMS was particularly harmful. Eichengreen *(1998, p.173)* highlights the surge in unit labor costs, which partly justifies the productivity growth slowdown shown in figure 1. A further element tends to support this statement. As after 1987 EMS economies refused to implement devaluating measures all the burden of adjustment fell upon labor salaries policies. Whereas an economy cannot devaluate its currency, companies see in wage restriction the only mean to preserve competitiveness in international market and profitability. Moreover, as Germany did not allow any change in its wage policies and inflation rates, the Italian, and Spanish, competitiveness deeply suffered by the inability of using devaluation policies:

"[…]leadership became a burden for member states when the key country exported restrictive policies, which in the end could no longer be tolerated" (Spahn, 2001, p.167).

The 1990s and the route to the Euro

> *"The euro primarily is no economic project. […] the euro is a strategic project. It is part of the building up of Europe in stages"*[9].
>
> *Helmut Schimdt*

The way to a definitive pegged currencies system seemed to reach an end during the first years of the 1990s. If Germany´s wage policies might be a reason for the end of the EMS, intense capital movements may be a second one *(Eichengreen, 1998, p. 183)*. Trying to keep attached currencies within this framework was extremely more challenging than the previous decades. Moreover, there is a consistent literature that considers the Maastricht Treaty as *"model of self-fulfilling crises" (Eichengreen, 1998, p.177).* Thus, as many academics and analysts expected few European currencies came under speculative attacks. The British Pound and the Italian Lira

[9] Quoted from Issing, 1997

were the most hit by the markets, which forced the governments to withdraw from the EMS. In the following year, the Italian Lira was free to fluctuate experiencing a depreciation of roughly 20% *(Bagnai, 2012)*. Once again figure 1 shows a pattern that reacts to the monetary policy of Italy. As can be noticed, a first slowdown corresponds to the period of narrower exchange rate flexibility. Yet, as Italy left the EMS, the trend began to rise once more. The balance of payments had a stable tendency, even though with slight surpluses in Italy, whereas Germany suffered from years of deficit, mainly due to the burden of the reunification *(Spahn, 2001, p.155).* This evidence underpins the claim that these results are mainly correlated with the characteristics of monetary arrangements. Table 5 proposes a further proof of pegged currency during the hard-EMS in 1990 and its effect on European economies. Germany, back at the time, ran a consistent surplus, while the rest of Europe struggled to reach a neutral balance of payments. This fiercely contrasts the following years of floating currencies, when a more equal balance of payments featured Europe. Nevertheless, as I am going to discuss later, the overall situation took a definitive way towards divergence at the turn of the millennium.

Thus, even though European economies differed in multiple indicators, a few years later Europe embarked itself in the last steps towards a single currency *(Spahn, 2001, p.171).* The milestone is represented by the Maastricht Treaty signed in 1992. As always, Germany had a central role in the decision process. It sets limits and targets for inflation rates, public expenditures and fiscal policies. The infamous criteria of an annual expenditure that does not have to exceed 3% of the GDP, public debts not more than 60% of national GDPs and an inflation rate for the entire Eurozone, which should not be above the 1,5% of the arithmetic average of the three lowest inflation rates. These parameters were agreed to pursue a convergence process that, despite all the attempts, did not, or could not, take place *(Spahn, 2001, p. 171).*

Once more, figure 1 line follows the decisions took by European institutions. To pave the way for the single currency, the countries of the future EA agreed to reintroduce a pegged system, which Italy decided to join in 1996. Like the previous times, pegging the Lira to the Deutsche Mark corresponded with a productivity growth slowdown of the country. Figure 4 in the appendix has a deeper and further upon some imbalances that started to worsen since the fixed exchange rate system was embraced. Current account (im)balances emphasize the doubtless shift of competitiveness from the periphery, Italy above all, to Germany. The surplus increase looks astonishing indeed. Austria and the Netherlands registered the same upward tendency, while the

rest of the continent began to suffer important negative results.
Nevertheless, the Euro project kept going. It has been pointed out many times that Europe was clustered in too many different economies, cultures and languages. On the edge to the introduction of the Euro, an obvious dichotomy already developed from the end of the war in 1945. An export-led core economy, composed by Germany, Austria and the Netherlands, was opposed by a periphery, Italy, Spain and Portugal, with France in a middle position as it shared features with both groups *(Koziara, 2013)*. Consequently, further issues generated during these years that led Europe to the monetary union. As just said core countries shared similar economic features and interests. Thus, it should not surprise if many worried about the fact that these economies tried to influence the measures and the shapes that the European Union and the new currency were going to assume.
Moreover, as described in the previous sections, Europe countries have constantly experienced interest rates that widely varied amid economies, which constituted, probably, the main difference. The troubles that loomed in front of Europe are very well outlined by Feldestein: *"Single currencies require all the countries in the monetary union to have the same monetary policy and the same basic interest rate […] Economists explained that the euro would therefore lead to greater fluctuations in output and employment, a much slower adjustment to declines in aggregate demand, and persistent trade imbalances between Europe and the rest of the world. Indeed, all these negative outcomes have occurred in recent years" (Feldestein, 2012)*. He describes it as a way that could be implemented to mitigate the effects of aggregate decreases recognizing its usefulness to react in case of shocks *(Feldestein, 2012).*

The euro

"For political reasons the dominance of one currency cannot be justified in the long term[10]" Toni Pierenkamper

The single currency began to circulate in 2002. Policymakers and European institutions welcomed it with enthusiastic statements: *"with the euro we will work a day less earning as if we*

[10] 1999, p.45

will work one day more[11] *".* A new spirit of integration and hope seemed to pervade the continent.

Nevertheless, the route to the Euro did not find total agreement. As stressed throughout the previous chapters, academics tried to express their concern about the project. In occasion of the Swedish referendum, an excellent work was published, which shortly summarized the main points debated against the single currency *(Ljungberg, 2004)*. In their book, the authors meant to address the main issues that have been discussed in the previous decades aiming to explain to the Swedish society the reasons to vote *"No"*. The main points of the book concerned the features that European countries still missed for forming an OCA. Lack of labor mobility and current account *(im)*balances were strongly marked as the main aspects that could have been led to stress economic tensions amid the EA.

Indeed, as widely predicted by the authors of the book, Europe, very soon, began to face severe balance of payments issues *(figure 3, table 4 in the Appendix)*. Bagnai *(2012)* perfectly describes what went wrong in the monetary unification: *"in the last eleven years we have been importing capitals (namely, borrowing from foreigner countries) for financing our imports. As many experts did not miss to notice, the fact that Southern Countries accumulated an excessive amount of loans from abroad was the actual reason of the European crisis" (Bagnai, 2012, p.39).* The Euro has indeed allowed a misleading perception to take place. Lending private institutions were even more involved in their capital transfers since the fear of a possible currency devaluation was removed: *"creditors have widely lent because they knew that the single currency, with its exchange rate 1:1 (one German Euro was equal to one Spanish Euro), abolished the risk of exchange rate* ***(and the risk of a devaluation pursued by the borrowing country)*** *" (Bagnai, 2012, p.54, underlined is mine)*. As result, massive amount of investments and loans began to steadily move from the center to the periphery of the EA. Yet, despite of what is commonly believed and claimed by main-stream analysts and mass media, the private sectors of Southern Europe were the main responsible of this disruptive trend. Families, companies and banks started to heavily borrow from financial institutions of Central Europe (mainly Germany). Shortly, it might be said, in a very schematic analysis, that the huge profits and revenues, that German companies performed in the years right after the monetary unification, were invested into the EA periphery, lured by higher interest rates that a few countries had at that time. Through this

[11] Romano Prodi, Italian prime minister 1996-98, 2006-08, from a conference 1998

process, countries such as Spain and Ireland, which, even though they both were on their ways to reduce their public deficits, witnessed capital inflows that deeply undermined the stability of the private sector *(Bagnai, 2012, p.130).* Thus, there are no wonders that once the crisis sparked in 2008, these two counties were hit the most by the financial turmoil as lenders, once they faced the havoc caused by the subprime crisis, demanded the repayment of their lent capitals *(Ljungberg, 2013).*

Nevertheless, in his book, Bagnai disagrees with those who only blame borrowing countries. On the contrary, he supports the view that firstly points at the Euro, which permitted the PIIGS to benefit of way lower interest rates than before causing, as we will see, relatively high inflation rates. Additionally, he also states that lender countries should carry part of the burden as well: *"actually private banks* ***(German and French ones)*** *lent too much and too badly" (Bagnai, 2012, p.105).* There are irresponsible borrowers only if there are irresponsible lenders: *"when they adopted the Euro, Portugal and Greece had a foreign debt already above 5% of national GDPs, which, very soon, reached mostly 15%. These values are incompatible with the financial stability of economies. […] Nobody, at the time, noticed it, although controls on foreign debts were clearly required by the Maastricht Treaty". (Bagnai, 2012, p.77)*

Moreover, meanwhile capital movements undermined the PIIGS, price tendencies had a crucial impact as well. As previously said, even though the ECB has fixed an overall inflation rate of 2%, the actual situation of the economy has always been different. Inflation rates have differed for the entire post-war period and the introduction of the single currency only narrowed down this difference, failing, though, to solve it *(Bagnai, 2012, p.116-117).*

Fostered by capital inflows, inflation rates, and consequently prices, steadily rose in periphery economies. These, normally, would have been kept under control by increased interest rates, which, however, were straightly ruled by the ECB that limited its actions to a mere *"one size fits all"* policy. Hence, the price asymmetry resulted being a meaningful factor, which outlined at least two important features of the Euro and its institutions.

Firstly, as emphasized by Ljungberg *(2013),* the ECB found itself without the required means, and perhaps without the political will, to contrast this asymmetry. Being unable to face these issues revealed the first mistake of adopting a centralized entity as unique ruler of monetary policies for such dissimilar economies. Furthermore, the absence of substantial political cooperation, and an overall disagreement over fundamental economic decisions *(Bibow, 2012),*

stressed the problem even further. Therefore, the second issue arises. Price asymmetries caused a divergence within the EA, as the competitivity of goods produced in the periphery saw an abrupt decline determined by higher inflation rates and rising prices. Thus, as result, Germany that invariably had lower inflation rates, experienced more contained price growth, which meant that *"Germany has indeed devaluated in actual terms if compared to all her European partners" (Bagnai, 2012, p.77-78).*

The outcomes for Italy are displayed in table 6, 7 and 8 in the Appendix. A marked drop in exports and economic and salaries growth slowdowns appear to be the obvious consequence to the new monetary framework. Furthermore, graph 2 (Appendix) should not surprise the reader. Making her goods more affordable through conservative wage policies, German companies took the lead in industrial production, as can be seen, a few years later the introduction of the single currency.

Conclusion

"Like Argentina, Italy faces a growing competitiveness loss given an increasingly overvalued currency and the risk of falling exports and growing current account deficit. The growth slowdown will make the public deficit and debt worse and potentially unsustainable over time. And if a devaluation cannot be used to reduce real wages, the real exchange rate overvaluation will be undone via a slow and painful process of wage and price deflation"[12]. Speaking at Davos in 2006, Roubini nailed the issue that Italy, and the entire EA, was about to face. I decided to conclude this overview over the last five decades of European integration process with his speech as it pictures the issue that I meant to address in both ways that I was most interested in pointing out.

Firstly, once more, it underlines that the backlashes derived from the introduction of a single currency in Europe were known and widely studied since the beginning of the European monetary new course. Economists expected and predicted part of the difficulties that arose after the abolition of national currencies. Reading through the literature presented in this work, I found extremely intriguing that were mainly American academics to warn European leaders about the obstacles that they would have confronted if the Euro project would have remained the same as it

[12] http://www.businessinsider.com/roubini-2006-post-talking-about-italian-debt-crisis-2011-11?IR=T

was planned in the first treaties (Maastricht and its straitjacket above all). The reason of this lack of qualified advises within European institutions during remains a mystery at the writer of this brief work. However, it appears likely that whereas statesmen acquired wise counsels they, instead, preferred to follow the paved path. As I tried to show in the section that described the succession of agreements and deals of the first post-war period, the EU then, and now, was put in place for tying together German and French interests, thus it should not amaze that the current framework of European institutions reflects the will of these two countries.

Secondly, these words were pronounced in one of the most important events for economic and financial advisors, who, alongside policymakers and bureaucrats, attend this kind of conferences. Some of them hold high positions within institutions, which rule over the lives of millions of Europeans. The fact the such high officials were warned in a countless number of occasions might suggest, one more time, that the project to unite the continent with a single currency was primarily driven by political intents. Indeed, the IMF itself recognizes current account asymmetries as one of the principal disruptive trends in international economics. Its article 7 states that once a country runs a structural (constant) surplus appropriate measures should be implemented to limit trades with such country (for diminishing its surpluses). Moreover, it seems as the European Commission shares the view of the IMF. In 2012 it published a research, which labelled current account surpluses as economic asymmetries and asserting that they should be balanced through agreed policies (Bagnai, 2012, p.41). Thus, someone might wonder why few countries can approach the international economic environment in a such dysfunctional way. It gives the impression that it follows the same logic above expressed.

To delineate the real shape of the Euro, throughout this work, I tried to remark that some of the facts that mass media and main-stream analysts propose do not find actual evidences, particularly considering the arguments against inflation and its correlation with employment and economic growth. Too often they avoid to mention the deflation measures that took place in core countries. The deregulation of the German labor market resulted in an overall 6% decrease of wages between 2003 and 2009 and it had a deeper impact on Europe than most of other economy turns (Bagnai, 2012, p.79). As already said, this trend followed an historical tendency, which gave to German companies a crucial advantage in dealing with intra-European competitors. Still, for defending the Euro, one of the most used topic is the reduction of transaction costs. Nevertheless, a study, funded by the European Commission, found that it would amounted only 0.4% of the

European Union GDP, that Eichengreen condemned it as too small for a risky project like the Euro (Bagnai, 2012, p.89).

Therefore, I believed it was worth to be outlined that the misleading information of the actual sources of the last decade economic troubles is systematically carried on in many of the countries that still languish in difficult situations. Austerity measures have been the only response that the EU have given to the worst crisis since the 1930s and the decision to adopt pro-cyclical policies have found opponents not only in universities and think-tanks. The attempt to keep a political project like the Euro alive is having risky consequences that will bring uncertain results, for both winners and losers of this economic hazard.

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Appendix

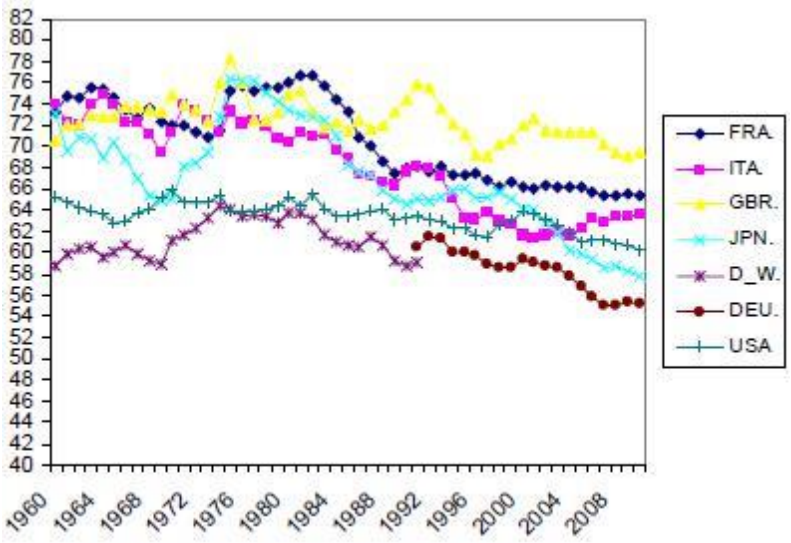

Figure 1. Adjusted wage share in % of GDP at current factor cost, total economy, source Cesaratto and Stirati, 2010

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Belgium	2.1	2.5	3.4	0.7	-2.3	2.7	1.8	0.1	-0.1	1.6	1.5	1.2
Bulgaria	7.1	6.9	7.3	6	-3.6	1.3	1.9	0	0.9	1.3	3.6	3.4
Czech Republic	6.4	6.9	5.5	2.7	-4.8	2.3	2	-0.8	-0.5	2.7	4.5	2.4
Denmark	2.3	3.9	0.9	-0.5	-4.9	1.9	1.3	0.2	0.9	1.7	1.6	1.3
Germany	0.7	3.7	3.3	1.1	-5.6	4.1	3.7	0.5	0.5	1.6	1.7	1.9
Estonia	9.4	10.3	7.7	-5.4	-14.7	2.3	7.6	4.3	1.4	2.8	1.4	1.6
Ireland	5.8	5.9	3.8	-4.4	-4.6	2	0	-1.1	1.1	8.5	26.3	5.2
Greece	0.6	5.7	3.3	-0.3	-4.3	-5.5	-9.1	-7.3	-3.2	0.4	-0.2	0
Spain	3.7	4.2	3.8	1.1	-3.6	0	-1	-2.9	-1.7	1.4	3.2	3.2
France	1.6	2.4	2.4	0.2	-2.9	2	2.1	0.2	0.6	0.6	1.3	1.2
Croatia	4.2	4.8	5.2	2.1	-7.4	-1.7	-0.3	-2.2	-1.1	-0.5	1.6	2.9
Italy	0.9	2	1.5	-1.1	-5.5	1.7	0.6	-2.8	-1.7	0.1	0.8	0.9
Cyprus	3.7	4.5	4.8	3.9	-1.8	1.3	0.3	-3.2	-6	-1.5	1.7	2.8
Latvia	10.7	11.9	9.9	-3.6	-14.3	-3.8	6.4	4	2.6	2.1	2.7	2
Lithuania	7.7	7.4	11.1	2.6	-14.8	1.6	6	3.8	3.5	3.5	1.8	2.3
Luxembourg	3.2	5.2	8.4	-1.3	-4.4	4.9	2.5	-0.4	4	5.6	4	4.2
Hungary	4.4	3.9	0.4	0.9	-6.6	0.7	1.7	-1.6	2.1	4	3.1	2
Malta	3.8	1.8	4	3.3	-2.5	3.5	1.4	2.6	4.5	8.3	7.4	5

Netherlands	2.2	3.5	3.7	1.7	-3.8	1.4	1.7	-1.1	-0.2	1.4	2	2.2
Austria	2.1	3.4	3.6	1.5	-3.8	1.9	2.8	0.7	0.1	0.6	1	1.5
Poland	3.5	6.2	7	4.2	2.8	3.6	5	1.6	1.4	3.3	3.8	2.7
Portugal	0.8	1.6	2.5	0.2	-3	1.9	-1.8	-4	-1.1	0.9	1.6	1.4
Romania	4.2	8.1	6.9	8.5	-7.1	-0.8	1.1	0.6	3.5	3.1	3.9	4.8
Slovenia	4	5.7	6.9	3.3	-7.8	1.2	0.6	-2.7	-1.1	3.1	2.3	2.5
Slovakia	6.8	8.5	10.8	5.6	-5.4	5	2.8	1.7	1.5	2.6	3.8	3.3
Finland	2.8	4.1	5.2	0.7	-8.3	3	2.6	-1.4	-0.8	-0.6	0.3	1.4
Sweden	2.8	4.7	3.4	-0.6	-5.2	6	2.7	-0.3	1.2	2.6	4.1	3.3
United Kingdom	3	2.5	2.6	-0.6	-4.3	1.9	1.5	1.3	1.9	3.1	2.2	1.8

Table 2. Growth rate in percentage, Source Eurostat

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
EU-28	9.3	9.0	8.2	7.2	7.0	9.0	9.6	9.7	10.5	10.9	10.2	9.4
Euro area	9.3	9.1	8.4	7.5	7.6	9.6	10.2	10.2	11.4	12.0	11.6	10.9
Belgium	8.4	8.5	8.3	7.5	7.0	7.9	8.3	7.2	7.6	8.4	8.5	8.5
Bulgaria	12.1	10.1	9.0	6.9	5.6	6.8	10.3	11.3	12.3	13.0	11.4	9.2
Czech Republic	8.3	7.9	7.1	5.3	4.4	6.7	7.3	6.7	7.0	7.0	6.1	5.1
Denmark	5.5	4.8	3.9	3.8	3.4	6.0	7.5	7.6	7.5	7.0	6.6	6.2
Germany	10.4	11.2	10.1	8.5	7.4	7.6	7.0	5.8	5.4	5.2	5.0	4.6
Estonia	10.1	8.0	5.9	4.6	5.5	13.5	16.7	12.3	10.0	8.6	7.4	6.2
Ireland	4.5	4.4	4.5	4.7	6.4	12.0	13.9	14.7	14.7	13.1	11.3	9.4
Greece	10.6	10.0	9.0	8.4	7.8	9.6	12.7	17.9	24.5	27.5	26.5	24.9
Spain	11.0	9.2	8.5	8.2	11.3	17.9	19.9	21.4	24.8	26.1	24.5	22.1
France	8.9	8.9	8.8	8.0	7.4	9.1	9.3	9.2	9.8	10.3	10.3	10.4
Croatia	13.9	13.0	11.6	9.9	8.6	9.2	11.7	13.7	16.0	17.3	17.3	16.3
Italy	8.0	7.7	6.8	6.1	6.7	7.7	8.4	8.4	10.7	12.1	12.7	11.9
Cyprus	4.6	5.3	4.6	3.9	3.7	5.4	6.3	7.9	11.9	15.9	16.1	15.0
Latvia	11.7	10.0	7.0	6.1	7.7	17.5	19.5	16.2	15.0	11.9	10.8	9.9
Lithuania	10.9	8.3	5.8	4.3	5.8	13.8	17.8	15.4	13.4	11.8	10.7	9.1
Luxembourg	5.0	4.6	4.6	4.2	4.9	5.1	4.6	4.8	5.1	5.9	6.0	6.4
Hungary	6.1	7.2	7.5	7.4	7.8	10.0	11.2	11.0	11.0	10.2	7.7	6.8
Malta	7.2	6.9	6.8	6.5	6.0	6.9	6.9	6.4	6.3	6.4	5.8	5.4
Netherlands	5.7	5.9	5.0	4.2	3.7	4.4	5.0	5.0	5.8	7.3	7.4	6.9
Austria	5.5	5.6	5.3	4.9	4.1	5.3	4.8	4.6	4.9	5.4	5.6	5.7
Poland	19.1	17.9	13.9	9.6	7.1	8.1	9.7	9.7	10.1	10.3	9.0	7.5
Portugal	7.8	8.8	8.9	9.1	8.8	10.7	12.0	12.9	15.8	16.4	14.1	12.6
Romania	8.0	7.1	7.2	6.4	5.6	6.5	7.0	7.2	6.8	7.1	6.8	6.8
Slovenia	6.3	6.5	6.0	4.9	4.4	5.9	7.3	8.2	8.9	10.1	9.7	9.0
Slovakia	18.4	16.4	13.5	11.2	9.6	12.1	14.5	13.7	14.0	14.2	13.2	11.5
Finland	8.8	8.4	7.7	6.9	6.4	8.2	8.4	7.8	7.7	8.2	8.7	9.4
Sweden	7.4	7.7	7.1	6.1	6.2	8.3	8.6	7.8	8.0	8.0	7.9	7.4
United Kingdom	4.7	4.8	5.4	5.3	5.6	7.6	7.8	8.1	7.9	7.6	6.1	5.3

Table 3. Unemployment rate in percentage for European economies, Source Eurostat

	1960-64	*1965-72*	*1973-80*	*1980-87*	*1988-95*	*1996-99*	*2000-04*
France	*1,5*	*2,3*	*4,3*	*8,9*	*10,5*	*11,9*	*9,1*
Italy	*3,5*	*4,2*	*4,5*	*6,7*	*8,1*	*9,9*	*8,8*
Netherlands	*0,9*	*1,7*	*4,7*	*10*	*7,2*	*4,7*	*3,2*
Spain	*2,4*	*2,7*	*4,9*	*17,6*	*19,6*	*19,4*	*11,1*
West Germ.	*0,8*	*0,8*	*2,9*	*6,1*	*5,6*	*7,1*	*8,3*

Table 4. Unemployment rate in percentage, from Eichengreen, 2008, p.264

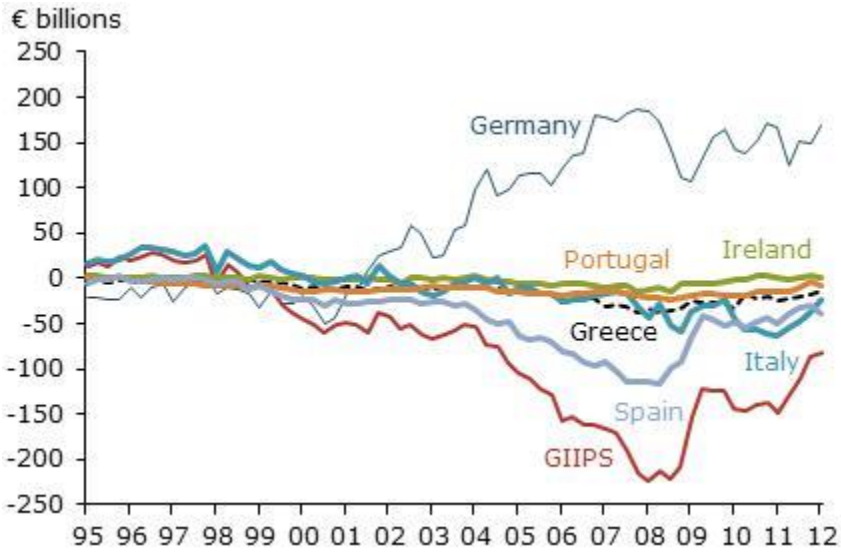

Figure 3. Balance of payments from 1995 to 2012, source Eurostat

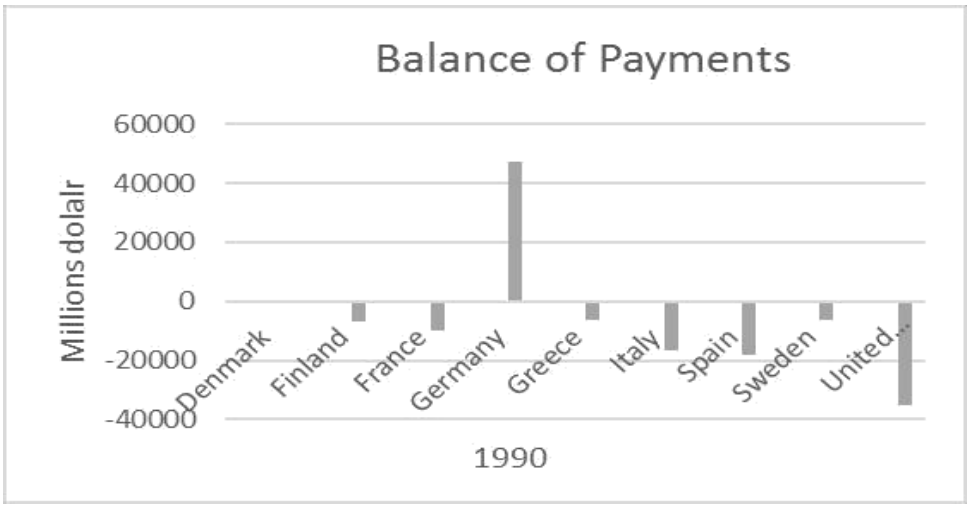

Table 5. Balance of payments for few European countries, source OECD.dat

Graph 2. Industrial production for Germany, France, Italy, Spain and the Euro Area, source Bank of Italy

Year	***Peg***	***Limited flexibility***	***Managed***	***Flexible***
1970	*97.2*	*0*	*0*	*2.8*
1975	*63.9*	*11.1*	*13.9*	*11.1*
1980	*38.9*	*5.6*	*47.2*	*8.3*
1985	*33.3*	*5.6*	*36.1*	*25*
1990	*19.4*	*13.9*	*30.6*	*36.1*
1995	*13.9*	*8.3*	*38.9*	*38.9*

1999	*11.1*	*11.1*	*33.3*	*44.5*

Table 2. Exchange rate classification by the IMF over the years, source Calvo, 2000

	1974-1980	***1981-1985***	***1986-1990***	***1991-1995***	***1996-2000***	***2001-2005***	***2006-2010***	***2011-2015***
France	*2.8*	*1.5*	*3.3*	*1.2*	*2.9*	*1.6*	*0.7*	*0.94*
Germany	*2.4*	*1.3*	*3.3*	*2*	*1.9*	*0.5*	*1.3*	*1.59*
Italy	*3.6*	*1.6*	*3.1*	*1.3*	*2*	*0.9*	*-0.2*	*-0.62*
Netherlands	*2.3*	*1.1*	*3.3*	*2.2*	*4.3*	*1.3*	*1.3*	*0.7*
Spain	*2.2*	*1.4*	*4.5*	*1.5*	*4*	*3.3*	*1.09*	*-0.14*

Table 3. Average annual GDP growth in percentage, source World Bank, own calculation

1960	1965	1973	1989	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
5817	7220	10510	16207	17565	17685	18009	18263	18611	19269	19603	19610	19465	19479	19329
-	2,4	6,4	3,3	2,8	0,7	1,8	1,4	1,9	3,5	1,7	0	-0,7	0,1	-0,8

Table 6. Italian GDP per capita (US$ 2000) and annual growth rate in percentage, source Sapelli, 2012, p.193

	1950-73	1973-89	1990	1995	2000	2005
France	8,2	4,6	4,2	8,4	12,4	3,1
Germany	12,4	4,7	13,2	6,3	13,5	6,3
Italy	11,7	4,9	6,9	12,4	9	0,3
Netherlands	10,3	3,6	5,6	8,8	11,3	5,9

Table 7. Exports of goods and services, annual growth rate %, source Sapelli, 2012, p.197

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
GDP	1,53	0,77	-0,89	2,15	2,83	0,72	1,89	1,44	1,93	3,58	1,8	0,34	0,04	1,07	-0,04
Exp/GDP	17,9	18,3	21,31	22,84	25,74	24,73	25,22	25,19	24,27	27,06	27,09	25,73	24,56	25,34	26,32

Table 8. Italy: annual GDP growth rate % and exports/GDP comparison in %, source Sapelli, p.198

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Austria	-1.7	-6.9	-6.7	-5.1	-3.5	-3.6	-1.4	-1.6	5.6	4.3	6.4	6.6	9.2	13.2	20.3	10.4	11.4	8.2	8.8	10.6
France	8.2	11.0	20.8	37.2	38.9	46.0	19.3	23.6	17.4	14.3	10.5	-10.4	-12.9	-25.9	-50.0	-39.4	-45.2	-59.6	-51.0	-46.2
Germany	-30.3	-29.4	-13.7	-10.0	-17.0	-29.0	-34.3	-0.3	40.6	47.1	124.6	137.9	180.9	250.2	226.9	197.7	196.2	204.6	187.5	199.5
Greece	-0.2	-3.2	-5.1	-5.3	-3.8	-7.7	-9.9	-9.5	-9.7	-12.8	-13.3	-18.3	-29.8	-44.9	-51.2	-36.0	-30.6	-29.3	-20.4	-17.2
Ireland	1.5	1.7	2.0	1.9	0.7	0.6	0.1	-0.7	-1.2	0.0	-1.1	-7.0	-7.9	-14.0	-15.1	-6.5	1.0	0.2	2.7	4.3
Italy	13.9	23.2	40.2	33.8	19.8	8.1	-5.7	-0.6	-9.8	-19.6	-16.4	-29.5	-48.1	-51.8	-65.4	-41.4	-71.7	-69.2	-45.5	-35.3
Netherlands	18.4	25.8	21.2	25.5	13.3	16.6	7.9	10.3	11.4	30.5	48.1	48.2	63.0	52.4	37.2	33.3	55.7	77.2	71.1	78.5
Portugal	-2.2	-0.2	-4.9	-6.8	-8.8	-11.0	-12.2	-12.4	-10.9	-10.5	-15.5	-19.8	-21.5	-23.5	-31.9	-25.6	-22.8	-15.4	-8.7	-4.9
Spain	-6.5	-1.7	-1.5	-0.6	-7.2	-17.9	-23.0	-24.0	-22.5	-31.1	-54.9	-83.1	-111.1	-144.6	-154.6	-69.9	-62.8	-52.6	-12.2	2.0
Euro area	17.1	44.3	71.3	90.5	51.6	21.6	-39.4	3.0	44.1	42.3	110.9	39.2	35.4	24.1	-93.3	21.1	43.3	62.5	130.7	193.9

Figure 4, Current account balances in billion USD 1994-2013, source OECD