Wrocław Summer School 2013

# HOW OLD AND NEW DEMOCRACIES COPE WITH THE ECONOMIC CRISIS

## FINAL REPORT

Uniwersytet Wrocławski

Wrocław Summer School

23 June – 7 July 2013

# How old and new democracies cope with the economic crisis

## Final report

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Wrocław 2013

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# LOCAL LEVEL

## Final Report of the Local Level Group

## Introduction

The international economic crisis has affected virtually every country in Europe, one way or another. The impact of the crisis varied throughout the member and the EU, with some of them facing serious financial problems, as it is the case with Greece, Spain or Ireland, but other countries, like Germany or Poland fared much better. This report aims at looking into some of this aspects, in order to compare and highlight differences and similarities between some of these countries which may account for the differences in country performance.

To this purpose, we focused our report on the workings of the local government's system and how local authorities manage their domains in order to cope with the economic crisis. Our effort represents just the first, smaller level of governance and it is meant to complement the other two levels, national and European, thus offering a comprehensive perspective on this subject.

We divided our research in two parts. The first part is a comparative study of the different administrative systems in Belgium, Croatia, the Czech Republic, Germany, Poland, Romania and Slovakia. The fields chosen for this comparison range from fiscal measures and budget expenditures, to changes in public administration and local initiatives. For the second part of our paper we took on a practical approach, a field research consisting of interviews with a number of representatives of the local and regional government in and around **Wrocław.** We were particularly interested to see how Polish local governments support the small and medium enterprises and what their strategies for attracting and ensuring the loyalty of foreign investors are. Apart from this we also looked into the relation between the different administrative levels and the role of decentralization in managing the available resources to the benefit of the local communities.

In doing so, we hope to find patterns of local governance that may benefit communities from other countries in coping with the economic crisis.

## Comparative Analysis

Small and Medium Enterprises were affected in all the countries analyzed. In some of them measures were undertaken to re-launch the activity of the SMEs but also to attract foreign investors and to motivate local entrepreneurs.

In **Germany**, 99.7 % of all companies in Germany are SMEs and they mostly provide services. During the crisis, the SMEs found it harder to get a credit (the interest rate went up 20%). Consequently, about 42% of SMEs were affected by the crisis. The federal government is using the economic stimulus packages 1 and 2 (which consist in the distribution of money to improve infrastructure, tax cutting, improving domestic consumption, lowering medical insurance fees etc.) to ease the economic burden on SMEs (to cut taxes for SMEs).

In **Belgium**, the SMEs are managed by the regions and the local government. Through Marshall Plan Green 2, the SMEs were financed and policies were passed to support and consolidate entrepreneurial spirit, the internationalization of companies and the territorial management for investments. Also, the enterprises that focus on innovation, research and development are exempted from taxes.

In the **Czech Republic**, the SMEs are in a difficult situation, with some bankruptcies, but there is no additional taxation for the companies.

In **Croatia**, more specifically in Zagreb ,there is a long-standing program which was implemented in order to finance the SMEs through credit subventions. This strategy was launched in 2009 and was completed with the help of Regional guarantee instruments, such as local micro-crediting projects.

In **Romania**, the SMEs are managed by the state. During the crisis, 15% of the SMEs in Romania declared bankruptcy and 72% declared a decrease in their activity. Also, the government raised the tax on dividends from 10 to 16%, making it harder for SMEs to reinvest their capital. The SMEs were assisted nationally by the Agency for the Implementation of Projects and Programs for the Small-to-Medium Sized Enterprises. They received credits and loans from small banks mostly.

In **Slovakia**, SMEs are not dealt with at the local level.

In **Poland**, in Wroclaw, based on the interviews taken, one can conclude that the focus is mainly on foreign investments. We can however give the example of Olesnica, where the local government created a sphere around the companies that increased cooperation, provided tax exemption and helped them stay competitive. Nevertheless, the interviews we made have shown that local entrepreneurs know some difficulties for receiving loans from banks.

Taking all this into account, each of the countries analyzed suffered from the economic crisis regarding to their SMEs. In all the countries, financial mechanisms had to be put in place to assist the SMEs, but the degree of assistance varied. The countries that entered the European Union later had to give more support to local entrepreneurship.

**Budget expenditures** were the main concern once the crisis hit, with spending being restructuring.

In **Germany**, the federal states don't have the possibility to apply for new credits from 2020 onwards. Another budget measure of balanced budget provision, called the "Debt Brake", was also implemented in 2009 and was legally reported in the German Constitution. However, in that provision, exceptions are made for catastrophes and natural disasters but also during recession's periods. The credits subscribed during the crisis times have to be refund during the economic recovery with an interest rate of 0.35% of the annual GDP. In Germany, the Federal Constitutional Court is playing a major role regarding the budget expenditures. Indeed, this one has the ability to void the budget and to vote measures to reach balanced government budgets. There is also a solidarity mechanisms put in place between the different federal states: the most efficient ones, such as Rhineland-Palatinate, have to financially support the economically weaker ones.

In **Belgium**, there was an increase regarding the local taxes and several cuts in spending have been operated in different sectors such as the promotion of green energy few months ago. There also has been a project of taxation for owners of solar panels which didn't obtain unanimity.

In **Romania,** according to the economic classification, one can noticed that there were some mismanagement regarding the budget expenditures between 2006 and 2009. Indeed, this report claimed that higher spending was attributed to unproductive realms (salaries of government members, pensions) which don't bring added value in the economy while spending for investments dropped. That occurred even if Romania received more than €10 billion from financial international institutions to improve its infrastructure. One can also observed a change in the projects public expenditures are targeting. Indeed, they are most aimed to support job creation, investments, businesses, labor market, to help people at risk during the crisis times and to boost the demand.

In **Croatia**, the local level witnessed a rise in its public expenditures. The total budget expenditure decreased after 2008 after a decision of the national government, but the compensation of employees continues to grow, so the savings are reached in another realm than the public one.

In the **Czech Republic**, there exists interdependence between the national and the local levels concerning the field of budget expenditures. In fact, the local level depends on savings made by the national government and so the regions could only save proportionally to the national level.

In **Slovakia**, there were some cuts in investments in favour of social measures. Also, no new taxes were introduced.

In **Poland**, at the local level, there was a small decrease in the budget expenditures but the politicians we interviewed declared that Wroclaw didn't suffer from this cut because the city relies almost on foreign investment and European funds for infrastructure mainly. These EU funds split between each level of powers during big campaign investments such as Euro2012, proving the territorial division of the country.

We could conclude this point about budget expenditures by saying that there doesn't exist a kind of uniformity across the European countries we tried to analyze. However, we could observe a general trend to an increase of the regime of taxes and a cut in public expenditures, except for some realms such as in Romania where the government operated a turn in its target spending.

**The Fiscal Measures** were one of the changes that the population could easily recognize and by which they were most affected.

In **Germany**, the taxes did not change as a result of the crisis.

In **Belgium**, at the local level the taxes increased before the economic crisis, so when the crisis hit, the local government had to seek other means for financing, for example by cutting the subsidies for green energy. Also, the Belgian government has also raised excised taxes on alcohol, tobacco and diesel fuel. In Belgium the general VAT remained at 21%, but the VAT for food and agricultural products dropped from 7 to 6 %.

In **Czech Republic**, the reaction to the crisis at the local level was mainly to implement an austerity package conceived at the national level in 2009. By 2011, the government deficit has dropped from 5,8 % of GDP in 2009 to 4,3% of GDP in 2011. Also, during the crisis, the normal VAT rose from 20% in 2009 to 21% in 2013 and the reduced VAT also rose from 10% in 2009 to 15% in 2013.

In **Croatia** there is a degree of fiscal decentralization. During the crisis, the central government applied a mechanism known as fiscal equalization through which it tried to reduce inequalities arising from the uneven distribution of income at lower levels authorities. In Croatia the VAT dropped from 25 to 22%.

In **Romania**, there is talk about the implementation of a law on fiscal amnesty for those local communities that are highly indebted to the national and private creditors. Also, the central government has put in place a tax exemption for companies that hire young graduates and people with disabilities. Furthermore, from the national level there is a special tax deduction for people that pay taxes using the eGovernment application. Moreover, there was a visible raise in local taxes (e.g. increase in the price of the tickets for public transportation, parking; massive cuttings of subsidies for heating, for the disabled – the city of Arad, registered an increase of 22% in taxes quite defective). Also, a national measure that had important local repercussions was the increase in the VAT from 19% to 24%.

In **Slovakia**, the VAT rose from 19 to 20%, but there were no fiscal measures taken locally that had any effect.

In **Poland**, from the surveys one can point out that firms benefit from a tax exemption for up to 10 years on (but this is a national directive). The local government can influence the offer on the price of the land. The VAT rose from 19 to 23%.

All in all, the fiscal policy is one of the most visible sector that was modified during the crisis and the one sector that had one of the largest impacts on day-to-day activities and at the local level.

**The Social System** is the one that is reformed during a crisis, mainly because of the complicated mechanisms and the large amount of money that goes through the system.

In **Germany**, there was a labor market reform (Agenda 2010) that regulated and brought together unemployment and social security benefits (2005). This reform indicates that unemployed people receive social benefits for 1 year, however if the unemployed don't find a job in a year they only got the minimum pay-out.

In **Belgium**, the social security system is in the competencies of the federal state, though the Flemish community wants to divide it between different communities. At the local level there are organisms such as FOREM and ONEM. The main objectives of these institutions are finding a job for the unemployed by providing trainings and language courses. Another organism is CPAS that provides allowances for the unemployed and socially deprived.

In **Croatia**, the number of applications for unemployment benefits has increased sharply as a result of the crisis. The government conducted two types of programs to help the unemployed. Firstly, income support programs, such as unemployment benefits. And secondly, the so-called active labor market programs, such as public works, subsidies for groups with lower employability or training to reintegrate the unemployed into the labor market. Also, the people to get social help will be selected on the grounds of a property census.

In the **Czech Republic**, the unemployed had the opportunity to earn money doing services for public good causes. But, the money for social services was reduced (for orphanage, house for retired people, single mothers with children, disabled people, civil organizations looking after disadvantaged people). Also, the taxation increased.

In **Romania**, there was a general increase in the expenditure for social assistance programs (e.g. unemployment relief, social benefits for disabled etc.), but there was also a recalculation of pensions for former army personnel, at the national level. Also, contributions paid by employers grew to 20,8% and that of employees to 10,5%. At the local level, there were initiatives to improve the living standards for Roma living in Pata Rat, a Roma settlement on the outskirts of the city. One such project was called the 'business incubator' which aimed to provide training in professional waste selection for adults who worked in the garbage dumps near the settlement, while an Inclusion Centre provided temporary and permanent shelters for young and vulnerable Roma families living in the settlements. In Arad, there were two local projects run by the municipality – an art therapy 'creative centre' and a laundry service which employed people with disabilities – with the aim to encourage the social and professional rehabilitation and independence of people with disabilities. These projects took place on 27-28 May 2013.

In **Slovakia**, the social system is not managed locally.

In **Poland,** there were no local level initiatives to interfere with the social system. At the national level, cash transfers for private funds should decrease to 2.3%.

All in all, it is clear that all countries worked hard to tackle unemployment and that the structure of the social system had to be reconfigured in light of the necessary budget cuts that had to be implemented because of the crisis.

**Public Administration** was one of the most affected sectors, especially because in most countries the bureaucratic apparatus is unnecessarily large. That's why the majority of layoffs happened in the public sector, more specifically, governmental positions.

In **Germany**, the salaries weren't affected. But in some areas the rate of unemployment increased.

In **Belgium**, there was no reduction of public administration apparatus and there were no salaries cuts. However, there was a limitation in the number of provincial deputies and concerning the public administration budget.

In **Croatia** the crisis brought about a decrease in salaries and a reduction in the number of employees in the civil services. Also the need for professional retraining of personnel in the public administration became paramount.

In **Czech Republic**, there were only some small reductions of positions.

In **Romania,** approximately 60 000 people lost their jobs from governmental positions. More than this, governmental positions on all levels were blocked. Salaries cuts, cuts in bonuses and compensations were also employed as means to fight the crisis.

In **Slovakia**, the regional state administration offices were replaced by new sectorial offices (which dealt with taxes). The wages were also frozen

In **Poland ,** the results of the surveys led us to believe that even though unemployment is an issue that the government is tackling (the local government even receives funds to fight the issue of unemployment), reductions and salary cuts were not an issue.

To sum up, besides budget expenditures, the public administration sector had to deal with a lot of changes, especially in the new member states of the European

Union. It's comes down to the political system and how well-organized, efficient and flexible it is.

**Local initiatives** are important because they can help improve the conditions for the local communities. If the local community gets involved, on the long-term it can be beneficial in building the awareness of the social community.

In **Germany**, to mitigate the effects of the global financial crisis, the Rhineland – Palatinate provincial government adopted the Future-Investment-Act. The Aim was to secure jobs, support companies and to invest sustainability. The additional capital expenditures have been around about 854 million euros. 2656 projects mainly in the communities were implemented. The federal republic sponsored 449 million euros. The rest was supported by the provincial government, the communities and the private agencies. Following examples: 10 out of 2665 projects from the Future-Investment-Act in Rhineland-Palatinate.

1. School restauration: Renewal of windows and exterior doors, heat insulation of the exterior wall in Kobern-Gondorf (Rhineland-Palatinate).

Investment volume: 397.000 Euro

2. School restauration: Energetic and fire protection-judical restauration of the auditorium inclusive the WC- area in Neuwied (Rhineland-Palatinate).

Investment volume: 982.940 Euro

3. Kindergarten restauration: Renewal of the roof, exteriall wall and windows in Stipshausen (Rhineland-Palatinate)

Investment volume: 370.000 Euro

4. Restauration of advanced training facilities: Energetic restauration due to roof insulation, replacement of windows and construction of a new solar collector system in Altenkirchen (Rhineland-Palatinate)

Investment volume: 254.361 Euro

5. Energy efficiency and electrical power supply: Construction of a biomass-heat-plant, a local heat net to supply communal facilities.

Dierdorf (Rhineland-Palatinate)

Investment volume: 3.662.702 Euro

6. Energyefficiency and electrical power supply: Construction of a biomass-heat-plant, a local heat net. As well as an energetic restauration of a sports hall in Altenahr (Rhineland-Palatinate)

Investment volume: 845.518 Euro

7. Fire service and emergency management: New construction of the fire department and the fire company in Bad Kreuznach (Rhineland-Palatinate)

Investment volume: 1.600.000 Euro

8. Sports complex construction: Overall restauration of the sports hall in Saulheim (Rhineland-Palatinate)

Investment volume: 2.122.000 Euro

9. Fire department control room: Technical installation of the integrated coordination-centre with information and communication technics in Landau (Rhineland-Palatinate)

Investment volume: 1.900.000 Euro

10. Broadband supply (ductwork): Ductwork laying to establish a broadband infrastructure development in Rockenhausen (Rhineland-Palatinate).

Investment volume: 352.862 Euro

In **Belgium**, the Marshall Plan Green 2 was implemented in the region of Wallonia. This program facilitated access to investment grants, reduced tax for enterprises, helped with the developing of industrial research and partnerships between universities and enterprises and it also helped with the developing and improvement access to vocational training. A second programe is Creative Wallonia (aim: Positioning Wallonia within a global, open and malleable economy; innovation is the driving force for the new economy).

In **Croatia**, more specifically in Zagreb, at the local level we can talk about a large number of social programs (social care centers, day care facilities, hospitals and institutions for mental patiens). There are also measures taken to support local stakeholders in defining, creating, facilitating and implementing local employment policy and human resource management through a partnership approach in Croatia.

But as opposed to these positive measure, some cities have added an additional tax (*prirez*) that the taxpayer have to pay to the municipality or city.

In the **Czech Republic** there was a significant rise in the civic society's activities in favour of anti-corruption idea. Corruption on local level is a big issue – it is said that if there were no coruption, then the local government would have enough money to cope with the crisis.

In **Romania,** in Sibiu there was a Romanian - German partnership with local CSOs and NGOs for the city rehabilitation, promotion and development (e.g. Foundation for Urban Rehabilitation). Public activities were also regulated, for instance parking in many major cities (Galati, Sibiu, Constanta) and reduction in the local transportation expenditure.

In **Slovakia**, there was an initiative of the Bratislava self.gov. region to increase transparency in self-governance, the so-called "Open Self-Government" Project.

In **Poland**, in Olesnica a sphere of cooperation was created so that the companies benefited from special tax exemption during the crisis and also special directives for imports and exports so that they could stay competitive. Moreover, the *gmina* is cooperating with the *powiat* to transform a military airport into a commercial terminal. The project will also include a scientific research center and a huge recreation area, with a flying school and a gliding club, as well as a pool and other facilities.

## Field surveys

The aim of the field surveys is acquiring first-hand data about the policies implemented at the local level. To this end we interviewed members from all three levels of administration—*gmina, powiat and województwo*— and from various political and professional backgrounds. The methodology used for this survey was a standardized set of open questions, designed to showcase the most important decisions and attitudes in managing the economic crisis. At this stage we should stress out the limitations of the methodology used. Firstly, the region selected for the case study, has several particularities, such as the geographic position and historical background, that gives it a privileged position compared to other Polish regions, and therefore, the results of this research may not reflect the Polish realities as a whole. Secondly, the relatively small scale of the survey must be taken into consideration. Eight members of the local and regional government were selected for this, and although they represent only a small fraction of the administrative apparatus, their comments and opinions on these issues are nonetheless relevant towards identifying a certain political mindset.

The causes for the economic crisis in Poland

From the analysis of these interviews, one conclusion is readily available right from the beginning. Unsurprisingly perhaps, when asked about the causes for the economic crisis in Poland, the majority of the respondents were quick to mention that Poland, or their region or municipality was not really in a state of economic crisis. **Jacek Ossowski**, Chairman of the City Council in Wrocław, noted for example that the economy is still stable and that it is one of the few in the region who still experiences economic growth. **Marek Dyuduch**, a member of the SLD party, stated that although the costs of living are increasing, the crisis has yet to reach Wroclaw, and it is rather an issue for the other countries. Others shared this view, although they pointed out some deficiencies in the economic sector. **Bartlomiej Ostrowski,** from the Department of Foreign Affairs at the voievodship level**,** lamented the gradual disspearence of the industry in Europe, caused by a decrease in competitiveness towards the Asian markets. The same problem was noticed by the members of the City Council in **Oława**, who remarked that it is almost impossible to compete with the cheap labour offered by countries such as China. Even so, the general tone with regard to the economic situation was optimistic, a fact which was visible not only in the large and influential Wroclaw, but also in smaller, neighbouring towns. **Zbigniew Potyrała,** the Foreman of the County Council in Olesnica, pointed out that although is region is facing an increase in unemployment, in his opinion, we cannot speak of an economic crisis and that an economic boom is yet to come.

Still, there was a general consensus that the crisis did have some effects and the **sector which was most affected** by this was the real estate. According to **Aleksander Marek Skorupa**, the Voievode of the Wrocław Region, this was in connection with credit and loans sectors, which suffered from the crisis, and which had a negative impact on constructions in general. The Foreman of the County

Council in Olesnica remarked a certain chain reaction that started with the difficulties in the real estate and affected the furniture industry in his county.

The interviews of Aleksander Marek Skorupa and that of Jacek Ossovski were particularily fruitful in giving an overview of the economic situation in the Wroclaw region. Although their main attributions diverge, when faced with the same set of questions, their answers identified similar causes and solutions for the crisis. They both pointed out that the Polish economy is a reactive one, strongly connected with the German economy and the Eurozone, as a whole. They also stressed the fact that the crisis in Poland has not been felt in 2008, with 2012 being actually the most challenging year of the national economy and with 2013 being a particular difficult year. So far, Poland has registered growth in the GDP, both nationally and locally.

Strategies and measures for managing the economic crisis.

The general positive outlook on the economic situation appears to be stemming from the large number of investments in that region. We certainly observed this even in smaller towns near Wroclaw. The case of Olesnica is especially telling. When asked about the long-term strategies employed in dealing with the crisis, **Zbigniew Potyrała** of the County Council in Olesnica, pointed out the very modern infrastructure that they managed to develop in their town and region. A highway connects Olesnica to Wroclaw which allows a person to go from one part to the other in 20 minutes and reach the Wroclaw airport in 40 minutes. Mr. Poty remarked that it actually takes less time to go from Olesnica, which is 30 km away from Wroclaw, to the Wroclaw airport, than from the airport to the center of Wroclaw. The modern road network is of particular importance to Olesnica, in light of a new massive investment which is the Olesnica Airport. Built on a former military base, the new civilian airport will act as an alternate for the Wroclaw airport and will have a capacity for up to 4 mil. passengers per year. The new airfield will also be the place for a production company from the aeronauticul industry, and the Politechnika Wroclawska will also have a research center there. Besides, the airfield will also be the home of a flying school and gliding club and a conference hall and recreational area will be built in the proximity. Investments like these are paramount to the local economy and show that smaller towns such as Olesnica can also be the sites of a dynamic economic environment.

Another important strategy was revealed by **Mr. Huzarski**, Chairman of Social Policy, Health and Family suport Committee of the regional level in Wroclaw. Apart from confirming the importance of developing the infrastructure (roads, industrial parks), he also stressed out the importance of investing in the human capital. „In order to have companies investing in your region, you have to have specialists who can meet the demand.", Mr Huzarski said. To achieve this, the region directed 70 mil PLN towards research and buying equipment for laboratories of the Technical University in Wroclaw. Apart from this, they will also invest in a new school that will prepare future workers in the hotel industry, as the region is home to the largest hotel in Europe. Because there is no significant strong local capital (production), the foreign companies employ the local highly trained human capital, which leads to the development of local entrepreneurs and thus, we can conclude that HR investments is indeed a very good long-term strategy for economic development.

<u>The role of the administrative system</u>

So far we have focused on the current economic situation and some of the most important policies undertaken at local level. However, one must also take into consideration the role of the administrative system. To this end, we asked the following question: "**Do you think the voivodships, powiats and gmina cooperate to solve the crisis? If Yes –How do they cooperate? If No – Why don't they cooperate?"**

Here too the responses were similar, with a few notable exceptions. The interviews, revealed a universal appreciation for the decentralized system. Mr. **Potyrała** who is a public servant for thirty years, compared the centralized system of the 80's to that of today and remarked that decentralization gave them new impetus, "new energy to act", as the decisions were not coming from the top any more. One comment was especially telling: "We do not like Warsaw knowing too much about what happens in our community." He also stated that in spite of the generally low funding from the state budget, they do receive quite a lot of funds for fighting unemployment and investing in infrastructure. Regarding the other levels, he commented that the division of responsibility is very strict and based on law so there are no conflicts between them.

The issue of the coordination between the three tiers of government in Poland is differently assessed by the two representatives of the Wroclaw administration, Mr. Skorupa and Mr. Ossovski, respectively. While they concur regarding the beneficial consequences of such cooperation, Mr. Ossowski perceives it as being imperiously necessary, together with the stability and continuity of the government, whereas Mr. Skorupa reasons that the *gminy* are to be left in managing their own activities, with the institution of the Woiewode stepping in only in special cases of emergency (*e.g.* floods and other natural hazards that might overwhelm the local communities). Hence, the Voievode's attribution is not that of suggesting what the *powiats* and the *gminy* should do, but rather to ensure the observance of the Constitution and of the national legislation in the communities. Nevertheless, the two representatives of the local authority emphasize the self-government as being a veritable success for Poland.

With regards to the distribution of funds from the national to the regional level, an interesting point was made by **Marek Dyuduc,** who said that he does not feel any solidarity with other regions that do not gain that much money from the funds because he thinks that if they are not inovative and competitive, they do not deserve the money.

<u>Conclusions</u>

There were several points which were stressed out by all officials that show that the decentralization mechanism in Poland is working effectively and that there is a coherent approach to vital issues. First of all, all the politicians interviewed agreed that Poland and more specifically the region of Wroclaw was not strongly affected by the crisis. There were several reasons for this and most of the politicians views converged on why they have this *status quo* in Poland, which are the main means to fight the crisis and which was the main sector affected by it.

For a more concrete approach, it has to be underlined that all the politicians agreed that Poland was very successful in attracting European Funds during the years of the crisis. Also, the presence of several large companies in the area (LG Mobile, GKN, KGHM) and decentralized structure of allocating and using the budget has helped the region remain strong (the Lower Silesian Voievodship is the second strongest Voievodship in the country). There is however one potential problem for this region. The local government's focus on attracting investors has created a very prosperous community, but it has also created a kind of vulnerability, that is the over dependency on foreign companies. But the local authorities have identified at least one way to deal with this problem. One of their strategies is the investment in human capital and research. Today’s economic environment and huge global markets make it very difficult for European companies to employ cost efficient labor force, when Asian markets, for example, offer very cheap labor. It is only natural that companies will seek to minimize their production costs, as much as possible and to relocate to other parts of the world. However, creating a very skilled workforce, together with supporting technological innovation are two ways of circumventing this short comings, and increasing competitiveness.

To sum up, the success of the administration in managing the crisis can be attributed to a proactive attitude, developing infrastructure projects and taking advantage of European funding whenever available, long-term planning and investments in research and education in order to create a highly skilled workforce that can both attract foreign companies and form the basis for future local businesses.

## Conclusion of the report

After analyzing and comparing these 7 countries of the European Union regarding their responses to the economic crisis at their respectives local level, we can firstly conclude that all the sectors we focused on have been and still to be affected by the crisis, at various degrees however.

In all the realms we analyzed, we pointed out that the sectors linked directly to the economy were those which were suffering the most from the recession's period. In this regard, we firstly focused on SMEs, budget expenditures and fiscal measures.

Concerning SMEs, a lot of local entrepreneurs throughout the EU encountered difficulties to get a credit from the bank, due to the crisis in the banking system which began in 2008 and the lack of trust from financial institution for new SMEs. Consequently, local entrepreneurs were suffering from a lack of support in their initiatives. The solutions provided by the different local governments in this perspective covered a certain uniformity in the coutries analyzed. We could sum their action into a double-folded strategy: on the one hand, the exemption of taxes and on the other hand the use of economic stimulus such as Plans, Packages, and credit subventions provided by governments and implemented at the local level.

Regarding to the budget expenditures, we could not observe a high degree of uniformity in the management of the local powers we analyzed. However, one can see a general trend towards an increase of the taxation regime (except for some countries such as Slovakia) and cuts in public expenditures.

The last category analyzed into the economic field is dealing with fiscal measures adopted by the different member states. The fiscal statement was highly modified during the time of the crisis in all the countries. In the majority of them, we could witness a rise in the taxation level by the local governments and in some of them, modifications have been introduced in order to ensure a better redistribution of the money collected by taxes between the different levels of power. Moreover, we can observe a difference between the older and the newer states. Broadly speaking, the formers are less affected by the economic crisis and had to put almost in place rigor measures concerning fiscality. The member states coming from the last eastern European enlargements had  to implement tougher fiscal measures, and sometimes they had to go to austerity to not deepen their public debt.

However, one could argue that eastern economies are maintaining ties with north-western ones, such as Poland which is keeping strong links with Germany on an exportation basis. Thus, those countries are consequently under less economic pressure than those in the South of Europe.

From a more political point of view, our analyses conducted us to focus on the impact of the economic crisis on the public administration in our seven countries. According to the hugeness of the buraucratic apparatus prevailing in EU member states, the different local public administrations were one of the most affected by the economic crisis, with cuts in public servant's salaries and limitations regarding the provision of jobs in the public service. Although the local public administration met difficulties to deal with the crisis, there were no big cuts in the majority of the countries analyzed proportionally to other sectors. We can also point out that there were more cuts in the new EU member states.

Concerning the social system implemented by the different countries, it has been subject to a lot of reforms and cuts in order to improve its performance. We observed that, in the majority of the cases, social security is nationally managed but redistributions are operated at the local level. Also, the main problem tackled by the different local governments is dealing with unemployment. Nevertheless, we remarked that some countries, such as Romania, are more actives than others ones by initiating a lot of social projects which are designed for different categories of population.

Actually, as we chose to deal with the question of the implementation of local initiatives to solve the economic crisis. We noticed that each country tried to put local actions in place but these are mostly managed by the national government with the establishment of plans which are designed for the local executives. However, we witnessed a increasing implication of different NGOs and of the civil society in order to conduct local initiatives. We also observed a positive correlation between the presence of an active civil society, such as in Germany, and the effective outcomes of local initiatives.

To put it in a nutshell, we can conclude by saying that all the countries we analyzed were more or less affected by the economic crisis, almost regarding the job promotion and the creation of opportunities in both economic and public sectors at the local and regional levels. However, local governments launched initiatives in order to revitalize their economy and to create jobs. We could also declare that there were differences in the management of the crisis between the newer and the older member states, the older ones meeting less difficulties and benefiting from more political stability. A last thing which caught our attention is the cooperation between the different levels of power in the countries analyzed in the aim to find solutions to overcome the economic crisis but also the cooperation, not deep enough yet, between the member states concerned, for example between Poland and Germany regarding import-export businesses and the presence of western organizations in eastern countries in order to support their local actions and to help them in the stabilization of their regimes in a crisis period.

# NATIONAL LEVEL

## Final Report of the National Level Group

Josip Lučev

## Introduction

This report will track the response to the 2008/09 crisis in seven countries. In order to assess the impact and course of the following recession real GDP rates, unemployment and investment levels will be investigated, as well as their changes through time. The report will shortly show ways in which these were influenced by fiscal policies, monetary responses and exchange rate behavior.

The European project could succinctly be summarized as a series of reforms intended to remove complexity and make the economic environment more stable and predictable. A single market removes the threat of protectionism and tariff wars. A single currency necessitates common monetary policy and removes any possibility of exchange rate fluctuations ensuring a stable trade relations and investment/saving conditions. A fiscal union is a final step in this process and if fully implemented it will stabilize aggregate demand management and public debt levels. The general hypothesis of this report is that stable and predictable macro-policies are not always the best solutions for a periphery country facing a recession. A common currency reduces an important maneuvering position in exchange rate policy which determines the trade balance, which suggests that any Eurozone member will not be able to stop GDP plummeting away by exchange rate modifications. The same is true for unilateral monetary expansionary policy, as this is the responsibility of the European Central Bank. Obviously, any EU member country is already generally unable to improve its short-term trade position by tariff changes. Finally, austerity measures implicit in the Fiscal compact will reduce the possibility of the hardest hit countries in resolving the crisis by expansionary fiscal policy.

An important element to bear in mind is that this trade-off of sacrificing the ability for counter-cyclical policy in favor of stability is very German indeed. Informed by a doctrine of *ordo-liberalism* it was a basis of German macro-policy even in the early phases of West Germany. There was only a brief Keynesian (i.e. fiscally expansive) interlude 1966-1974 before counter-cyclical fiscal policy was again supplanted by a monetarist approach to crises (Dauderstädt, 2013). In its current position Germany stands to benefit from a common market, a common currency and a common fiscal stability, as it sports a substantial (and steadily growing) trade surplus enabling low unemployment levels and good average growth levels (although not necessarily during crisis). Same is not true for many countries on the European periphery, where the ability for an independent macro-policy might be helpful in resolving unfavorable economic conditions such as an aggregate demand crisis or long-term competitiveness problems.

## Effects of the crisis

Almost all European countries experienced two real GDP[1] downturns in the past years. Still, the economies of the seven countries in question handled the recession quite differently. Following is a short summary of their growth patterns.

Poland is a notable exception. It is the only EU member with no real GDP contraction in 2009, and one of the few with no contraction in 2012. In this sense it is not only the best performer of the selected seven countries, it is the best EU performer in recent years. Real growth rates were 6,79% in 2007, a slightly lower 5,13% in 2008, the lowest point of 1,63% in 2009, a recovery of 3,88% in 2010 and 4,32% in 2011 and a new slowdown at 2,05% in 2012 (IMF, WEO April 2013). This makes the average growth rate for 2008-2012 period 3,4%.

Real growth in Slovakia fell from a remarkable 10,49% in 2007 to 5,75% in 2008 and contracted in 2009 at -4,94%. Still, in 2010 Slovakia could boast the fastest growth of the Eurozone (and second only to Sweden in the EU) at 4,38%, a slightly lower 3,23% in 2011 and a slowdown in 2012 at 2,03% (IMF, WEO April 2013). The average growth rate for 2008-2012 period was 2,09%.

Germany is often dubbed the motor of the European Union. Often enough, this is construed as a reference to its high net export rates. Germany is, however, a country preferring several pro-cyclical policies (e.g. fiscal responsibility), enabling the sharp downturn in 2009 and a marked slowdown in 2012. Still, its overall robustness helped it to a quick recovery in 2010, and should produce another one in the years to come. Real growth rates were 3,39% in 2007, a much lower 0,8% in 2008, the lowest point of -5,07% in 2009, a recovery of 4,02% in 2010 and 3,1% in 2011 and a new slowdown at 0,87% in 2012 (IMF, WEO April 2013). This makes the average growth rate for 2008-2012 period 1,18%.

[1] Nominal GDP corrected for inflation

Belgium historically produced low but stable real growth rates, typical for a developed market economy. A normal growth rate of 2,88% in 2007 slowed down to 0,99% in 2008, and contracted at -2,78% in 2009. There was a growth recovery in 2010 (2,42%) and 2011 (1,78%) and a small contraction of -0,2% in 2012. (IMF, WEO April 2013). The Belgian economy grew at an average of 0,44% in the 2008-2012 period.

Romania is the only one of the seven economies whose real growth accelerated in 2008 at 7,35% compared to 6,32% in 2007. Still, in 2009 Romania experienced a contraction of 6,58%, and in 2010 the contraction continued at a further -1,15%. There was a minor recovery in 2011 at 2,16 which slowed down in 2012 to 0,33% (IMF, WEO April 2013). This translates into an average growth rate for 2008-2012 of 0,42%.

Czech economy slowed down from 5,74% in 2007 to 3,1% in 2008 and -4,51% in 2009. Its recovery was less then remarkable at 2,49% in 2010 and 1,89% in 2011, contracting another -1,25% in 2012. (IMF, WEO April 2013). The average growth rate for 2008-2012 period was therefore 0,34%

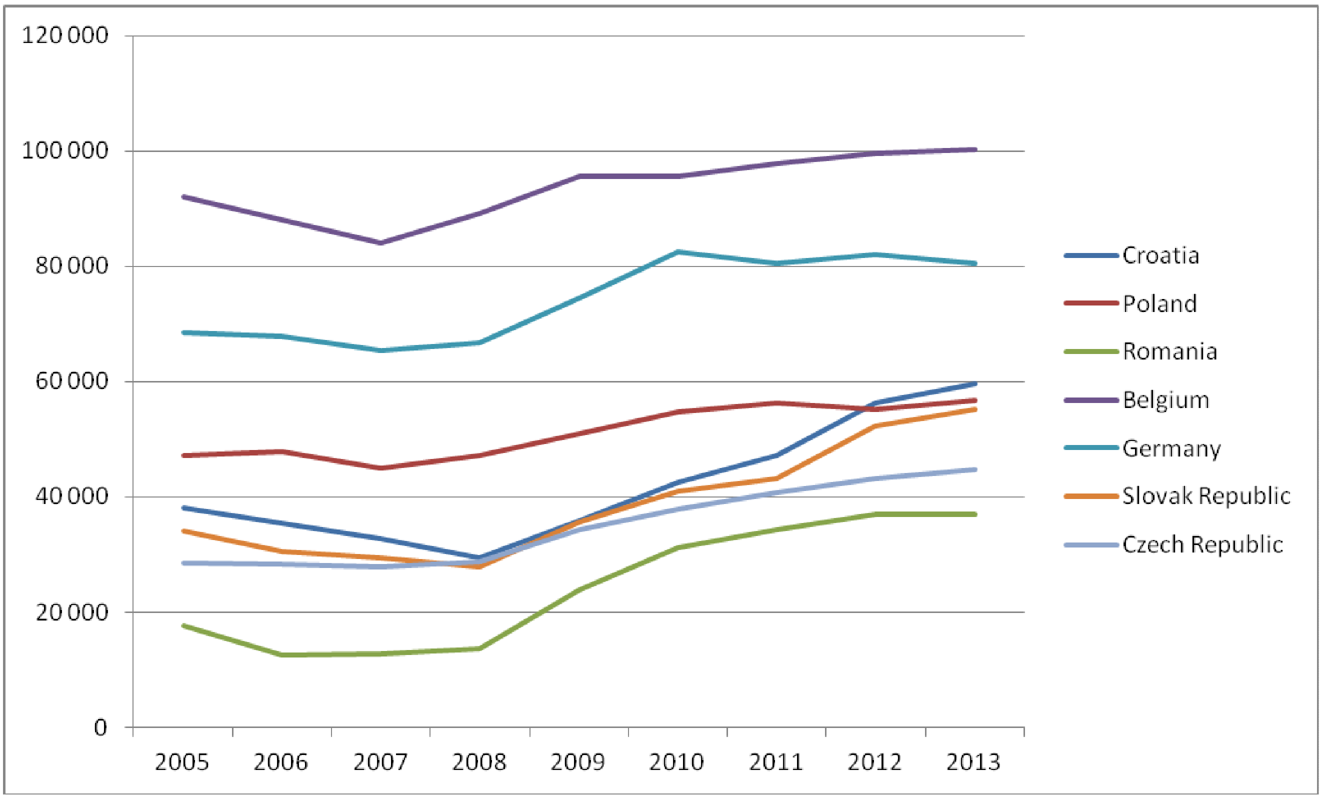
Unlike almost all EU members, Croatian GDP growth never recovered between the first dip of 2009 and the second dip of 2012. Each year was a further contraction. Real GDP growth in Croatia was a relatively decent 5,06% in 2007, which slowed to a 2,08% in 2008, only to contract at -6,95% in 2009, -2,27 in 2010, -0,05% in 2011 and an estimated -1,98% in 2012. The current projections (April 2013) do not show a positive GDP growth until 2014. (IMF, WEO April 2013). Thus, the average growth rate for 2008-2012 was -1,83%

To summarize, measured as average real growth rates of 2008-2012, Poland weathered the recession the best at 3,4%. Average growth in Slovakia was also decent at 2,09%, while Germany was somewhat slower, for all its size and strength, at 1,18%. Romania and Czech Republic were approaching growth neutrality at 0,42% and 0,34% respectively, while Croatia contracted at a devastating average of -1,83%.

<u>Fiscal response</u>

2009 was a shock to the age old mainstream wisdom of preserving stable macroeconomic environment and dealing with crises on a strictly monetary basis (the “Great Moderation”). The prevailing old prescriptions did not work and focus was suddenly on the role of fiscal policy in fighting falling growth and rising unemployment levels. It seemed the 40 year old “new classical” mainstream has shifted, and some dubbed this a Keynesian resurgence[2]. Most developed countries responded to the crisis with a stimulus package (counter-cyclical expansionary fiscal policy). The trade off here was a stimulus of aggregate demand by public spending (accompanied by falling unemployment and rising GDP levels) purchased by higher budget deficits and more public debt. In 2010 there was another shift away from fiscal expansion (Krugman, 2012). OECD and the European Commission started stressing a need for austerity measures as a priority with new vigor. Once more, growth and employment were sidetracked by concerns of lowering public debt levels. In assessing the sustainability of public finances, the European Commission seems to favor the benchmark of public debt to GDP ratio at a 60% level. This methodology might be severely flawed in a recession. As previously mentioned, growth rates in the past years were quite different in various countries; a persistent contraction in Croatia means the ratio of public debt to GDP would increase even if debt itself remained equal. On the other hand, high GDP growth rates in Poland mean public debt/GDP levels would remain the same even if growing steadily[3]. The graph below shows the movement of debt/GDP levels 2005-2013.

[2] i.e. a return of the older 1930-ies to 1970-ies political-economic mainstream
[3] as long as its growth rate did not exceed the growth rate of GDP




source: IMF, WEO April 2013. The data for 2013 for all countries and 2012 for Croatia, Belgium and Czech Republic are estimates

The first thing to observe is that the only two countries whose ratio of public debt/GDP does not remain within Maastricht criteria[4] (60%) are Germany and Belgium at 82% and 99,6% respectively. This is expected of large and developed economies, i.e. "old democracies" (often these levels will inflate during recessions and wars). The four countries with a recent transition past, i.e. "new democracies" remain within the 60% limit which mirrors the relatively good public debt position of most post-socialist countries. In 2012 these levels were at an estimated 56% for Croatia and 43.2% for Czech Republic, and a calculated 55.2% for Poland, 52.3% for Slovakia and 37% for Romania (IMF, WEO April 2013).

Even the behavior of budgetary deficits might make for a poor comparison as falling GDP suggests falling government revenue. A rising deficit might reflect cuts in government expenditure disguised by a more rapid contraction in expenditure. An attempt to gauge austerity by contrasting growth and deficit behavior shows that of these seven countries[5] Belgium was the only fiscally countercyclical (in the 2006-

[4] And by extension, the Fiscal Compact and ESM.
[5] The seven countries are here mentioned by order of austerity from lesser to higher

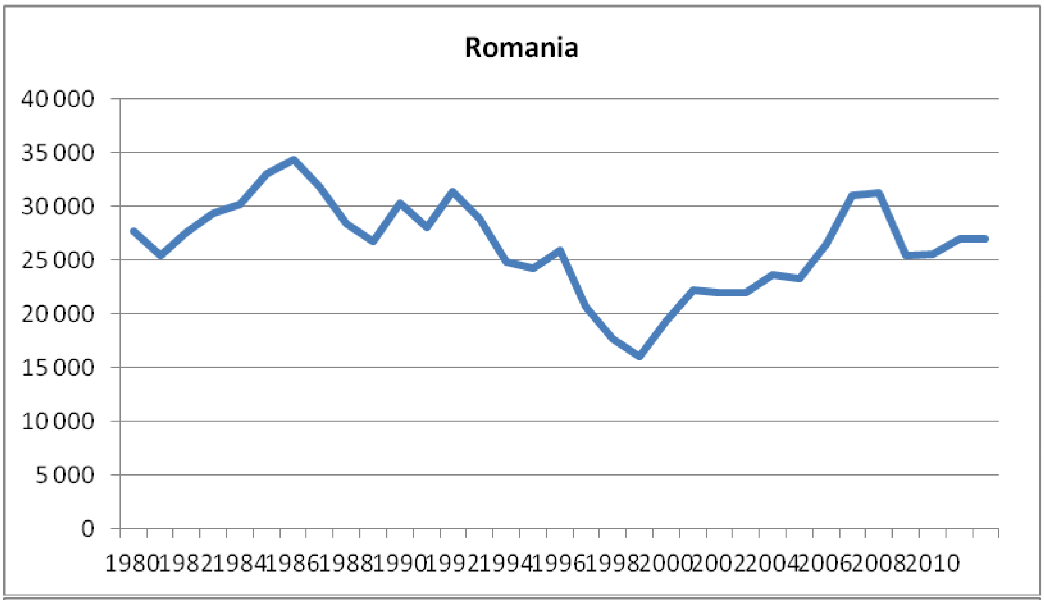
2012 period). Slovakia and Poland were only moderately pro-cyclical (contractionary), Romania and Germany were very pro-cyclical, while Croatia and Czech Republic displayed extremely pro-cyclical and contractionary fiscal policy (Lučev, forthcoming).

Monetary response

In accordance with the prevailing political-economic mainstream, there was a widespread belief that cutting key central bank rates would be sufficient to resolve crises and revitalize the economy[6]. Logically, this was a widespread response of central banks. For Germany, Slovakia and Belgium such a move is the responsibility of the European Central Bank. The ECB cut the nominal rate (marginal lending facility) from 5,25% in mid 2008 to 1,75% in mid 2009. In response to a partial recovery of 2010/11 the rate was slightly raised to 2,25% by July 2011, only to be cut again to 1% in May 2013 (ECB). The Romanian nominal policy rate was cut from 10,25% in the beginning of 2009 to 4,5% in August 2013 (BNRO). In Croatia the Lombard rate was kept at 9% 2008-2010 and cut in 2011 to 6,25% (HNB, 2013). In the Czech Republic the Lombard rates were progressively cut from 4,75% in February 2008 to 0,25% in November 2012 (CNB). In Poland it was cut from 7.5% in 2008 to 5% in mid 2009, raised again in early 2011 to 6% (and 6,25% in mid 2012) and dropped in response to a new slowdown to 4% in July 2013 (PNB).

A cut in key rates was a general response of central banks to the 2009 contraction. The Croatian central bank was the only truly sluggish responder with a late cut in rates (only in 2011). Still, it soon became globally apparent that general rate-cutting would not be sufficient to resolve the recession and return to the previous state of high growth rates. Below are graphs of investment for each country.

[6] These are the rates at which comercial banks can take overnight loans at the central bank (Lombard rates). It is assumed that the movement of these rates has an effect on movements of rates on the private market. A lower rate for a private entity (a firm) means cheaper investment money and ultimately higher profit rates. Cutting the key rates of a central bank in therefore an inticement to investment accross the whole economy.


Romania
40 000
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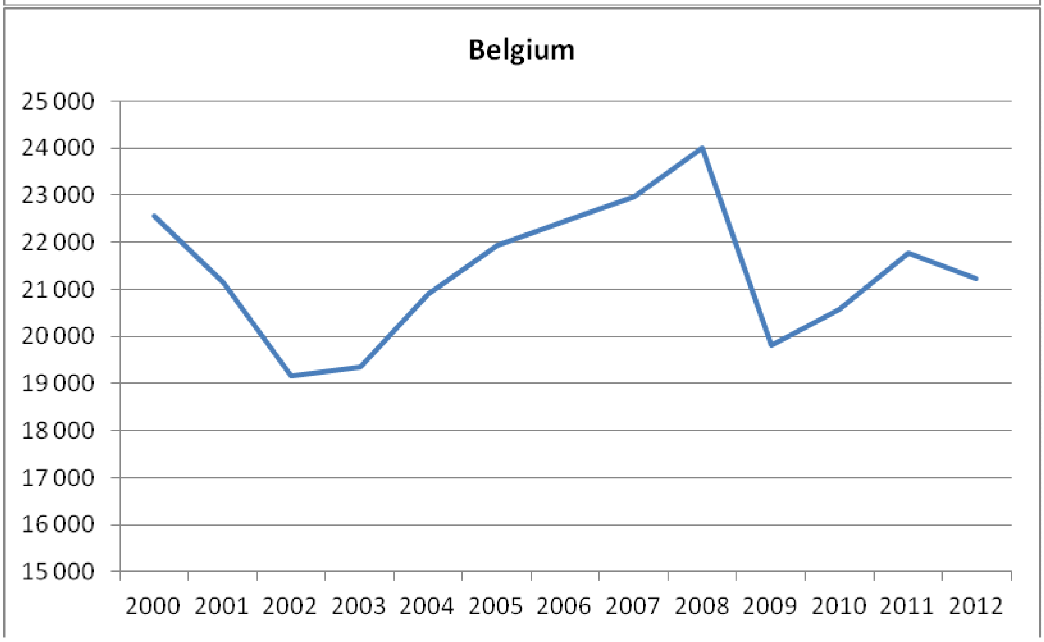
1980 1982 1984 1986 1988 1990 1992 1994 1996 1998 2000 2002 2004 2006 2008 2010


Belgium
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Germany
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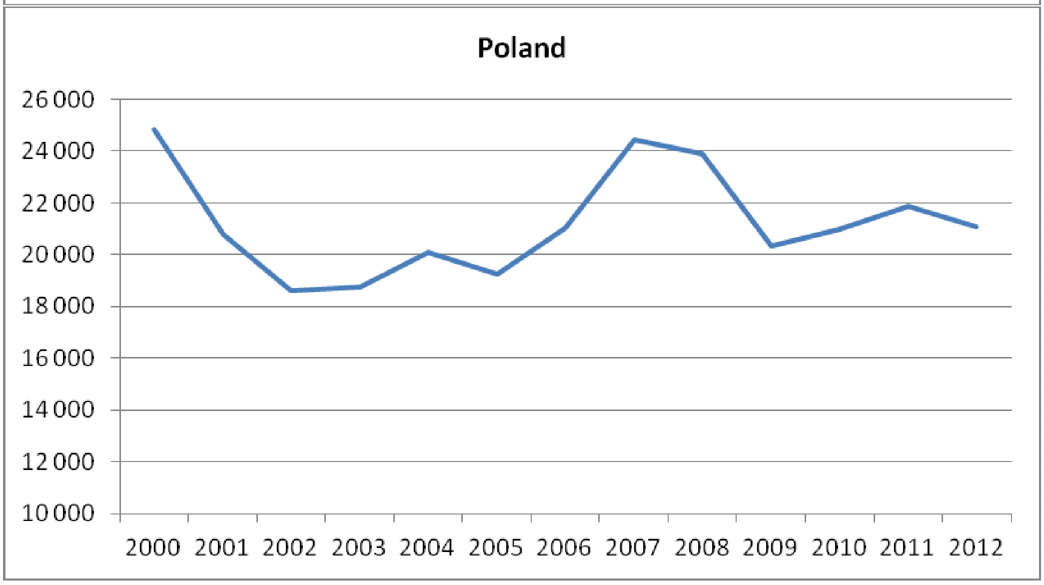
2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012


Poland
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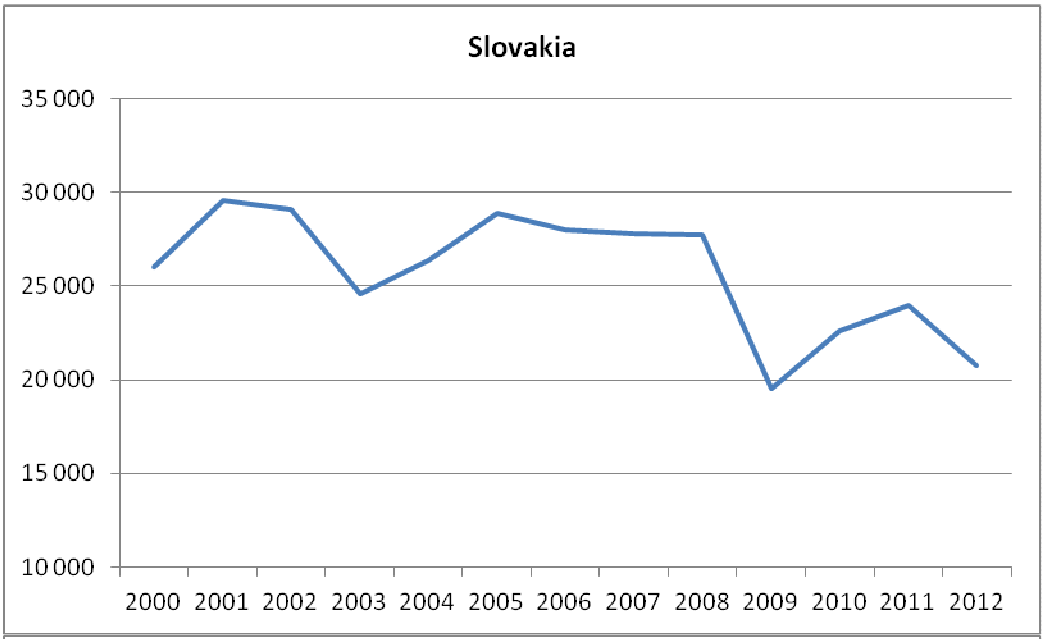
Slovakia
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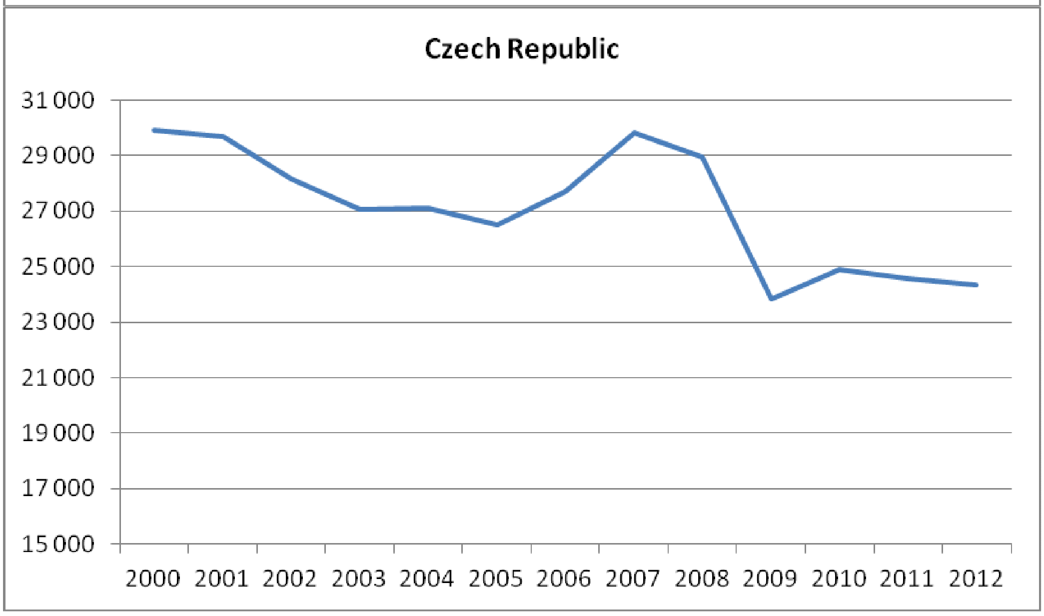
Czech Republic
31 000
29 000
27 000
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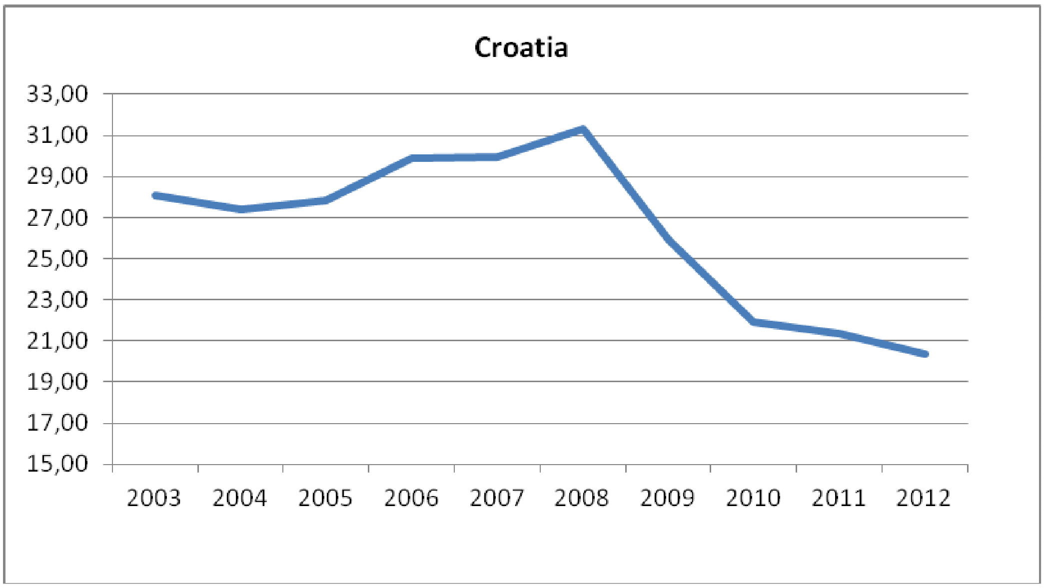
21 000
19 000
17 000
15 000
2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012




Total investment as a percentage of GDP, source: IMF, WEO April 2013

The graphs show highest pre-crisis overall investment levels in Croatia, Romania and the Czech Republic, slightly lower in Slovakia, even lower in Poland and Belgium and relatively low in Germany (not unusual for a country as developed as Germany). Investment in Germany, Belgium, Slovakia and Poland show signs of a slow relative recovery until 2011 and a new decrease in 2012. Investment in Romania and the Czech Republic show tendencies of stabilization on a lower level, while investment in Croatia kept falling until 2012.

<u>Exchange rate and net exports</u>

In recent years comparisons were made likening the effect of Euro in the 2008/09 crisis and the gold standard in the Great Depression of the early 1930-ies (e.g. Eichengreen and Temin, 2010). Both of those regimes disable a countries ability to intervene via exchange rate policy to a deteriorated aggregate demand. Countries with a central position benefit from a stable exchange rate arrangement, while periphery position countries lose an important maneuvering capability. How can we discern the relative position of the seven countries? A broad measure of trade balances is the current account balance (as reported by the MMF) measuring the net export of both goods and services. Looking at this measure as a percentage of GDP in 2007 we can get a clear view of their pre-crisis trade positions. A central position of Germany can be discerned with a trade surplus of 7,45%, as well as a slightly worse, but still net quite positive position of Belgium with a Current Account positive balance of 1,89%. All of the other countries displayed show a negative trade position (in order of deterioration): Czech Republic (-4,39%), Slovakia (-5,27%), Poland (-6,23%), Croatia (-7,26%) and Romania (-13,43%). Off course, Belgium, Germany and Slovakia are Eurozone members[7]. The other four countries had an ability to devaluate their currency against the Euro to improve their trade position. The table below shows the average positions of their currencies against the Euro for each year. It is clearly visible that two of the four countries chose to devaluate substantially in response to the crisis (highlighted in yellow); Poland depreciating the Zloty for 23,22% and Romania depreciating the Leu for 15,13%.

| CURRENCY/TIME | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|---|
| Romanian leu | 3,6209 | 3,5258 | 3,3353 | 3,6826 | 4,2399 | 4,2122 | 4,2391 | 4,4593 |
| Polish zloty | 4,0230 | 3,8959 | 3,7837 | 3,5121 | 4,3276 | 3,9947 | 4,1206 | 4,1847 |
| Croatian kuna | 7,40080 | 7,32470 | 7,33760 | 7,22390 | 7,34000 | 7,28910 | 7,43900 | 7,52170 |
| Czech koruna | 29,782 | 28,342 | 27,766 | 24,946 | 26,435 | 25,284 | 24,590 | 25,149 |

source: Eurostat

In sharp contrast with this, the other two countries depreciated only slightly, preferring the stability to an export boost; Croatian Kuna depreciated for 1,6%, while the Czech Koruna depreciated for 6%, which meant that the average exchange rate in 2009 was still stronger than the 2005-2007 period and only a depreciation when compared to the unusually strong 2008 exchange rates. This suggests that the Czech trade position *via* exchange rates was actually more or less continuously worsened in the 2005-2012 period. In the case of Croatia the Kuna-Euro stability was necessary due to a high level of credit "eurisation"[8] of over 70% in 2009 (Radošević, 2012). Under these conditions, depreciation to Euro would automatically reduce profit rates and disposable income levels of most indebted parties, which would have offset any gains in the trade position.

[7] While Slovakia was a Euro member since 1.1. 2009, it was a participant in the ERMII since late 2005. During this time it not only held a strong exchanged rate against the Euro, but also negotiated a harder, revalued exchange rate repeatedly.
[8] i.e. credits denominated in Euro rather than in Kuna

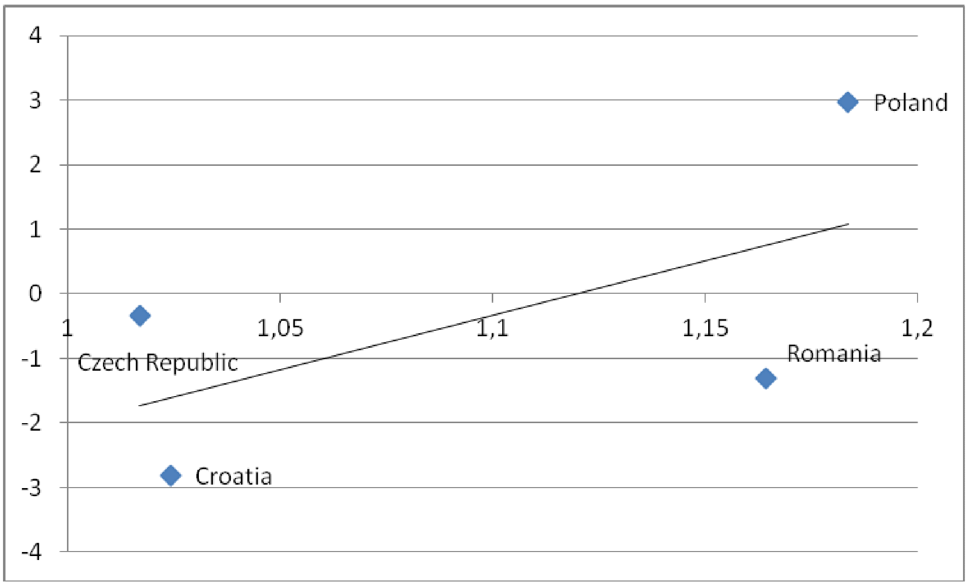
In the following table the success of these moves can be viewed. The two devaluating countries (Romania and Poland) both show improvements in trade positions in 2009 compared to 2008.

| Country | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|---|
| Croatia | -5.271 | -6.679 | -7.263 | -8.957 | -5.121 | -1.063 | -0.985 | -0.142 |
| Czech Republic | -0.930 | -2.109 | -4.394 | -2.121 | -2.459 | -3.821 | -2.924 | -2.704 |
| Poland | -2.382 | -3.848 | -6.231 | -6.603 | -3.981 | -5.115 | -4.868 | -3.568 |
| Romania | -8.646 | -10.389 | -13.426 | -11.635 | -4.163 | -4.422 | -4.524 | -3.822 |

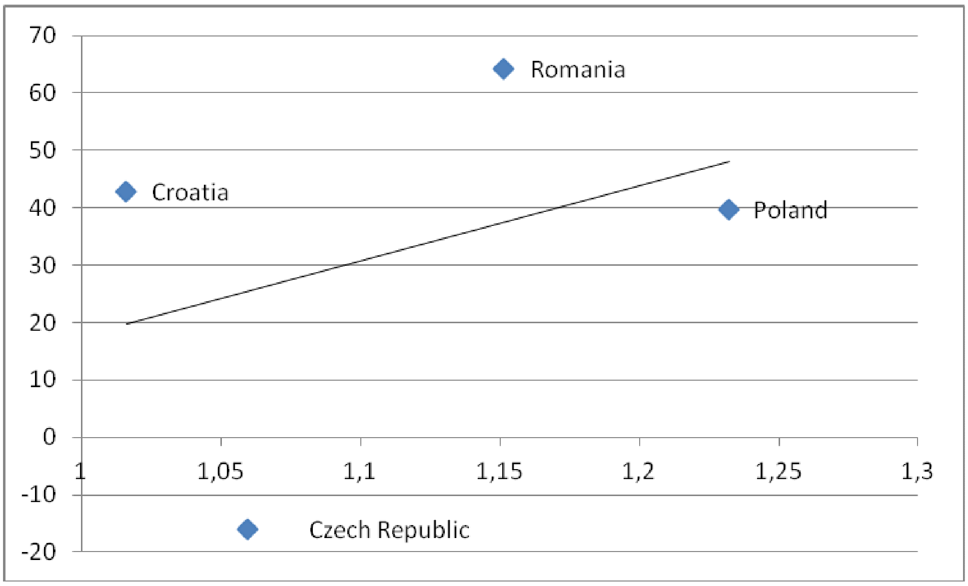
source: IMF, WEO, April 2013. The data for 2012 for Romania, Belgium, Croatia and the Czech Republic are IMF estimates

The current account balance as a percentage of GDP index rose by 64,22% in Romania and 39,71% in Poland, it can therefore be surmised the devaluation was successful. The Czech Republic balance of trade index predictably deteriorated by 15,94%. The Croatian trade position, however, improved in the years following 2008., including 2009. Croatian current accounts differ from the other three countries' in the large effect of tourism (entering the calculation as a service export) which did not deteriorate as much as the trade of goods. The private consumption in Croatia was also hit quite hard in 2009; falling by 7,6%, (HNB, 2013) reflected largely in smaller imports[9] and correcting the trade balance. The following two graphs show the changes in exchange rates vs. real GDP growth (graph 1) and vs. current accounts (graph 2) in 2009. To summarize, the trade position of three of the four countries outside the Eurozone performed in relation to its exchange rate position. This is an instrument irrevocably lost with Eurozone membership.

[9] this is admittedly generally true for any country entering a recession




Average exchange rates 2009-2012 shown against average real GDP growth rates 2009-2012
source: Eurostat (exchange rates), IMF (real GDP growth), own calculation.




Change in average exchange rates 2009/2008 shown against improvement in trade position that year
source:Eurostat (exchange rates), IMF (current accounts), own calculation.

## Institutional reforms and the labour market

The table below shows unemployment rate movements 2006-2012. In contrast with Common Law countries where unemployment rates doubled or even tripled in response to contractions (in one or two years), the response of all seven countries was moderate. Unemployment was actualy substantially reduced in Germany (10,2% in 2006 and 5,5% in 2012) and Poland (13,8 in 2006 and 10,3% in 2012) and noticably reduced in Belgium (8,3% to 7,3%). The levels are comparable in Romania (7,3% to 7%), Czech Republic (7,1% to 7%) and Slovakia (13,5% to 14%). It is only in Croatia that unemployment rose slowly but surely (11,1% to 15%) with no end in sight.

| Country | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | Estimates After |
|---|---|---|---|---|---|---|---|---|
| Croatia | 11.124 | 9.412 | 8.273 | 9.052 | 12.213 | 13.681 | 15.000 | 2011 |
| Poland | 13.840 | 9.602 | 7.118 | 8.166 | 9.637 | 9.631 | 10.347 | 2012 |
| Romania | 7.270 | 6.413 | 5.788 | 6.859 | 7.277 | 7.400 | 7.000 | 2011 |
| Belgium | 8.267 | 7.467 | 7.017 | 7.892 | 8.283 | 7.175 | 7.342 | 2012 |
| Germany | 10.192 | 8.783 | 7.600 | 7.742 | 7.058 | 5.950 | 5.458 | 2012 |
| Slovak Republic | 13.467 | 11.233 | 9.575 | 12.117 | 14.492 | 13.608 | 14.000 | 2012 |
| Czech Republic | 7.148 | 5.320 | 4.392 | 6.662 | 7.279 | 6.700 | 7.027 | 2010 |

source: IMF, WEO April 2013

The rapidity of reaction of the unemployment rate is determined by labor market flexibility. While the success (and thus usefulness) of this institutional arangement was mainly determined by a wider set of institutional options (see Hall and Soskice, 2001; Hall and Gingerich, 2004; Hancké et al , 2007), there is now an imperative pressure towards greater flexibilisation in EU. There is an entirely logical progression of the european project to be considered here. When monetary policy does not suffice to resolve a recession (as it did not in 2009), what tools remain available for an EU or Eurozone member? If expansionary fiscal policy in the EU is disabled by the Fiscal Compact and exchange rate policy is disabled by Euro or ERMII[10] membership, it leaves very little short-term possibilities. Both general growth recovery and trade balances are then mostly left to the private market. From the viewpoint of central and eastern europe this is a true, if pointless, conclusion of the transition processess of the past two and a half decades. Market triumphant in exchange (where manuevering is already constricted by the single market) means that starting productivity levels/competitiveness in exchange perpetuate themselves and yield progressively greater results. One of the only possible and desirable interventions becomes lowering factor costs, i.e. real wages (as in the Euro+ pact). This will effectively produce positive trade balance changes at the price of lower standards of living for workers producing the goods traded. On the other hand, the only possible solution for high unemployment levels becomes greater flexibilisation of labor markets, making both lay-offs and new employments easier for employers. The alternative approach to reducing unemployment would have been the very expansionary policies lost in the many european processes as described above. The only remaining instrument improving growth rates under the presumption of sole acceptability of market-solutions is improving the investment possibilities on the private market. These two preferences (investment incentives and labor flexibilization) are reflected in many reform projects in the seven countries.

Labor flexibilization can be measured by aggregate indices such as the Heritage Labor index (see also Lučev and Babić, 2013). It gauges ratio of minimum wage to the average value added per worker, hindrance to hiring additional workers, rigidity of hours, difficulty of firing redundant employees, legally mandated notice period, and mandatory severance pay (Heritage). Comparing the relative positions of 2007 and 2013 indices it is visible that only Czech Republic of the seven countries made a substantial change in labor market regulation. The Czech labor liberalization will surely make itself felt in the years to come (with a reduced unemployment rate),

[10] Exchange Rate Mechanism is obligatory for any Eurozone aspirant. It constricts the movement of currencies against the Euro.

but will also mean the next recession will most probably result in a far quicker unemployment growth.

## Summary

Germany, Belgium and Slovakia as Eurozone members do not have monetary (key rates) and exchange rate modification possibilities. Still, the ECB monetary response was quick and decisive (although hampered by low inflation rate target; see Blanchard et al, 2010). Even though the Belgian fiscal response was far less austerity based, particularly when compared to expected reactions to GDP movement, Germany achieved somewhat better average growth rates and Slovakia recovered very quickly. Croatian policy was the most pro-cyclical and therefore conducive to dire growth results: monetary response was very slow and modest, echange rate remained fixed to Euro, and there is evidence to suggest Croatian fiscal policy was one of the least active ones in Europe. This much is also true for the Czech Republic. In addition it kept the Koruna-Euro exchange rate relatively fixed and detrimental to its trade, but the monetary response was prompt and adequate, and its overall growth acceptable, if unremarkable. In contrast, Poland and Romania pursued relatively expansive counter-cyclical policies. Romania was forced to request a *balance-of-payments* bail-out[11] in late 2008. The result was an unavoidable deficit cut regardless of GDP movements. It was, however, able to depreciate its curency against the Euro as well as cut interest rates in time and its average growth rates are comparable to those of Belgium and the Czech Republic. On the other hand, Poland managed to react expansivelly on all fronts. It devalued the currency against the Euro by 23%, followed a reasonable fiscal policy and cut key rates quickly, even if a little cautiously and its average growth outstripped the rest six countries by far.

If there is one central lesson to be learned from the past few years, it it that business cycles are real. Even as we climb out of the abbys of this particular recession, it is useful to keep in mind that this is not a unique event. Crises and recessions are an unavoidable human experience. In the following years each of the seven countries will at some point have to deal with a similar, if smaller and more localized occurance. In the meantime the monetary and fiscal european union might

[11] backed by the EC, EIB, IMF, EBRD and the World Bank

be completed as a project. This will mean that all of the described policies that Poland pursued in 2009 might become impossible during the next contraction. There will be no exchange rate policy (due to a common currency), monetary affairs will largely become the responsibility of the European Central Bank and fiscal policy will be constricted by the Fiscal Compact. In such circumstances, it is conceivable that the only two options available to Poland could be the economic performance of Czech Republic in the best case[12] or the economic performance of Croatia in the worst case.

## Appendix – interviews with politicians

During the course of the summer school several Sejm and Senat members were interviewed by members of the national level group; Michał Jaros, a Sejm representative of the government party Platforma Obywatelska; Wincenty Elsner, a Sejm representative of Ruch Palikota and Jarosław Obremski, an independent member of the Polish Senat. It was hoped their various positions would allow for a diverse sample of opinions, and some of their statements do have a direct bearing on this report. It would appear the three politicians support a Polish currency as a necessity in crises. This is interesting, as Poland is obliged by its Treaty of Accession to eventually enter the Eurozone. While there was a consensus on the need for a Fiscal Compact, there were, somewhat paradoxically, dissenting opinions on the need for austerity measures in Poland. Both Jarosław Obremski and Wincenty Elsner expressed disagreement with further austerity. This is also interesting as Poland is still struggling to meet the deficit criteria of 3% GDP requested by the European Commission. To stop reducing the deficit would mean to counter the efforts of 2010-2013 in the opposite, anti-cyclical direction and directly contradict the Fiscal Compact.

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BNRO – National Bank of Romania (www.bnro.ro) [30.7.2013]

[12] and in the case of an adequate ECB response

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# EU LEVEL

## Final Report of the EU Level Group

## *The EU's Approach to the Crisis: Old Measures and More Austerity*

## Genesis of the Crisis - Some are Just Too Big to Fail

The financial crisis of 2007–2008 appears to have been the most severe since the Great Depression of the 1930s, with some of the world's best-known financial institutions collapsing or having to be nationalized, while many others survived only through massive state-funded direct support.[13] As the free enterprise has been hailed in the past decades as always being the best available option, this crisis has shown that one of the mainstream model's deficits is taking into account the human element, or more specifically, the complexity of non-rational human behavior.[14] Culturalists' and structuralists' age old opposition to the rationalist approach appears to be finding its way again to the center of today's main debates.

Within the European Union, the financial crisis started as a banking system crisis due to liquidity problems, involving both public and important private financial institutions such as Fortis, ING or ABN AMRO. In most cases, the national response was to design policies aimed at the bailout of the banks using taxpayers' money. Governments regarded many of the institutions that reached the point of bankruptcy as being to be "too big to fail" (TBTF) given that they were so interconnected with the rest of the financial system that the end cost of allowing them to fail was judged to be too high. In the absence of any other available options, governments themselves recapitalised these TBTF entities – using taxpayers' funds.[15] In return, this situation created the impossibility for some countries within the Eurozone to repay or re-finance their government debt without the assistance of third parties, creating a sovereign debt crisis out of the so-called "*dance of death*"[16] practiced between sovereigns and banks. In states like Ireland and Spain banks brought sovereigns to their knees while in Greece and Italy the weakness of the state was the one that cost the banks dearly. This idea of treating banks as too big to fail is not new, and neither are the challenges that such institutions pose for policymakers

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[13] Eric Helleiner; *Understanding the 2007–2008 Global Financial Crisis: Lessons for Scholars of International Political Economy*; Annual Review of Political Science; 2011; No. 14; pp. 67–87; First published online as a Review in Advance on January 20, 2011

[14] Andrew W. Lo cited in Cate Reavis, *The Global Financial Crisis of 2008: The Role of Greed, Fear, and Oligarchs*; MIT Sloan School of Management – Learning Edge online publishing; March, 2012

[15] Paul Melaschenko; Noel Reynolds; *A template for recapitalising too-big-to-fail banks*; BIS Quarterly Review, June 2013; pp. 25 – 39;

[16] Sonny Kapoor; Charles Goodhart; *Europe's dance of death between sovereigns and banks*; RE-Define Institute; first published on http://www.re-define.org/node/114#sthash.ZvR26xPh.dpuf

around the world. The last century has witnessed a considerable proliferation of policies meant to establish mechanisms and agencies to oversee banking systems. However proliferation and effectiveness do not go hand in hand in this case as both the US and European policy makers have failed in their attempts. Just how big are these TBTF institutions? In the fourth quarter of 2011, the official statistics showed the assets of the world's 50 largest banks (located in 16 countries which account for 74 % of the world's GDP) to equal 70 % of total bank assets, and seven of these institution's assets exceed 100 % of the GDP of their home countries. [17]

It must be stressed that, although especially manifesting at the level of the Eurozone, the financial crisis severely affected also the Member States which have not yet adopted the euro as a national currency. Due to the financial predicament, the real economy was strongly affected, with historic decreases of gross domestic product (GDP) and high rates of unemployment throughout the European Union. Most of the governments of the countries affected by the crisis and the recession adopted austerity measures in order to minimise the public expenditure.

At the country level, it is considered that Greece, Ireland, Spain, Portugal and Cyprus were the Eurozone states most affected by the crisis and the subsequent recession. Taken as a whole, the EU has experienced since the autumn of 2008 successive periods of contraction and only minimal growth of economy, largely depending on the performance of major national actors such as Germany, France, United Kingdom, Italy and Spain. Also, differences of growth were measured between EU27 and the Eurozone economy. As an example, Poland is the only Member State managing to avoid recession. On the other hand, Hungary, Romania and Bulgaria as well as the Baltic states experienced economic hardships despite very high differences between their public debts.

Although treating some large banks as TBTF may appear at first to mitigate the systemic risk posed by the interconnectivity of the state's economy with the banks' activities, one must not lose sight of the TBTF's *dark side* that is moral hazard.[18] This represents the tendency for insurance to encourage risk-taking. A government guarantee that protects a bank's creditors from loss enables may actually be the best encouragement for greater risk-taking, a behavior that lay at the foundation of today's crisis

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[17] James R. Barth, Apanard (Penny) Prabha, Phillip Swagel; Just how big is the too big to fail problem?; Milken Institute Publishings; March 2012; published online at http://www.milkeninstitute.org/pdf/TBTF.pdf
[18] David C. Wheelock; *Too Big To Fail: The Pros and Cons of Breaking Up Big Bank*s; Regional Economist; No. 10/2012, October 2012 (http://law-journals-books.vlex.com/vid/big-fail-pros-cons-breaking-banks-413899610)

## EU's Focus on Austerity and Its Attitude to Germany's Fear

The development of EU policy regarding the economic crisis in the past two years has been considered at times not to be the outcome of the highly publicized speech about stronger integration, collaboration and collective compromise among the member states, but rather the application of the "*German approach based on austerity and price stability at the expense* (some might say) *of economic growth*".[19] With the IMF admitting in June of 2013 that its handling of Greece's situation through severe austerity measures was not the best available option, the question of austerity as the best solution for the countries' sovereign debt crisis has once again been taking the center stage in the debate on the efficiency with which the EU is managing its economic crisis, especially with regards to the requirements imposed by the ESM. Following the decades old tendency of overly-optimistic forecasting, the IMF's admission that it might have been too optimistic in the recovery expectations and also that it might have miscalculated the effects of the spending cuts appear to be in sharp contrast to the EU's continuing praise of austerity as a way of boosting the economy.

After the Greek program was approved, the country was required to immediately cut some of its debt and implement structural reforms, but it seems that from the economic perspective of the main institutional lender, these reforms were "notable failures" as they were unsuccessful in restoring the confidence of investors plunged the state into the worst peace-time recessions the country has witnessed so far, with output falling 22% from 2008 to 2012[20]. One might wonder why, after last year the Fund admitted that government spending cuts may hurt growth more than it had previously thought and that countries should postpone deep spending cuts while their economies remain wobbly, the EU is still pushing forward with considerable emphasis for harsher austerity measures? The austerity packages imposed on Italy and Ireland have also been raising questions of effectiveness. So why do the MS continue down this path and why does Germany insist on it?

One answer that is given constantly is Germany's historical fear of hyperinflation due to the experience of the Weimar Republic, on the one hand, and the simple national interest of a country that has not felt the dire effect of the crisis on

[19] Sebastian Dullien and Ulrike Guérot; The long shadow of ordoliberalism: Germany's approach to the euro crisis; European Council on Foreign Relations – Policy Brief; ECFR, Issue no. 48; February 2012

[20] "*IMF says 'sorry' for Greek crisis handling, EU Commission in denial*"; published on 6th of June 2013 at http://www.euractiv.com/euro-finance/imf-sorry-greek-crisis-handling-news-528355

the other hand. But to this one might add the structure of the ideological edifice behind German economic orthodoxy that has shaped the debate in the country in a specific manner that is by no means characteristic for other countries of the EU, especially the newcomers who joined the EU in 2004. According to Sebastian Dullien and Ulrike Guerot, *the intellectual tradition of the theory of ordoliberalism underlies Germany's approach to the euro crisis* [(…) framing] *a position that contrasts with the Anglo-Saxon debate that predominates international institutions such as the International Monetary Fund (IMF).*[21]

The pillars of this theory reside in the belief that quick and decisive budget consolidation can be achieved by reducing public expenditure and increasing taxes. Hence less government spending today mean less taxation in the future and more investment, while harsh austerity measures are considered to improve the outlook for growth and have no significant negative economic effects.[22] Also in this line of thought elaborated by such economists as Walter Eucken and Franz Böhm, bailouts are regarded as the last-resort necessary evil, "*as they seemed to risk affecting the incentives faced by governments in profligate countries and make overspending possible*"[23]. Obviously, German economists do not share identical beliefs as one can witness a debate between the ordoliberal tradition, that has influenced the thinking of all five main political parties in Germany, and the alternative New Keynesian thinking that has some influence on the opposition parties. But even so, the basic German approach and fixation on authority is unlikely to be quickly reformed, as "*the mainstream neo-classical belief in the need for stricter fiscal rules is shared by the Social Democrats and also has strong support inside the Green party*."[24]

While the ordoliberal tradition may explain the Germany's push for austerity, why was this perspective adopted at the European level? The embracing of austerity can be understood better in a political context. As Philip Arestis and Theodore Pelagidis argue, *European politicians have proven to be incapable of directing stimulus toward productive public investment, and of fostering demand,* [while] *the public continues to reject tax increases to cover the future deficits that today's stimulus would create*[25]. Embarking on austerity increases the risk of negative growth of the gross domestic

[21] Sebastian Dullien and Ulrike Guérot; The long shadow of ordoliberalism: Germany's approach to the euro crisis; European Council on Foreign Relations – Policy Brief; ECFR, Issue no. 48; February 2012
[22] Idem 9
[23] Idem 9
[24] Idem 9
[25] Philip Arestis and Theodore Pelagidis; The case against deficit hawks – Absurd austerity policies in Europe; Challenge, vol. 53, no. 6, November/December 2010, pp. 54–61

product, sovereign default and political instability, outcomes that make bank failures more likely[26]. In this same line of thought, considerable emphasis has been put on the need for liberalization and privatization, with Italy approving new liberalization programs in 2011 and Portugal privatized the remainder of the national electricity provider, EDP, with plans to do the same in regards to its national water utilities, air carrier, and postal service.[27] However, if this will lead to a cost / price reductions and so to an increase in external competitiveness is not actually clear, just as cutting salaries might not improve competitiveness by reducing unit labour costs, and increasing export growth, but actually reduce growth in internal aggregate demand and thus reduce GDP growth.[28]

The popular discourse of the opposition parties throughout the EU has focused on picturing the banks as the ones mainly responsible for the crisis situation, and austerity measures imposed upon the people as a savage way of paying for bankers' recklessness. According to Dr. Pacześniak, although there is a common opinion that banks are responsible for the crisis as such and that European institutions and the Member States must pay for their mistakes, there appears to be no agreement in the European Union on the question of who should pay for banks' mistakes and for wrong decisions made earlier[29]. Nevertheless:

> *"There is a big difference between the situation in 2008 and the one in 2013. In 2008, the first reaction to the crisis was to give some public aid to the private companies. The recent discussions about the Banking Union should introduce a different perception, that not the whole society is financially responsible for banks' mistakes, but rather the customers of those banks, but also the institutions that were customers of those banks. There is much more public aid given in Europe than in the United States, but on the other hand, there is a political disagreement between technocrats and the common perception, the society. In the European Parliament, the German Socialists are more willing to improve the social policy of the European Union and this political way of action is against financing private banks by public resources."*[30]

[26] Sebastian Dullien and Ulrike Guérot; The long shadow of ordoliberalism: Germany's approach to the euro crisis; European Council on Foreign Relations – Policy Brief; ECFR, Issue no. 48; February 2012
[27] Corrado Andini, Ricardo Cabral; *Further Austerity and Wage Cuts Will Worsen the Euro Crisis*; IZA Policy Paper No. 37; February 2012; p.03
[28] Corrado Andini, Ricardo Cabral; *Further Austerity and Wage Cuts Will Worsen the Euro Crisis*; IZA Policy Paper No. 37; February 2012; p.08
[29] Interview with Dr. Pacześniak of the University of Wroclaw, taken on the 4th of June 2013; transcripts available in the appendix
[30] Interview with Dr. Pacześniak of the University of Wroclaw, taken on the 4th of June 2013; transcripts available in the appendix

One opinion that benefits from a largely shared consensus, apart from the idea of austerity being an improper mechanism of dealing with the crisis, is that the EU should start focusing more on socially oriented policies. The unemployment rates are becoming a major concern for Southern states and given that the last European summit was concerned with youth unemployment, it would appear that the EU is at least aware of this problem.

> *"Nevertheless, the MEPs are more concerned with discursive and populist questions, like how to speak about Europe, in the context of next year`s elections than with the real problems and the populist parties will point out that the mainstream in Europe is not able to solve the problem of youth unemployment."*[31]

## The EU's Political Answers to the Economic Problems

The EU's main reactions to the economic and financial crises have been aimed at salvaging Europe's prosperity from the spillover of the American financial crisis, focusing on the elaboration of a coordinated response to the crisis. Since 2008, the EU has proposed and adopted a series of measures aimed officially at restructuring the current system, in order to allow the fixing of current problems and eliminate the possibility of a similar situation arising in the future. At the discursive level emphasis was put on re-establishing the confidence of the people, raising demand, and underlining the importance of investments that are supposed to bring long-lasting and stable prosperity.

The initial coping strategy for dealing with the effects of the crisis was summed into two bills: The European Economic Recovery Plan (COM(2009) 615, 19.11.2009 and the Temporary Framework for State aid measures to support access to finance in the current financial and economic crisis (OJ C 83, 7.4.2009). The European Economic Recovery Plan focused on increasing investments in infrastructure and key sectors such as cars, construction and green technologies. Also, it mobilized funds for improving labor market growth and decreasing unemployment rates. The plan proposed that the Member States co-ordinate national budgetary stimulus packages in the attempt to optimize their impact and avoid negative spill-over effects from one country to another. The total package amounts to around € 200 bn, which represents

[31] Interview with Dr. Pacześniak of the University of Wroclaw, taken on the 4th of June 2013; transcripts available in the appendix

1.5 % of the EU's GDP. On top of that, the EIB increased its annual level of financing by some €15 billion between 2009 and 2011. The Temporary Framework was written in the form of a communication from the Commission and had the purpose of providing Member States with additional instruments for counterbalancing the effects of the financial crisis on the real economy. These instruments were aimed on one side at ensuring companies' access to financing through low interest loans with a State guaranteed maximum sum and on the other side at encouraging companies to invest in sustainable solutions, such as allowing subsidized loans for the development of green products.

However, as time passed and, contrary to the official forecast, the crises deepened, hence calling for a new set of measures to tackle the problems arising more and more frequently. The EU's response to the economic problems of its Member States was to slid onto an unbroken path of austerity. With the crisis spreading to Spain and Italy in 2010 and 2011, it seemed that saving the euro and the Eurozone states from bankruptcy *"would require massive infusions of capital, coordinated national efforts, and international collaboration"*.[32] Among the various recommendations and decisions adopted, three pacts hold the spotlight at the moment in terms of importance: the European Fiscal Pact, the European Economic Stability Mechanism and the proposal for the European Banking Union.

Leaving aside the official discourse of the political sphere, at a close analysis of both the situation in which the EU member states find themselves and the afore-mentioned treaties elaborated in response to the crisis, one cannot help but realize the idiosyncrasy of the EU's response capacities – economic problems have been being tackled through economically inefficient political responses. While many political figures push forward towards deeper integration and institutionalized austerity, the majority of the experts in the field of economics and political science are underlining the inefficiency of the adopted measures and warning the EU against continuing on the current path as this will not lead to economic recovery. The measures underlined in the three afore-mentioned treaties introduce relatively few new elements, many of them having been part of former agreements that were however never truly enforced, or just simply ignored. Moreover, no mechanism has been envisaged so far at a common level that could tackle one of the most important problems – the Member States' propensity for overly optimistic deficit forecasts. Even if the opinion *"that annual deficits and long-term debt can best be held in check*

[32] Karen Fasano Thomsen, *What Measures Did Europe Take to Contain the Crisis*?, University of Iowa Center for International Finance and Development; April 2012.

*through fiscal policy rules or mechanisms such as deficit or debt cap"* is true, the efficiency of these mechanisms "*depends on making accurate forecasts of government spending and revenues*"[33]

Jeffrey A. Frankel and Jesse Schreger have shown that over the last 20 years the EU countries, and especially the Eurozone countries have "*postponed painful adjustment by making overly optimistic forecasts of future growth and budget positions and arguing that the deficits will fall below the cap within a year or two*"[34]. It would seem that there is a strong tendency, to the point of a unanimous constant, for the governments' "*official forecasts of growth rates, tax receipts, and budget balances to be over-optimistic* (…) *especially when they have large contemporaneous budget deficits, and especially during booms*".[35] The Member States have almost never forecasted violations of the 3% imposed ceiling and as this tendency will probably continue. Most likely, the lack of an appropriate mechanism to deal with this issue will curtain the efficiency of the new Fiscal Pact just as it curtained that of the Stability and Growth Pact.

The provisions contained in the Fiscal pact, namely the "Golden Rule", the "1/20 Rule", the imposed 3% [0,5%, and for exceptional situations 1.0%] deficit limit and the 60% of GDP limit on debt are not new elements, the Member States having agreed to abide by them since the signing of the ESM's predecessor, the EFSF. This former pact has already been breached by the two major power players of the union – Germany and France, making for a strong precedent in the eyes of less influential states. A new provision indeed is the capacity of one Member State to bring another in front of the European Court of Justice for violations of the treaty with the Court having the right to impose a fine of up to 0.1% of GDP to the country that is proven to be in breach of the treaty. However, if one looks at what the odds are for such a situation to actually occur, the overall efficiency of the official punitive measures seems considerably flawed. What country, that does not possess Germany's influence, would engage in such a diplomatically risky action? And is fining a state in economic difficulty, with a considerable amount, a rational options, given that the ultimate end is that state's economic recovery?

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[33] Interview with Dr. Klimowicz of the University of Wroclaw, taken on the 3rd of July 2013; transcripts are available in the appendix.
[34] Jeffrey Frankel, Jesse Schreger, *Over-optimistic official forecasts and fiscal rules in the Eurozone*, June 2013, Volume 149, Issue 2, pp 247-272.
[35]Jeffrey Frankel, Jesse Schreger, *Over-optimistic official forecasts and fiscal rules in the Eurozone*, June 2013, Volume 149, Issue 2, pp 247-272.

Given the structural weaknesses and the gaps of the governmental frameworks revealed by the crisis and the EU's weakness against external shock, the European Stability Mechanism was put in place to provide temporary financial support and to ensure the stability of the euro, on the basis of rigid conditionality. While the program is hailed on the political scene as a considerable step towards further integration, its actual economic inefficiency is a matter of strong consensus amongst experts. The reproaches to the program focus both on the size of the program (in revenue terms) and on its actual core, namely the adjustment programs based on austerity measures that condition the funding. As Dr Klimowicz underlined:

> *"Money earns money. You don't need to save it, but rather spend it in order to make it. There is no economic theory that says that austerity is a good thing for individuals, let alone for countries. Greece is quite a good example. The problem was in rating – it was really low, so they couldn't borrow more money from the financial institutions. The purpose of the measures was to show that they were more stable, in order to borrow more money. So, for a short period of time, that could have been a good idea but in a long term perspective, such a strategy in my opinion wouldn't work, neither for the companies, not the citizens, because you need money in order to make money".*[36]

In this regard, the 700 bn Euro budget of the ESM, with its 500 bn lending capacity out of which only 80 bn are actual financial resources, the rest being state insurances, are regarded as completely insufficient for the needs that might have to be met. According to Dr. Pacześniak, although *"from the point of view of Member States such as Poland the sum may seem really huge, for the Eurozone as a whole it might be not sufficient"*[37]. Italy has a 1,5 trillion debt and 502bn of the so-called PIIGS debt is about to mature this year alone, thus just giving money might not prove to be the best option, especially when it comes to injecting capital into private banks. Prof. Klimowicz's summary of the EU's approach is highly insightful:

> *"I think that the idea of the European Union in solving the crisis is to give money, not to give any ideas how to fix things, how to cope with the actual problem. I think that none of the European institutions have an idea about how to cope with the crisis.*

[36] Interview with Dr. Klimowicz of the University of Wroclaw, taken on the 3rd of July 2013; transcripts are available in the appendix.
[37] Interview with Dr. Pacześniak of the University of Wroclaw, taken on the 3rd of July 2013; transcripts are available in the appendix.

> *The only idea is to give money, to survive and maybe eventually find a plan. Giving money to financial institutions, whose purpose is to earn money, is a bad idea."* [38]

Other elements of the treaty, such as the incorporation of the balanced budget requirement into the national constitutions has also been criticized by economists, with Paul Krugman emphasizing that this would be a very unsound policy which would adversely affect the economy.

It would seem in the end that the political sphere's approach to tackling the crisis is not just relatively unproductive, but also unavoidable. "*The ideological differences between EU member states and varying political, economic, and cultural climates still pose major obstacles to potential solutions to the crisis*".[39] Treaties and pacts may be based on economic issues but they have always been a matter of political decisions, and the Fiscal pact and the ESM are no exception.

Some of the questions we might want to ask ourselves are "*whether or not politicians are aware of what they are signing; are they aware if they will be able to fulfill the conditions? Looking at the creation of the Eurozone and taking Greece as an example, economists will tell you that even if you sign an agreement you can cheat. Given that pacts are a political decision, even if there are some countries that are unable to fulfill some of the conditions, solutions will be found to "resolve" these problems. Also, similar norms for all the countries are not a good solution."*[40]

## The Effects of the EU's Crisis Management on Democracy

The issue of the democratic deficit of the EU has arisen as one of the main questions in view of the measures taken to deal with the European crisis as supranational level. The issue of democratic deficit within the European Union refers mainly to the powers of the European Parliament, in the narrow meaning, but originally this concept was much wider. The essence of democratic deficit is expressed in an opinion that *the European Union and its various bodies suffer from a lack of democratic*

[38] Interview with Dr. Klimowicz of the University of Wroclaw, taken on the 3rd of July 2013; transcripts are available in the appendix.

[39] Karen Fasano Thomsen, *What Measures Did Europe Take to Contain the Crisis*?, University of Iowa Center for International Finance and Development; April 2012.

[40] Interview with Dr. Klimowicz of the University of Wroclaw, taken on the 3rd of July 2013; transcripts are available in the appendix.

*accountability and legitimacy, moreover they seem inaccessible to ordinary citizens because their operating method is very complex, opaque and remote.*[41] Taking into consideration the wider approach on democratic deficit, one can recall both the role of the European Parliament and of national parliaments within the European Union as embodiments of representative democracy[42].

The main claims involving the democratic deficit regards the following: *European integration has meant an increase in executive power and a decrease in national parliamentary control* (Andersen and Burns, 1996; Raunio, 1999)[43]. *The actions of the executive agents at the European level are beyond the control of national parliaments and hence governments can effectively ignore their parliaments when making decisions in Brussels.*[44]

According to N. Foster and Martha Zalewska, another issue regarding the so-called democratic deficit "*concerns the division and control of competences between the Union and the Member States, as well as related principles of subsidiarity, proportionality and the principle of conferral*"[45]. Regarding the possible democratic deficit elaborated through the implementation of the fiscal pact and ESM's rules, opinions among experts are divided. If one is to look at the Union only from an economic point of view, as being a strictly an economic zone, then

> "*giving more decision powers to big states would be explainable because they have stronger economies.* [However the] *EU wasn't created this way. It was created as an equal partnership of countries. The current system of representation gives much power to big countries, rich and with stable economies countries – France, Germany and Great Britain. The current representation system is not a good one because in the EU most of the countries are small ones, they are not stable, they are never going to be stable, because the EU is too large, you have a lot of countries and there are* (only) *two or three big countries. So, small countries don't feel represented.*"[46]

[41] Interview with Dr. Pacześniak of the University of Wroclaw, taken on the 3rd of July 2013; transcripts are available in the appendix.

[42] Marta Zalewska, Oskar Josef Gstrein; *National Parliaments and their Role in European Integration: The EU's Democratic Deficit in Times of Economic Hardship and Political Insecurity;* Bruges Political Research Paper; no. 28; 2013

[43] Andreas Follesdal; Simon Hix; *Why There is a Democratic Deficit in the EU: A Response to Majone and Moravcsik;* JCMS 2006 Volume 44. Number 3. pp. 533–562

[44] Andreas Follesdal; Simon Hix; *Why There is a Democratic Deficit in the EU: A Response to Majone and Moravcsik;* JCMS 2006 Volume 44. Number 3. pp. 533–562

[45] N. Foster, cited in Marta Zalewska, Oskar Josef Gstrein; *National Parliaments and their Role in European Integration: The EU's Democratic Deficit in Times of Economic Hardship and Political Insecurity;* Bruges Political Research Paper; no. 28; 2013

[46] Interview with Dr. Klimowicz of the University of Wroclaw, taken on the 4th of June 2013; transcripts available in the appendix

However, given the actual influencing capacity, in political and economic issues, of member states such as France and Germany have been present since the beginning of the whole European integration process, and have been in effect a lot stronger, one can state that

> *"the European Union is considered in such a way to overcome the possible dictate of those larger states and usually there is not a strictly proportional system of voting, so those smaller states are somewhat overvalued to increase their power or influence. [In reality] the percentage for those large states is not actually as high as the possible value. The question if the rule of representativeness or the rule of effectiveness is the most important one at the moment, but it's a matter of deciding which rule is the most important in this case."*[47]

Ratifying treaties without referenda has been one of the issues touched upon when opposition was voiced regarding the measures taken by the Union. While in principle, the idea of a referendum seems to be a good one, and the lack thereof seems as a part of this supposed democratic deficit, in practical terms, more elements must be taken into account when reflecting on this issue. The most important aspect would seem to be the populations' education and awareness level of the subject at hand, as this is the best way of curtaining also the perils of populism:

> *"If we talk about democracy, this [referenda] is the best solution. If you have a democratic country, I think that the voice of the citizens is the most important (…) and populism is always there. [But] the more you understand, the more better decisions you will make. (…) when you ask a poor person what he is thinking of the future he would say that everything [what] is good for him is good for the country, that's why you have the populists. They can say everything and if you believe them you will say it's a good idea. If you have a very good education system, from primary school, you will create a very conscious society. Then the democratic system is the best solution. (…) Not asking the citizens is not a good idea. You need to ask them."*[48]

But not all associate the democratic deficit with this need for referendums, especially when looking at the actual state of the ordinary man's capacity to make an educated judgment. For Dr. Pacześniak, the problems with the fiscal treaties is that:

> *"the technocrats are negotiating them, by a long and detailed process and it looks like that there is a rupture between technocrats and the rest of the society. Nevertheless, by such referenda, ordinary people do not answer the questions as such, but they answer*

[47]Interview with Dr. Pacześniak of the University of Wroclaw, taken on the 4th of June 2013; transcripts available in the appendix

[48] Interview with Dr. Klimowicz of the University of Wroclaw, taken on the 4th of June 2013; transcripts available in the appendix

> *to them according to their trust or distrust towards their own political elites. So, the question of the referenda shouldn't be associated to the democratic deficit in the European Union and by introducing such referenda we would not improve democratic procedures in the European Union."*[49]

## Conclusions

The financial and economic crisis represent a stepping stone in the development of the EU construction, a new major crisis that can push the Member Countries to reevaluate their approach towards further integration as well as towards crisis management skills. The last 5 years have brought to light inconsistencies in both the European construction and Member state's way of handling their budgetary and deficit forecasts. Many Member states have registered historic decreases of gross domestic product (GDP) and high rates of unemployment while the European Union had a reactive position towards what was happening within the single market and its policies were primarily aimed at salvaging the large financial institutions on the brink of collapse.

This report covered four aspects considered extremely relevant for giving an overview of the situation within the European Union between 2008 and 2013. The first chapter offers some critical considerations regarding the genesis of the crisis and the overall measures taken by the EU Institutions in order to cope with the issues arising among the Member States' national economies. The effects of the crisis were country specific, with the possibility of drawing a division between the Northern states, most of them maintaining the stability of their national financial and economic markets, and the South region of the EU, where countries such as Greece, Spain and Portugal were strongly affected.

The second section was concerned with the austerity policy and the connection of this strategy with the German approach towards excessive deficit. Those types of measures proved to be inadequate for solving the crisis, but the EU and Germany continue to insist on them for various reasons, the most important being the particular economic approach of ordoliberalism which takes precedence in an European economic arena dominated by the German market over the alternative

[49] Interview with Prof. Dr. Pacześniak of the University of Wroclaw, taken on the 4th of June 2013; transcripts available in the appendix

New Keynesian theories. In the present context, the proposition of consolidating budgets through reducing expenditure and increasing taxes was translated into a practical failure. Those measures resulted in the reduction of growth in internal aggregate demand and thus reduced GDP growth. Also, the banks were seen as the main culprits for the crisis and the problem of responsibility became one of high importance. Some experts even proposed that the customers of the banks, either individuals or companies, should pay the bill. The failure of austerity measures brought about a new interest towards social issues, especially unemployment.

EU's political answers to the economic problems were analyzed in the third part of the report. Three of the main treaties adopted by the European institutions came into discussion: the Economic Stability Measures, the Fiscal pact and the banking union, all of which proved to be mainly collections of older provisions reiterated in new pacts but without real thought as to whether or not they will be actually correctly implemented this time around. Moreover, they were inefficient economic measures taking through political decisions and were coupled with over-optimistic predictions of the evolution of the national economies of the Member States.

The last section regarded the effects of the crisis management strategies adopted by the European institutions on the already existing democratic deficit of the European Union. There is a trend in increasing the executive power in the detriment of the national parliaments, with the MS governments being able to surpass the decisions of the latter. Also, the balance of power between the EU and the Member States started to incline in the favour of the supranational entity.

Thus, to sum up, the EU's handling of the crisis is imbedded by the German approach on austerity measures as being beneficial for budgetary consolidation, instead of detrimental towards budgetary consolidation and hence towards the overall economic growth of the struggling Member States. Secondly, the measures hailed as being effective solutions for the prevention of future similar situations, proved to be not so new, as they have actually been agreed on previously and ignored. What was missing, a mechanism to insure their optimal implementation by Member states has not been established and the logic behind the punitive measures seems to be faulty. Last but not least, the democratic deficit, considered to have been accentuated by the crisis, remains an issue of debate as the perceptions towards the European construction and what represents "fairness" in terms of power distribution amongst Member states still vary to a large degree.

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# Apenndix 1.

## Statistical and historical data

Table 1: Chronology of the European economic crisis

**2008**

| | |
|---|---|
| 15th September | The US bank Lehman Brothers has to file bankruptcy. |
| October | The ECB takes additional crisis measures. |
| 12th October | First meeting of the heads of government and the heads of state of the Euro zone (European Council) in Paris. |
| 15th to 16th October | The European Council confirms the will of concerted action. |

**2009**

| | |
|---|---|
| 20th October | The incoming Greek government released dramatic deficit revisions. |

**2010**

| | |
|---|---|
| 11th February | The first EU-Meeting regarding the financial situation of Greece takes place. |
| 25th to 26th March | The European Council and EU-Summit: The Eurozone members oblige to coordinate the bilateral credits, if Greece couldn´t refinance; including appropriate IMF-funds. |
| | The European Council establishes the "Van Rompuy Task Force": strategies for the crisis management and fiscal discipline till the end of 2010. |
| 23rd April | Greece uses financial aid and gets controlled by ECB and IMF. |

| | |
|---|---|
| 2nd May | Greece aid package approved: up to 80 billion € from the Eurozone and up to 30 billion € from IMF. |
| 7th to 8th May | The European Council passed the "Euro-rescue-fund" and the Greece aid package. |
| 9th to 10th May | The EU Finance ministers arrange details of the "European Financial Stability Facility" (EFSF) and the "European Financial Stabilization Mechanism" (EFSM): EU state credit guaranties 440 billion €; 60 billion €, 0€ from community funds and 250 billion € from the IMF. |
| 10th May | European Central Bank starts buying state bonds from crisis-ridden countries. |
| 7th September | The Council of the European Union decides on the "European Semester": a cycle to coordinate the economic policy. |
| 29th September | The Government presents the 'Six-pack'. |
| 18th October | Angela Merkel and Nicolas Sarkozy present a permanent mechanism to save insolvent states. |
| 21st October | The "Van Rompuy Task Force" submits their report to the European Council. |
| 28th November | As the first state Ireland gets an emergency-credit from the EFSF. EFSM= 22,5 billion €, EFSF and – bilateral – Great Britain, Sweden and Denmark = 22,5 billion €, IMF= 22,5 billion €. |
| 16th to 17th December | The European Council determines the permanent European Stability Mechanism (ESM). |

**2011**

| | |
|---|---|
| 11th March | The EU-Meeting to deliberate upon Libya takes place. Enhancement of the EFSF. |
| 24th to 25th March | European Council decided a change in the EU law: constitution of a permanent ESM. ESM: 80 billion € basic capital paid by the Euro-zone-countries, starting 2013. Credit guaranties about 620 |

| | |
|---|---|
| | billion €. Supplementing the ESM capacity up to 250 billion €, given by the IMF. |
| 17th May | Portugal gets a necessary credit: up to 78 billion €. EFSF, EFSM and IMF accepted 26 billion for each of them. |
| 21st July | European Council: The second aid package for Greece is necessary and also extending EFSF competences. |
| 28th September and 4th October | The European Parliament (28th September) and the Council of the European Union (4th October) adopted the “Six-pack“: Fiscal policy rules of the “Stability and Growth Pact“ got reformed and stronger coordination of national policy (first presented by the European Commission on 29th September 2010). |
| 26th October | EU- summit: The European Council determines “package of measures“ for the stabilization of the Eurozone, including the following aspects: The Greek creditors quit up to 50 percent of their claims, the EFSF capacity raising up from 250 billion € through “leverages“ to the four- to fivefold and recapitalization of the European banking system. |
| 8th and 9th December | The EU- summit and the European Council determine more measures right up to a “politic- economic stability union“, which will stronger intervene into national budgets (primarily right). If the European Commission realizes a country breaks the 3% border of the budget deficit, there will automatically be consequences. Except the member states of the European monetary area built and majoritarian opposition. |

**2012**

| | |
|---|---|
| January | All EU-members except Great Britain and Czech Republic have to commit themselves to determine a debt limit like Germany. The maximum of the economic deficit is 0,5%. |
| 29th February | 800 banks get 530 billion €. |
| 11th July | The ECB reduces the interest rate (0,75%). |

| | |
|---|---|
| April | Cyprus gets several billions of Euros from the EU (Emergency Liquidity Assistance). |
| 2nd May | The ECB reduces the euro-rate (0,5%). |
| 9th June | The European finance ministers promise a 100-billion Euro-credit for Spain. |
| July | The European finance ministers concede a higher period for reducing the new indebtedness. |

**2013**

| | |
|---|---|
| 16th March | Cyprus and the EU determine an aid package about 10 billion Euros. |
| 25th March | The Agreement between Cyprus and the Troika about the 'Cyprus Popular Bank' gets disbanded and 4.2 billion Euros get deposit at a so called "Bad bank". |
| May 2013 | Cyprus gets 3 billion Euros from the EU. |

Table 2: Paid-in shares and capital of ESM

| ESM Shareholders | ESM Key (%) | Number of shares | Subscribed capital | Subscribed capital called and paid |
|---|---|---|---|---|
| Federal Republic of Germany | 27.1464 | 1,900,248 | 190,024,800 | 8,686,848 |
| French Republic | 20.3859 | 1,427,013 | 142,701,300 | 6,523,488 |
| Italian Republic | 17.9137 | 1,253,959 | 125,395,900 | 5,732,384 |
| Kingdom of Spain | 11.9037 | 833,259 | 83,325,900 | 3,809,184 |
| Kingdom of the Netherlands | 5.7170 | 400,190 | 40,019,000 | 1,829,440 |
| Kingdom of Belgium | 3.4771 | 243,397 | 24,339,700 | 1,112,672 |
| Hellenic Republic | 2.8167 | 197,169 | 19,716,900 | 901,344 |
| Republic of Austria | 2.7834 | 194,838 | 19,483,800 | 890,688 |
| Portuguese Republic | 2.5092 | 175,644 | 17,564,400 | 802,944 |
| Republic of Finland | 1.7974 | 125,818 | 12,581,800 | 1,437,920 |
| Ireland | 1.5922 | 111,454 | 11,145,400 | 509,504 |
| Slovak Republic | 0.8240 | 57,680 | 5,768,000 | 263,680 |
| Republic of Slovenia | 0.4276 | 29,932 | 2,993,200 | 136,832 |
| Grand Duchy of Luxembourg | 0.2504 | 17,528 | 1,752,800 | 80,128 |
| Republic of Cyprus | 0.1962 | 13,734 | 1,373,400 | 62,784 |
| Republic of Estonia | 0.1860 | 13,020 | 1,302,000 | 59,520 |
| Malta | 0.0731 | 5,117 | 511,700 | 23,392 |
| Total | 100.0000 | 7,000,000 | 700,000,000 | 32,862,752 |

Source: European Stability Mechanism

Table 3: At-risk-of-poverty thresholds

| TIME | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|---|---|---|
| GEO | | | | | | | | | | |
| Belgium | 9,313(b) | 9,405 | 9,947 | 10,328 | 10,540 | 10,791 | 11,588 | 11,678 | 12,005 | : |
| Bulgaria | 845 | 876 | 934 | 830(b) | 888 | 1,303 | 1,697 | 1,810 | 1,741 | : |
| Czech Republic | : | : | 2,540(b) | 2,881 | 3,254 | 3,641 | 4,377 | 4,235 | 4,471 | : |
| Denmark | 12,554(b) | 12,735 | 13,274 | 13,598 | 14,004 | 14,497 | 15,017 | 15,401 | 15,837 | : |
| Germany (until 1990 former territory of the FRG) | : | : | 9,836(b) | 9,398 | 10,686 | 10,986 | 11,151 | 11,278 | 11,426 | : |
| Estonia | 1,485 | 1,539(b) | 1,788 | 2,183 | 2,689 | 3,328 | 3,725 | 3,436 | 3,359 | : |
| Ireland | 10,248(b) | 10,845 | 11,279 | 11,854 | 13,239 | 13,797 | 13,467 | 11,929 | 11,836 | : |
| Greece | 4,923(b) | 5,306 | 5,650 | 5,910 | 6,120 | 6,480 | 6,897 | 7,178 | 6,591 | : |
| Spain | 5,923 | 6,285(b) | 6,360 | 6,888 | 7,223 | 7,770 | 7,980 | 7,818 | 7,509 | : |
| France | 9,024 | 9,145(b) | 9,567 | 9,726 | 9,865 | 11,395(b) | 11,786 | 12,035 | 11,997 | : |
| Croatia | 2,441 | : | : | : | : | : | : | 3,433(b) | 3,326 | : |
| Italy | : | 8,131(b) | 8,611 | 8,714 | 9,003 | 9,383 | 9,382 | 9,562 | 9,583 | : |
| Cyprus | 7,547 | : | 7,894(b) | 8,722 | 9,609 | 9,614(b) | 9,871 | 9,871 | 10,328 | : |
| Latvia | : | : | 1,322(b) | 1,520 | 2,010 | 2,899 | 3,284 | 2,722 | 2,490(b) | 2,662 |
| Lithuania | : | : | 1,235(b) | 1,520 | 1,966 | 2,502 | 2,889 | 2,436 | 2,403 | : |
| Luxembourg | 15,468(b) | 16,165 | 17,038 | 17,688 | 17,935 | 18,550 | 19,059 | 19,400 | 19,523 | : |
| Hungary | 2,196 | : | 2,068(b) | 2,310 | 2,361 | 2,640 | 2,844 | 2,544 | 2,721 | : |
| Malta | : | : | 5,147(b) | 5,423 | 5,581 | 6,032 | 6,392 | 6,225 | 6,517 | : |
| Netherlands | 10,523 | : | 10,200(b) | 10,358 | 10,946 | 11,713 | 12,094 | 12,175 | 12,186 | : |
| Austria | 9,378(b) | 10,200 | 10,801 | 10,713 | 10,893 | 11,406 | 11,931 | 12,371 | 12,791 | : |
| Poland | : | : | 1,520(b) | 1,867 | 2,101 | 2,493 | 3,058 | 2,643 | 3,015 | : |
| Portugal | : | 4,149(b) | 4,317 | 4,386 | 4,544 | 4,886 | 4,969 | 5,207 | 5,046 | : |
| Romania | : | : | : | : | 995 | 1,172 | 1,297 | 1,222 | 1,270 | : |
| Slovenia | 4,742 | : | 5,278(b) | 5,590 | 5,944 | 6,536 | 7,118 | 7,042 | 7,199 | : |
| Slovakia | : | : | 1,698(b) | 1,988 | 2,383 | 2,875 | 3,403 | 3,670 | 3,784 | : |
| Finland | 9,855 | 10,008(b) | 10,489 | 10,982 | 11,222 | 11,876 | 12,577 | 12,809 | 13,096 | 13,619 |
| Sweden | : | 10,398(b) | 10,499 | 10,795 | 11,307 | 12,344 | 12,749 | 11,825 | 13,504 | : |
| United Kingdom | 10,150 | : | 11,124(b) | 11,697 | 12,686 | 11,354 | 9,757 | 10,263 | 10,281 | : |
| Iceland | : | 13,420 | 14,207 | 17,075 | 17,268 | 19,323 | 13,417 | 10,992 | 11,384 | : |
| Norway | 16,498(b) | 15,834 | 15,395 | 17,046 | 17,358 | 19,068 | 20,242 | 19,438 | 21,838 | : |

Source: Eurostat

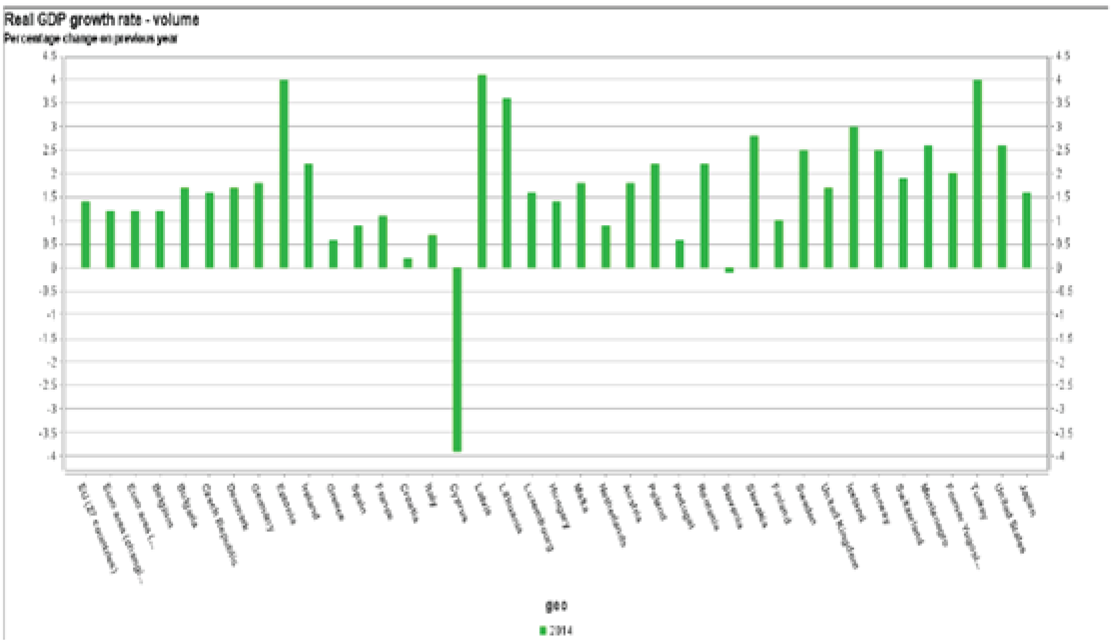
Table 4: Real GDP growth

**Real GDP growth rate - volume**
Percentage change on previous year

| geo \ time | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| EU (27 countries) | 1.5 | 2.6 | 2.2 | 3.4 | 3.2 | 0.4 | -4.5 | 2.1 | 1.6 | -0.4 | -0.1 (f) | 1.4 (f) |
| Euro area (changing composition) | 0.7 | 2.2 | 1.7 | 3.2 | 2.9 | 0.4 | -4.4 | 2.0 | 1.5 | -0.6 | -0.4 (f) | 1.2 (f) |
| Euro area (17 countries) | 0.7 | 2.2 | 1.7 | 3.2 | 3.0 | 0.4 | -4.4 | 2.0 | 1.5 | -0.6 | -0.4 (f) | 1.2 (f) |
| Belgium | 0.8 | 3.3 | 1.8 | 2.7 | 2.9 | 1.0 | -2.8 | 2.4 | 1.8 | -0.3 | 0.0 (f) | 1.2 (f) |
| Bulgaria | 5.5 | 6.7 | 6.4 | 6.5 | 6.4 | 6.2 | -5.5 | 0.4 | 1.8 | 0.8 | 0.9 (f) | 1.7 (f) |
| Czech Republic | 3.8 | 4.7 | 6.8 | 7.0 | 5.7 | 3.1 | -4.5 | 2.5 | 1.9 | -1.3 | -0.4 (f) | 1.6 (f) |
| Denmark | 0.4 | 2.3 | 2.4 | 3.4 | 1.6 | -0.8 | -5.7 | 1.6 | 1.1 | -0.4 | 0.7 (f) | 1.7 (f) |
| Germany | -0.4 | 1.2 | 0.7 | 3.7 | 3.3 | 1.1 | -5.1 | 4.2 | 3.0 | 0.7 | 0.4 (f) | 1.8 (f) |
| Estonia | 7.8 | 6.3 | 8.9 | 10.1 | 7.5 | -4.2 | -14.1 | 3.3 | 8.3 | 3.2 | 3.0 (f) | 4.0 (f) |
| Ireland | 3.9 | 4.4 | 5.9 | 5.4 | 5.4 | -2.1 | -5.5 | -0.8 | 1.4 | 0.9 | 1.1 (f) | 2.2 (f) |
| Greece | 5.9 | 4.4 | 2.3 (b) | 5.5 | 3.5 | -0.2 (b) | -3.1 (b) | -4.9 (b) | -7.1 (b) | -6.4 (b) | -4.2 (f) | 0.6 (f) |
| Spain | 3.1 | 3.3 | 3.6 | 4.1 | 3.5 | 0.9 | -3.7 | -0.3 | 0.4 | -1.4 | -1.5 (f) | 0.9 (f) |
| France | 0.9 | 2.5 | 1.8 | 2.5 | 2.3 | -0.1 | -3.1 | 1.7 | 2.0 | 0.0 | -0.1 (f) | 1.1 (f) |
| Croatia | 5.4 | 4.1 | 4.3 | 4.9 | 5.1 | 2.1 | -6.9 | -2.3 | 0.0 (p) | -2.0 (p) | -1.0 (f) | 0.2 (f) |
| Italy | 0.0 | 1.7 | 0.9 | 2.2 | 1.7 | -1.2 | -5.5 | 1.7 | 0.4 | -2.4 | -1.3 (f) | 0.7 (f) |
| Cyprus | 1.9 | 4.2 | 3.9 | 4.1 | 5.1 | 3.6 | -1.9 | 1.3 | 0.5 | -2.4 | -8.7 (f) | -3.9 (f) |
| Latvia | 7.6 | 8.9 | 10.1 | 11.2 | 9.6 | -3.3 | -17.7 | -0.9 | 5.5 | 5.6 | 3.8 (f) | 4.1 (f) |
| Lithuania | 10.3 | 7.4 | 7.8 | 7.8 | 9.8 | 2.9 | -14.8 | 1.5 | 5.9 | 3.7 | 3.1 (f) | 3.6 (f) |
| Luxembourg | 1.7 | 4.4 | 5.3 | 4.9 | 6.6 | -0.7 | -4.1 | 2.9 | 1.7 | 0.3 | 0.8 (f) | 1.6 (f) |
| Hungary | 3.9 | 4.8 | 4.0 | 3.9 | 0.1 | 0.9 | -6.8 | 1.3 | 1.6 | -1.7 | 0.2 (f) | 1.4 (f) |
| Malta | 0.7 | -0.3 | 3.6 | 2.8 | 4.1 | 3.9 | -2.8 | 3.2 | 1.8 | 1.0 | 1.4 (f) | 1.8 (f) |
| Netherlands | 0.3 | 2.2 | 2.0 | 3.4 | 3.9 | 1.8 | -3.7 | 1.6 | 1.0 | -1.0 | -0.8 (f) | 0.9 (f) |
| Austria | 0.9 | 2.6 | 2.4 | 3.7 | 3.7 | 1.4 | -3.8 | 2.1 | 2.7 | 0.8 | 0.6 (f) | 1.8 (f) |
| Poland | 3.9 | 5.3 | 3.6 | 6.2 | 6.8 | 5.1 | 1.6 | 3.9 | 4.5 | 1.9 | 1.1 (f) | 2.2 (f) |
| Portugal | -0.9 | 1.6 | 0.8 | 1.4 | 2.4 | 0.0 | -2.9 | 1.9 | -1.6 | -3.2 | -2.3 (f) | 0.6 (f) |
| Romania | 5.2 | 8.5 | 4.2 | 7.9 | 6.3 | 7.3 | -6.6 | -1.1 | 2.2 | 0.7 | 1.6 (f) | 2.2 (f) |
| Slovenia | 2.9 | 4.4 | 4.0 | 5.8 | 7.0 | 3.4 | -7.8 | 1.2 | 0.6 | -2.3 | -2.0 (f) | -0.1 (f) |
| Slovakia | 4.8 | 5.1 | 6.7 | 8.3 | 10.5 | 5.8 | -4.9 | 4.4 | 3.2 | 2.0 | 1.0 (f) | 2.8 (f) |
| Finland | 2.0 | 4.1 | 2.9 | 4.4 | 5.3 | 0.3 | -8.5 | 3.3 | 2.8 | -0.2 | 0.3 (f) | 1.0 (f) |
| Sweden | 2.3 | 4.2 | 3.2 | 4.3 | 3.3 | -0.6 | -5.0 | 6.6 | 3.7 | 0.7 | 1.5 (f) | 2.5 (f) |
| United Kingdom | 3.9 | 3.2 | 3.2 | 2.8 | 3.4 | -0.8 | -5.2 | 1.7 | 1.1 | 0.2 | 0.6 (f) | 1.7 (f) |
| Iceland | 2.4 | 7.8 | 7.2 | 4.7 | 6.0 | 1.2 | -6.6 | -4.1 | 2.9 | 1.6 | 1.8 (f) | 3.0 (f) |

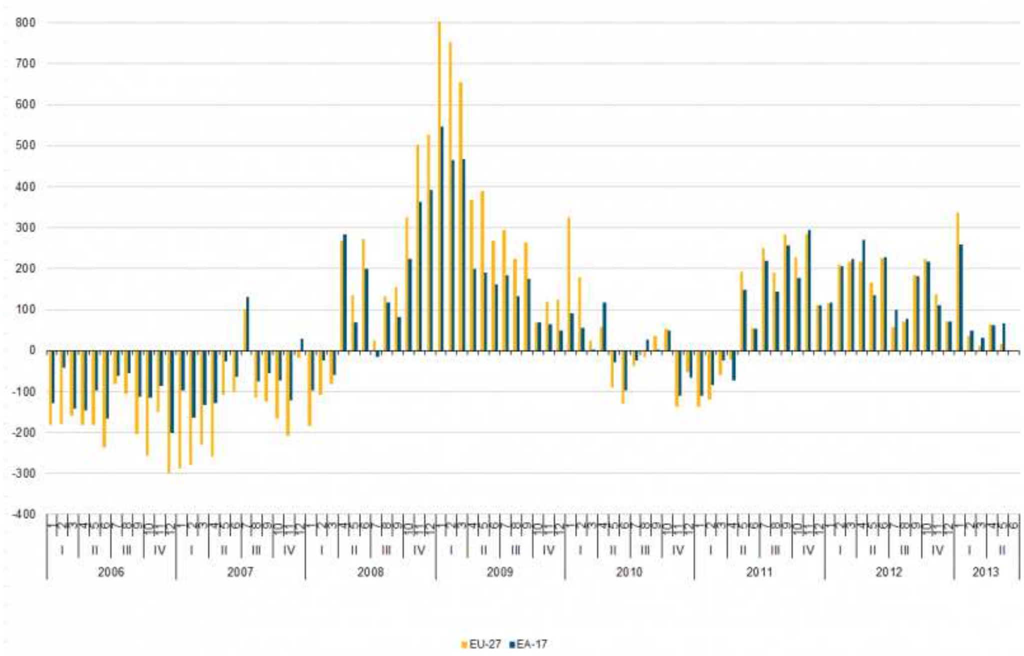
Source: Eurostat

Picture 1: Real GDP growth rate volume



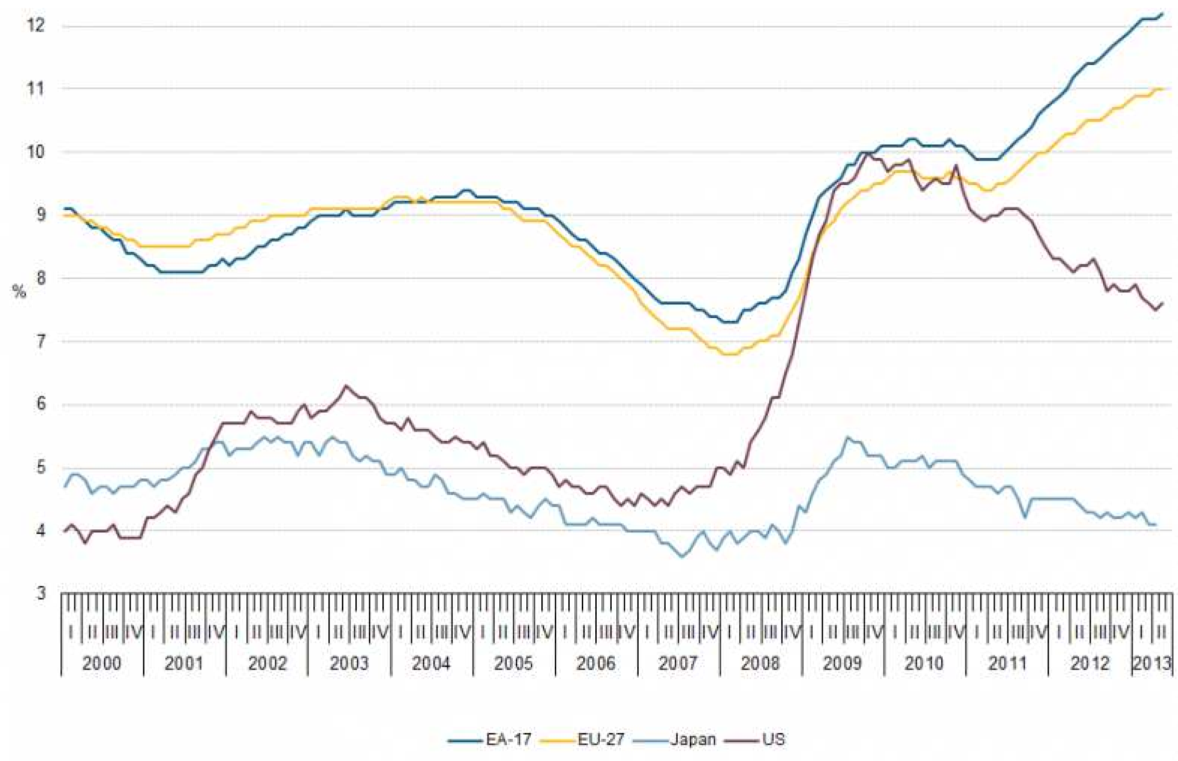

Source: Eurostat

Picture 2: Change in the number of unemployed persons (2006 – 2013)



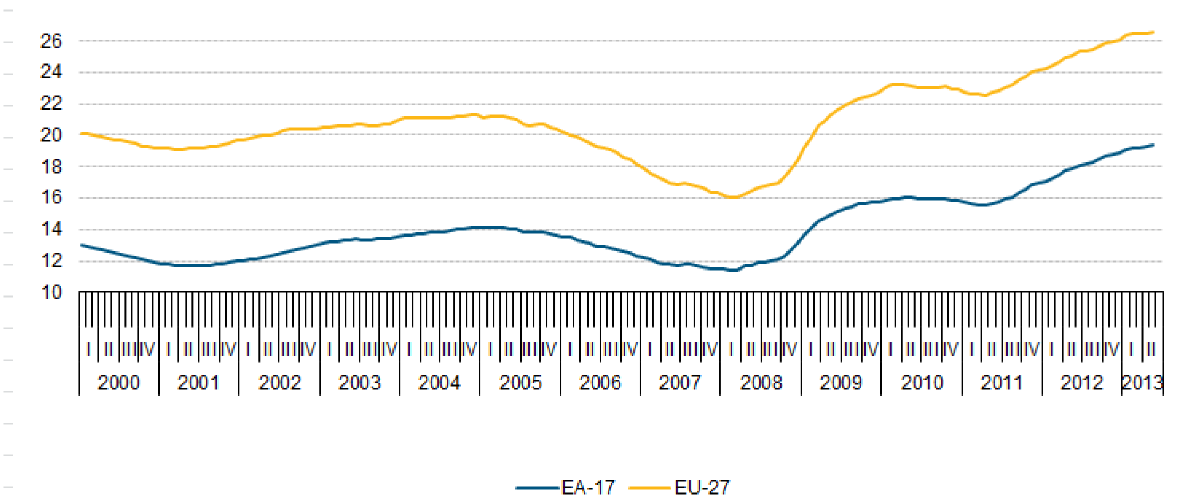
Source: Eurostat

Picture 3: Unemployment rates EU-27, EA-17, US and Japan (2000 – 2013)



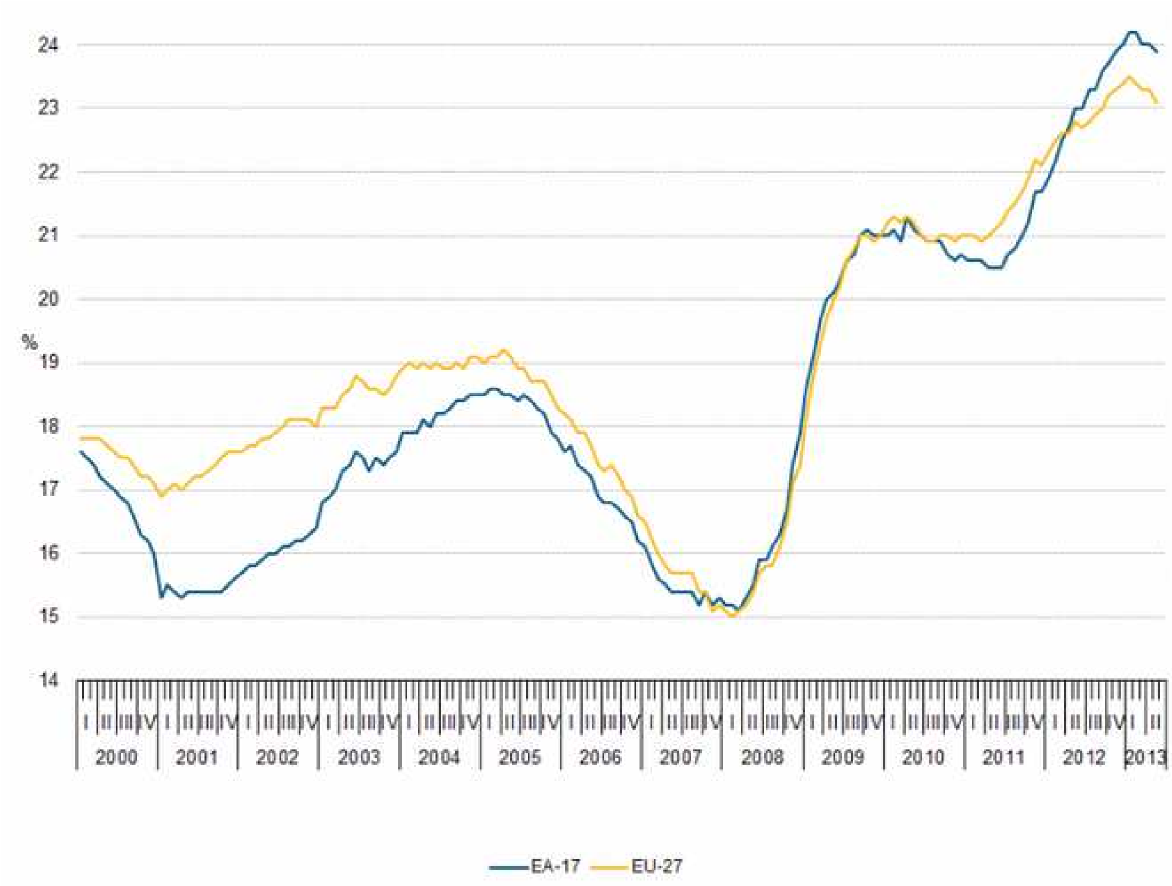

Source: Eurostat

Picture 4: Unemployed persons in millions EU-27 and EA-17 (2000 – 2013)




Source: Eurostat

Picture 5: Youth unemployment rates EU-27 and EA-17 (2000 – 2013)




Source: Eurostat

Table 5: Youth unemployment by member state (2012)

| | Youth unemployment rate | | | | Youth unemployment ratio | | |
|---|---|---|---|---|---|---|---|
| | 2010 | 2011 | 2012 | 2012Q4* | 2010 | 2011 | 2012 |
| EU-27 | 21.1 | 21.4 | 22.8 | 23.2 | 9.0 | 9.1 | 9.7 |
| Euro area | 20.9 | 20.8 | 23.0 | 23.7 | 8.7 | 8.7 | 9.6 |
| Belgium | 22.4 | 18.7 | 19.8 | 22.0 | 7.3 | 6.0 | 6.2 |
| Bulgaria | 21.8 | 25.0 | 28.1 | 28.4 | 6.7 | 7.4 | 8.5 |
| Czech Republic | 18.3 | 18.1 | 19.5 | 19.3 | 5.7 | 5.4 | 6.1 |
| Denmark | 14.0 | 14.2 | 14.1 | 14.2 | 9.4 | 9.6 | 9.1 |
| Germany | 9.9 | 8.6 | 8.1 | 7.9 | 5.1 | 4.5 | 4.1 |
| Estonia | 32.9 | 22.3 | 20.9 | 19.3 | 12.6 | 9.1 | 8.7 |
| Ireland | 27.6 | 29.1 | 30.4 | 29.4 | 12.0 | 12.1 | 12.3 |
| Greece | 32.9 | 44.4 | 55.3 | 57.9 | 10.0 | 13.0 | 16.1 |
| Spain | 41.6 | 46.4 | 53.2 | 55.2 | 17.8 | 19.0 | 20.6 |
| France | 23.6 | 22.8 | 24.3 | 25.4 | 8.9 | 8.4 | 9.0 |
| Italy | 27.8 | 29.1 | 35.3 | 36.9 | 7.9 | 8.0 | 10.1 |
| Cyprus | 16.6 | 22.4 | 27.8 | 31.8 | 6.7 | 8.7 | 10.8 |
| Latvia | 37.2 | 31.0 | 28.4 | 24.7 | 13.9 | 11.6 | 11.4 |
| Lithuania | 35.3 | 32.2 | 26.4 | 24.2 | 10.4 | 9.0 | 7.7 |
| Luxembourg | 15.8 | 16.4 | 18.1 | 18.5 | 3.5 | 4.2 | 5.0 |
| Hungary | 26.6 | 26.1 | 28.1 | 28.8 | 6.6 | 6.4 | 7.3 |
| Malta | 13.1 | 13.8 | 14.2 | 14.5 | 6.7 | 7.1 | 7.2 |
| Netherlands | 8.7 | 7.6 | 9.5 | 9.8 | 6.0 | 5.3 | 6.6 |
| Austria | 8.8 | 8.3 | 8.7 | 8.7 | 5.2 | 5.0 | 5.2 |
| Poland | 23.7 | 25.8 | 26.5 | 27.5 | 8.2 | 8.7 | 8.9 |
| Portugal | 27.7e | 30.1 | 37.7 | 38.4 | 8.2 | 11.7 | 14.3 |
| Romania | 22.1 | 23.7 | 22.7 | 22.2 | 6.9 | 7.4 | 7.0 |
| Slovenia | 14.7 | 15.7 | 20.6 | 23.2 | 5.9 | 5.9 | 7.1 |
| Slovakia | 33.9 | 33.5 | 34.0 | 35.1 | 10.4 | 10.0 | 10.4 |
| Finland | 21.4 | 20.1 | 19.0 | 19.3 | 10.6 | 10.1 | 9.8 |
| Sweden | 24.8 | 22.8 | 23.7 | 24.1 | 12.8 | 12.1 | 12.4 |
| United Kingdom | 19.6 | 21.1 | 21.0 | 20.7 | 11.6 | 12.4 | 12.4 |

* The quarterly youth unemployment rate is seasonally adjusted.
e: estimate

Source: Eurostat

Table 6: Unemployment rate by member state (2001 – 2012)

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| EU-27 | 8.6 | 8.9 | 9.1 | 9.3 | 9.0 | 8.3 | 7.2 | 7.1 | 9.0 | 9.7 | 9.7 | 10.5 |
| Euro area | 8.1 | 8.5 | 9.0 | 9.3 | 9.2 | 8.5 | 7.6 | 7.6 | 9.6 | 10.1 | 10.2 | 11.4 |
| Belgium (1) | 6.6 | 7.5 | 8.2 | 8.4 | 8.5 | 8.3 | 7.5 | 7.0 | 7.9 | 8.3 | 7.2 | 7.6 |
| Bulgaria | 19.5 | 18.2 | 13.7 | 12.1 | 10.1 | 9.0 | 6.9 | 5.6 | 6.8 | 10.3 | 11.3 | 12.3 |
| Czech Republic | 8.1 | 7.3 | 7.8 | 8.3 | 7.9 | 7.1 | 5.3 | 4.4 | 6.7 | 7.3 | 6.7 | 7.0 |
| Denmark | 4.5 | 4.6 | 5.4 | 5.5 | 4.8 | 3.9 | 3.8 | 3.4 | 6.0 | 7.5 | 7.6 | 7.5 |
| Germany | 7.9 | 8.7 | 9.8 | 10.5 | 11.3 | 10.3 | 8.7 | 7.5 | 7.8 | 7.1 | 5.9 | 5.5 |
| Estonia | 12.6 | 10.3 | 10.1 | 9.7 | 7.9 | 5.9 | 4.6 | 5.5 | 13.8 | 16.9 | 12.5 | 10.2 |
| Ireland | 3.9 | 4.5 | 4.6 | 4.5 | 4.4 | 4.5 | 4.7 | 6.4 | 12.0 | 13.9 | 14.7 | 14.7 |
| Greece | 10.7 | 10.3 | 9.7 | 10.5 | 9.9 | 8.9 | 8.3 | 7.7 | 9.5 | 12.6 | 17.7 | 24.3 |
| Spain | 10.5 | 11.4 | 11.4 | 10.9 | 9.2 | 8.5 | 8.3 | 11.3 | 18.0 | 20.1 | 21.7 | 25.0 |
| France | 8.2 | 8.3 | 8.9 | 9.3 | 9.3 | 9.2 | 8.4 | 7.8 | 9.5 | 9.7 | 9.6 | 10.2 |
| Italy | 9.0 | 8.5 | 8.4 | 8.0 | 7.7 | 6.8 | 6.1 | 6.7 | 7.8 | 8.4 | 8.4 | 10.7 |
| Cyprus | 3.9 | 3.5 | 4.1 | 4.6 | 5.3 | 4.6 | 3.9 | 3.7 | 5.4 | 6.3 | 7.9 | 11.9 |
| Latvia | 12.9 | 12.8 | 11.3 | 11.2 | 9.6 | 7.3 | 6.5 | 8.0 | 18.2 | 19.8 | 16.2 | 14.9 |
| Lithuania | 17.4 | 13.8 | 12.4 | 11.3 | 8.0 | 5.2 | 3.8 | 5.3 | 13.6 | 18.0 | 15.3 | 13.3 |
| Luxembourg | 1.9 | 2.6 | 3.8 | 5.0 | 4.6 | 4.6 | 4.2 | 4.9 | 5.1 | 4.6 | 4.8 | 5.1 |
| Hungary | 5.6 | 5.6 | 5.8 | 6.1 | 7.2 | 7.5 | 7.4 | 7.8 | 10.0 | 11.2 | 10.9 | 10.9 |
| Malta | 7.6 | 7.4 | 7.7 | 7.2 | 7.3 | 6.9 | 6.5 | 6.0 | 6.9 | 6.9 | 6.5 | 6.4 |
| Netherlands | 2.5 | 3.1 | 4.2 | 5.1 | 5.3 | 4.4 | 3.6 | 3.1 | 3.7 | 4.5 | 4.4 | 5.3 |
| Austria | 3.6 | 4.2 | 4.3 | 4.9 | 5.2 | 4.8 | 4.4 | 3.8 | 4.8 | 4.4 | 4.2 | 4.3 |
| Poland | 18.3 | 20.0 | 19.8 | 19.1 | 17.9 | 13.9 | 9.6 | 7.1 | 8.1 | 9.7 | 9.7 | 10.1 |
| Portugal | 4.6 | 5.7 | 7.1 | 7.5 | 8.6 | 8.6 | 8.9 | 8.5 | 10.6 | 12.0 | 12.9 | 15.9 |
| Romania | 6.6 | 7.5 | 6.8 | 8.0 | 7.2 | 7.3 | 6.4 | 5.8 | 6.9 | 7.3 | 7.4 | 7.0 |
| Slovenia | 6.2 | 6.3 | 6.7 | 6.3 | 6.5 | 6.0 | 4.9 | 4.4 | 5.9 | 7.3 | 8.2 | 8.9 |
| Slovakia | 19.5 | 18.8 | 17.7 | 18.4 | 16.4 | 13.5 | 11.2 | 9.6 | 12.1 | 14.5 | 13.6 | 14.0 |
| Finland | 9.1 | 9.1 | 9.0 | 8.8 | 8.4 | 7.7 | 6.9 | 6.4 | 8.2 | 8.4 | 7.8 | 7.7 |
| Sweden | 5.8 | 6.0 | 6.6 | 7.4 | 7.7 | 7.1 | 6.1 | 6.2 | 8.3 | 8.6 | 7.8 | 8.0 |
| United Kingdom | 5.0 | 5.1 | 5.0 | 4.7 | 4.8 | 5.4 | 5.3 | 5.6 | 7.6 | 7.8 | 8.0 | 7.9 |
| Iceland | : | : | 3.3 | 3.1 | 2.6 | 2.9 | 2.3 | 3.0 | 7.2 | 7.6 | 7.1 | 6.0 |
| Norway (2) | 3.4 | 3.7 | 4.2 | 4.3 | 4.5 | 3.4 | 2.5 | 2.5 | 3.2 | 3.6 | 3.3 | 3.2 |
| Croatia | : | 14.8 | 14.2 | 13.7 | 12.7 | 11.2 | 9.0 | 8.4 | 9.1 | 11.8 | 13.5 | 15.9 |
| Turkey (3) | : | : | : | : | 9.2 | 8.7 | 8.8 | 9.7 | 12.5 | 10.7 | 8.8 | 8.1 |
| Japan (1) | 5.0 | 5.4 | 5.3 | 4.7 | 4.4 | 4.1 | 3.9 | 4.0 | 5.1 | 5.1 | 4.6 | 4.3 |
| United States | 4.8 | 5.8 | 6.0 | 5.5 | 5.1 | 4.6 | 4.6 | 5.8 | 9.3 | 9.6 | 8.9 | 8.1 |

Source: Eurostat

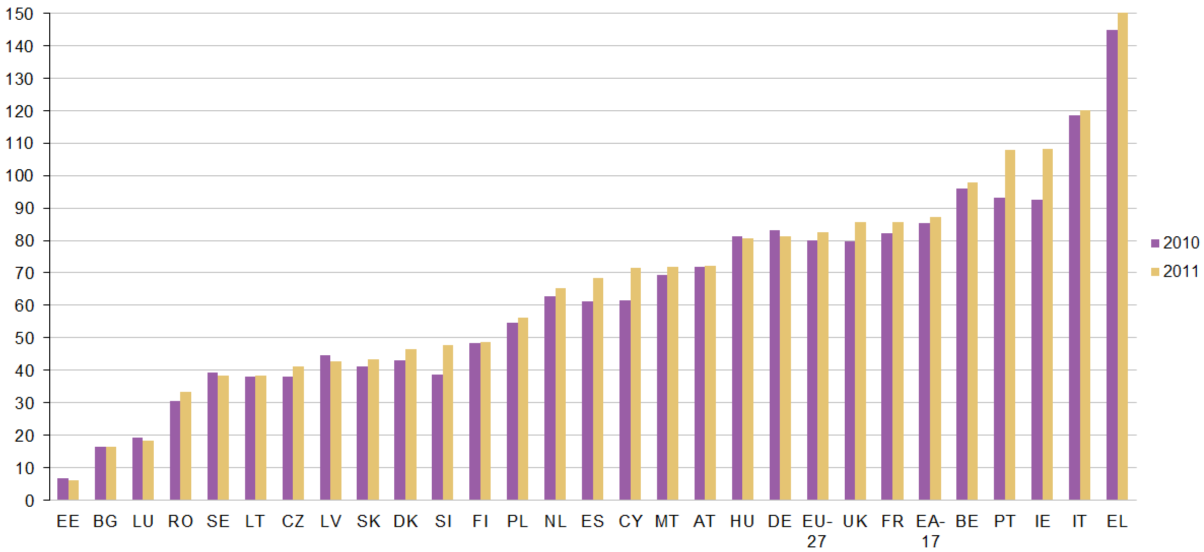
Table 7: Unemployment rate by type EU-27 (2003 – 2012)

| | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 |
|---|---|---|---|---|---|---|---|---|---|---|
| Male | 8.5 | 8.6 | 8.4 | 7.6 | 6.6 | 6.6 | 9.1 | 9.7 | 9.6 | 10.4 |
| Female | 9.9 | 10.1 | 9.8 | 9.0 | 7.9 | 7.6 | 8.9 | 9.6 | 9.8 | 10.5 |
| Less than 25 years | 18.5 | 19.0 | 18.8 | 17.5 | 15.7 | 15.8 | 20.1 | 21.1 | 21.4 | 22.8 |
| Between 25 and 74 years | 7.8 | 7.9 | 7.7 | 7.1 | 6.1 | 6.0 | 7.6 | 8.3 | 8.3 | 9.1 |
| Long-term unemployment rate | 4.2 | 4.3 | 4.1 | 3.7 | 3.1 | 2.6 | 3.0 | 3.9 | 4.1 | 4.6 |
| Male | 3.8 | 3.9 | 3.8 | 3.5 | 2.9 | 2.4 | 2.9 | 3.9 | 4.2 | 4.6 |
| Female | 4.6 | 4.7 | 4.5 | 4.1 | 3.4 | 2.8 | 3.1 | 3.8 | 4.1 | 4.6 |
| Very long-term unemployment rate | 2.4 | 2.5 | 2.4 | 2.2 | 1.8 | 1.5 | 1.5 | 1.8 | 2.2 | 2.5 |

No higher resolution available.
Unemployment_rate,_EU-27,_2003-2012_(%).png (734 × 166 pixels, file size: 9 KB, MIME type: image/png)

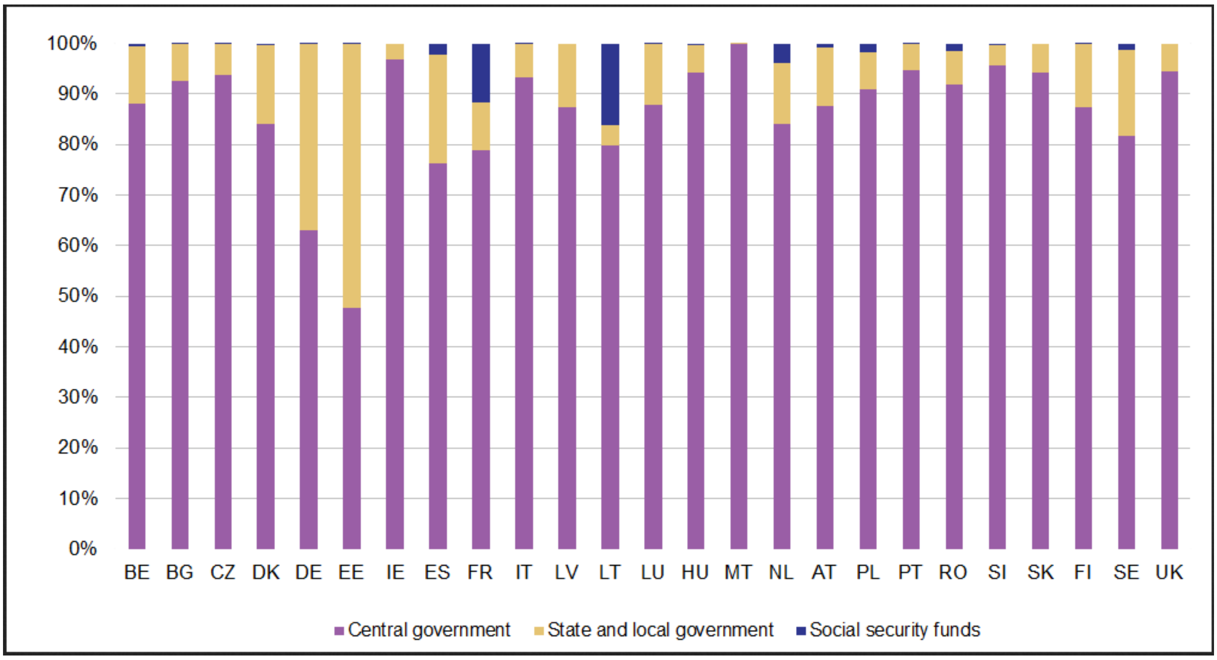
Source: Eurostat

Picture 6: Sovereign debt as % of GDP (2010 – 2011)



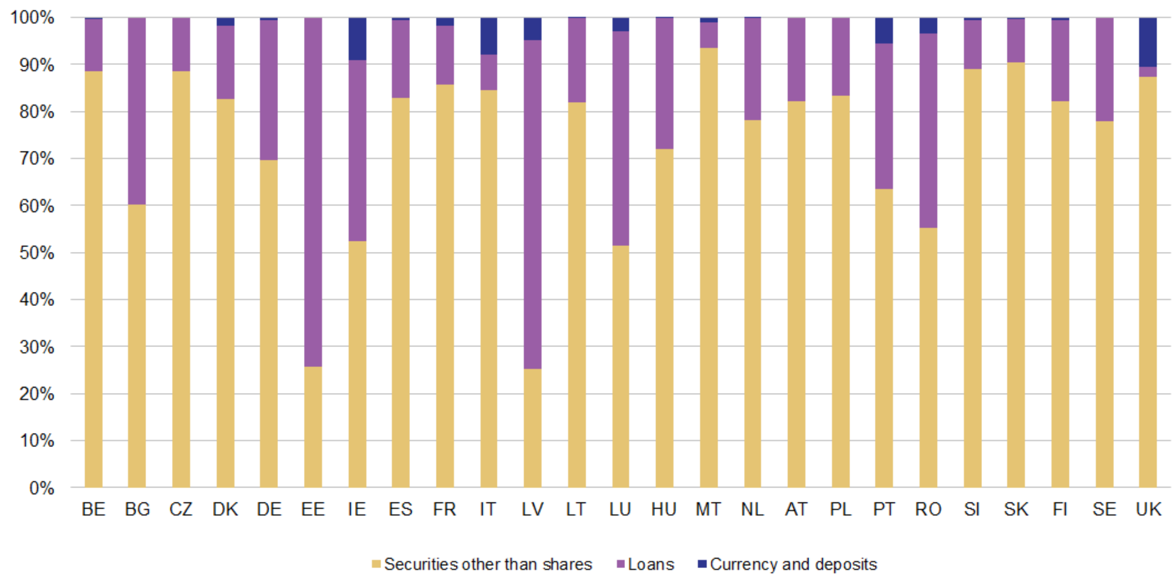

Source: Eurostat

Picture 7: Sovereign debt by subsector (2011)




Source: Eurostat

Picture 8: Sovereign debt by financial instrument (2011)



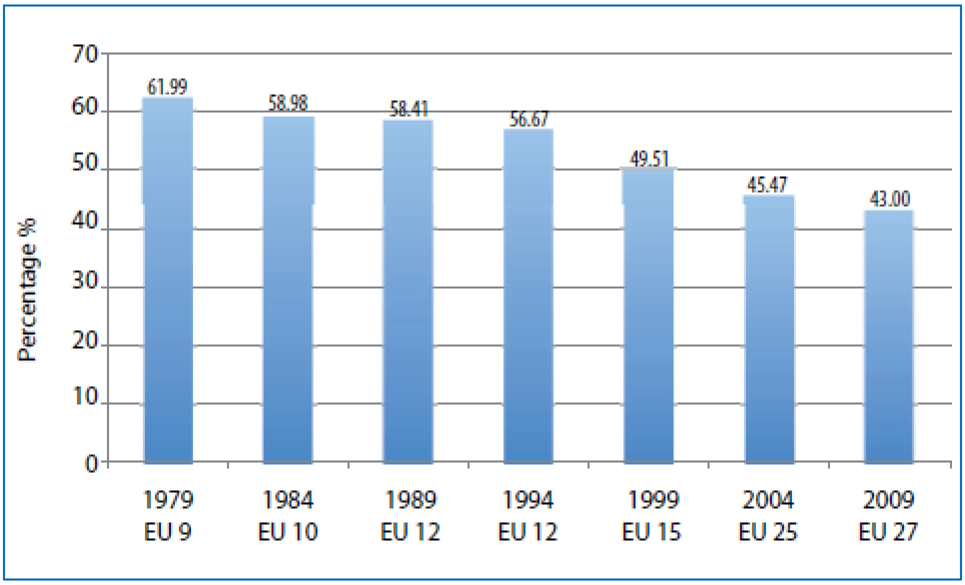

Source: Eurostat

Table 7: Voter turnout in European Parliament elections (1979 – 2009)

| | 1979 | 1981 | 1984 | 1987 | 1989 | 1994 | 1995 | 1996 | 1999 | 2004 | 2007 | 2009 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| BE | 91.36 | | 92.09 | | 90.73 | 90.66 | | | 91.05 | 90.81 | | 90.39 |
| DK | 47.82 | | 52.38 | | 46.17 | 52.92 | | | 50.46 | 47.89 | | 59.54 |
| DE | 65.73 | | 56.76 | | 62.28 | 60.02 | | | 45.19 | 43 | | 43.3 |
| IE | 63.61 | | 47.56 | | 68.28 | 43.98 | | | 50.21 | 58.58 | | 58.64 |
| FR | 60.71 | | 56.72 | | 48.8 | 52.71 | | | 46.76 | 42.76 | | 40.63 |
| IT | 85.65 | | 82.47 | | 81.07 | 73.6 | | | 69.76 | 71.72 | | 65.05 |
| LU | 88.91 | | 88.79 | | 87.39 | 88.55 | | | 87.27 | 91.35 | | 90.75 |
| NL | 58.12 | | 50.88 | | 47.48 | 35.69 | | | 30.02 | 39.26 | | 36.75 |
| UK | 32.35 | | 32.57 | | 36.37 | 36.43 | | | 24 | 38.52 | | 34.7 |
| EL | | 81.48 | 80.59 | | 80.03 | 73.18 | | | 70.25 | 63.22 | | 52.61 |
| ES | | | | 68.52 | 54.71 | 59.14 | | | 63.05 | 45.14 | | 44.9 |
| PT | | | | 72.42 | 51.1 | 35.54 | | | 39.93 | 38.6 | | 36.78 |
| SE | | | | | | | 41.63 | | 38.84 | 37.85 | | 45.53 |
| AT | | | | | | | | 67.73 | 49.4 | 42.43 | | 45.97 |
| FI | | | | | | | | 57.6 | 30.14 | 39.43 | | 40.3 |
| CZ | | | | | | | | | | 28.3 | | 28.2 |
| EE | | | | | | | | | | 26.83 | | 43.9 |
| CY | | | | | | | | | | 72.5 | | 59.4 |
| LT | | | | | | | | | | 48.38 | | 20.98 |
| LV | | | | | | | | | | 41.34 | | 53.7 |
| HU | | | | | | | | | | 38.5 | | 36.31 |
| MT | | | | | | | | | | 82.39 | | 78.79 |
| PL | | | | | | | | | | 20.87 | | 24.53 |
| SI | | | | | | | | | | 28.35 | | 28.33 |
| SK | | | | | | | | | | 16.97 | | 19.64 |
| BG | | | | | | | | | | | 29.22 | 38.99 |
| RO | | | | | | | | | | | 29.47 | 27.67 |
| Total EU | 61.99 | | 58.98 | | 58.41 | 56.67 | | | 49.51 | 45.47 | | 43 |

Source: European parliament

Picture 9: Voter turnout in European Parliament elections (1979 – 2009)




Source: European parliament

## Apenndix 2.

Interviews

**Interview questions**

1. Do you think that the budgetary norms adopted by Fiscal pact are able to recover the economies of the Eurozone given that similar norms had already existed previously (Maastricht treaty, Pact of Stability and Growth)
2. In the ESM treaty some states (namely Germany and France) possess over 20% of the voting weight. The qualified majority is 80%. Is this a good system of representation? What effects might it cause?
3. Some member states (for instance Spain, Cyprus) recently required financial aid but the ESM could not provide direct flows to them. Is the construction of the ESM appropriate?
4. Is the total lending capacity (that is 500 bln euros) of the ESM sufficient, given that the whole Eurozone's needs are much higher (considering the whole Italy's debt is about 1.5 trillion euros)?
5. The economic treaties (such as Fiscal pact, the treaty establishing the ESM etc.) were not ratified by referendum. Do you think that such treaties should be legitimized by popular vote (referenda)? How does this refer to the problem of so-called democratic deficit?
6. Private banks became very influential in the aftermath of the economic crisis. For instance, the aid given to Greece was initiated by France (because the French banks were strongly involved in financing Greece's public debt). Do you think that banks' influences in Europe might be reduced (considering the slogan 'too big to fail')?
7. The treaty establishing the banking union was signed in 2012. How will the member states react to the transfers of authority from them to the European institutions such as the ECB, the European Resolution Authority?
8. Do you think economic policies of the EU are adequate solutions for the emerging social conflicts (the occupy movement)? Should the EU's future

approach focus more on social instead of financial affairs (unemployment, lower salaries)?

**Interview with Dr. PACZEŚNIAK on July the 3rd**

1. *Do you think that the budgetary norms adopted by Fiscal pact are able to recover the economies of the Eurozone given that similar norms had already existed previously (Maastricht treaty, Pact of Stability and Growth)?*

Because dr. Pacześniak is a political scientist in European affairs, she is trying to look from the political rather than economic perspective.

All the aforementioned treaties are also political decisions that have to be made by politicians and their agreement is not so common in the contemporary European Union. For instance, the main Opposition party in Poland, Law and Justice, just recently wanted to ask the Constitutional Court if the Fiscal treaty is legal in accordance with the Polish constitution. Similar problems appeared in Germany.

So dr. Pacześniak thinks that the problem is from the perspective of the states that are beyond the Eurozone. And from the political perspective, if the Eurozone will agree on those treaties and on this particular political treaty, the Fiscal pact, because still must be ratified by all of the Member States, that's all from the political perspective.

2. *In the ESM treaty some states (namely Germany and France) possess over 20% of the voting weight. The qualified majority is 80%. Is this a good system of representation? What effects might it cause?*

From the beginning of the whole European integration, those bigger states such as France and Germany were more important and more influential, both in politics and economic issues. From the other hand, the European Union is considered in such a way to overcome the possible dictate of those larger states and usually there is not a strictly proportional system of voting, so those smaller states are somewhat over valued to increase their power or influence.

So, considering France's and Germany's potential to influence the decision making processes, such numbers as 20% or 27% for those states is not actually as high as the possible value for these states.

On one hand, this is still a matter of finding consensus between a great majority of states within the EU, at least within the Eurozone, and even by such divisions of voting ways. On the other hand, there is a danger of some blocking coalitions that would be opposed to certain decisions, those so called veto players that might appear.

> *Additional Question: Do you think that this system, at this moment is appropriate or would you rather see some other mechanisms of making it more efficient?*

The question if the rule of representativeness or the rule of effectiveness is the most important one.

So, the problem is that such a system is perceived not to be a very effective one, but if we consider the representativeness of this system it's seems appropriate, so it's a matter of deciding which rule is the most important in this case.

According to Dr. Pacześniak point of view, we are facing a crisis which was triggered mainly political, but at least also political problems to the Union as Such and..

So because of that, putting accent on effectiveness wouldn't have improved the general evaluation of the EU within the European society as such or European societies.

3. *Some member states (for instance Spain, Cyprus) recently required financial aid but the ESM could not provide direct flows to them. Is the construction of the ESM appropriate?*

It's also a matter of how large are the financial resources of the EU or at least the Eurozone as such for sending money for states such as Spain or Cyprus.

The general perception of Dr. Pacześniak is that the Eurozone of the EU is not capable to deal with the crisis, even with this European Stability Mechanism.

Especially in such cases as Spain, which is a very large economy and it must receive really huge amounts of money to recover.

Dr. Pacześniak would like to remind you the problem of political agreement, because the majority of Northern European states is not very willing to give assistance to the Southern states.

Nevertheless, in the contemporary political situation a different solution than the ESN is just impossible. That's the final answer to this question. Quite pessimistic, but quite real in dr. Pacześniak's opinion.

4. *Is the total lending capacity (that is 500 bln euros) of the ESM sufficient, given that the whole Eurozone needs are much higher (considering the whole Italy's debt is about 1.5 trillion euros)?*

The answer was partially given in the question, because from the point of view of states such as Poland the sum seems really huge, but for the Eurozone as a whole it might be not sufficient.

There is no opportunity for finding agreement for increasing the amount, so it's also a matter of politics.

5. *The economic treaties (such as Fiscal pact, the treaty establishing the ESM etc.) were not ratified by referendum. Do you think that such treaties should be legitimized by popular vote (referenda)? How does this refer to the problem of so-called democratic deficit?*

The problem with the fiscal treaties is that the technocrats are negotiating them, by a long and detailed process and it looks like that there is a rupture between technocrats and the rest of the society. Nevertheless, by such referenda, ordinary people do not answer the questions as such, but they answer them according to their trust or distrust towards their own political elites. So, the question of the referenda shouldn't be associated to the democratic deficit in the European Union and by introducing such referenda we would not improve democratic procedures in the European Union.

6. *Private banks became very influential in the aftermath of the economic crisis. For instance, the aid given to Greece was initiated by France (because the French banks*

*were strongly involved in financing Greece's public debt). Do you think that banks' influences in Europe might be reduced (considering the slogan 'too big to fail')?*

It appears that there is no agreement in the European Union on the question of who should pay for banks mistakes and wrong decisions made earlier. There is a common opinion that banks are responsible for the crisis as such and that European institutions and Member States must pay for their mistakes. There is a big difference between the situation in 2008 and the one in 2013. In 2008, the first reaction to the crisis was to give some public aid to the private companies. The recent discussions about the Banking Union should introduce a different perception, that not the whole society is financially responsible for banks mistakes, but rather the customers of those banks but also the institutions that were customers of those banks. There is much more public aid given in Europe than in the United States, but on the other hand, there is a political disagreement between technocrats and the common perception, the society. In the European Parliament, the German Socialists are more willing to improve the social policy of the European Union and this political way of action is against financing private banks by public resources.

7. *The treaty establishing the banking union was signed in 2012. How will the member states react to the transfers of authority from them to the European institutions such as the ECB, the European Resolution Authority?*

The level of euro skepticism has definitely increased recently, including some counties that were not euro skeptic, like Netherlands. There is a sort of paradox, because we expect that EU institutions should solve the problems triggered by the crisis, but in the same time, many political elites and members of the society don`t want to strengthen the competences of the European institutions and to transfer authorities from national to European level. There are contradictory arguments that EU is not effective or that it is too effective in the sense of being too powerful and this different arguments lead to the same thesis, that of an increase of euro skeptic reactions to the EU.

*What do you think is particular for euro skepticism in Central in Eastern Europe and in specially for the Polish case, because there are many ways of being euro skeptical?*

In the case of Poland, in the National Parliament there is no euro skeptic political party. The main opposition party *Low and Justice* defines itself rather as being euro critic than euro skeptic. All the political parties that were typically euro skeptic and used to be stronger after the Polish accession to the European Union are not popular anymore and usually don`t even enter the Parliament. We could speak of a soft euro skepticism rather than of a typical euro skepticism in Poland. The great majority of the Polish society supports the integration, but there is an exception, because joining the euro zone is very unpopular in Poland. There is a sort of tiredness, of disappointment of the Polish society, that can`t really be defined as being only a euro skeptical reaction. It`s mostly an awareness of the fact that the accession to the European Union didn`t solve many internal problems.

8. *Do you think economic policies of the EU are adequate solutions for the emerging social conflicts (the occupy movement)? Should the EU's future approach focus more on social instead of financial affairs (unemployment, lower salaries)?*

The EU should focus on social issues rather than on financial affairs. If we consider austerity measures, this approach is not the proper way to cope with the crisis. The problem of unemployment, in especially in the Southern countries, is the most important and urgent for Europe and this is regardless of being more leftwing or rightwing oriented. The last European Summit was concerned with the problem of unemployment, so it looks like EU is at least aware of this problem. Nevertheless, the MEP are more concerned by discursive questions, like how to speak about Europe, in the context of next year`s elections than by the real problems.

The occupy movement will be more visible in societies that are more political oriented, like Spain or France, that in Central and Eastern Europe (in spite of the social problems and inequalities), who are not that that capable of mass mobilizations and large-scaled protests.

*How could you predict the importance of the social question, in specially the problem of youth unemployment for the MEP in the context of next year`s elections?*

The populist parties will point out that the mainstream in Europe is not capable to solve the problem of youth unemployment. Most probably, in the next years, we will face more radicalism, both leftwing and rightwing oriented.

*Could you predict a revival of the left in the context of the crisis?*

Al the EU level, the mainstream left, the so-called social democracy didn't come to any solutions to cope to the crisis. The crisis of the left is complex, it started in the early 1990, when the mainstream left started to use the neoliberal language and paradigm, mainly because of the so-called Third Way. We could see that neoliberalism appeared to be the wrong solution for the economy as such, so it should be criticized and the problem is that social democracy is not capable to do this. We could speak of an electoral crisis of the left, because in the last elections at the EU level and also at the national level, the left wasn`t very successful.

**Interview with Dr. KLIMOWICZ on July the 3rd**

1. *Do you think that the budgetary norms adopted by Fiscal pact are able to recover the economies of the Eurozone given that similar norms had already existed previously (Maastricht treaty, Pact of Stability and Growth)*

When you look at the previous treaties, the creation of the Eurozone, the TSCG, they are based on economic issues but are matter of political decisions. So, the Fiscal compact is again based on economic issues, strategies but is still a political decision. The biggest problem is that if MS accept the rules the first question is Are politicians aware of what they are signing, are they aware if they will be able to fulfil the conditions. Because of the crisis inside and outside the countries there are many circumstances that can make the economic system unstable. The second thing – if you look on the creation of the Eurozone and take Greece as an example, every economist will tell you that even if you sign an agreement you can cheat. Given that pacts are a political decision, even if there are some countries that are unable to fulfil some of the conditions, we will find a solution to solve these problems. In my opinion the main strategy in the EU to fight the crisis is to integrate – deeper and stronger integration, because we have the fiscal pact, because we have the banking union. I don't think that the fiscal pact is a solution for another crisis. But it is a step towards deeper integration. The Fiscal Pact is connected not only with the crisis, but with the public debt. The crisis was the reason for the fiscal pact, but not the only one, it was discussed before the crisis. In general, I don't think similar norms for all the countries are a good solution.

*Additional question: Austerity measures are linked with the lack of social funds. Do you believe austerity to be the best option?*

No, I don’t believe. Money earns money. You don’t need to save it, but rather spend it, earn it. There is no economic theory that says that austerity is a good thing even for persons, as individuals, nor for countries. Greece is quite a good example. The problem was in ranking – it was really low, so they couldn’t loan more money from the financial institutions. So the purpose was to show that they were more stable, in order to loan more money. So, for a short period of time, that could have been a good idea. In a long term perspective, such a strategy in my opinion wouldn’t work, neither for the companies, not the citizens, because you need money in order to make them.

2. *In the ESM treaty some states (namely Germany and France) possess over 20% of the voting weight. The qualified majority is 80%. Is this a good system of representation? What effects might it cause?*

I would agree with this representing system if we say that the EU is an economic zone. In such a case, if giving more decision powers to big states would be explainable because they have stronger economies. EU wasn’t created this way. It was created as an equal partnership of countries. The current system of representation gives much power to big countries, rich and with stable economies countries – France, Germany and Great Britain.

*But Great Britain has a high public debt.*

The public debt is not a problem because it is the money that the countries needs for development. But if you start having problems, you will never find a solution. You are looking for money to pay the debt.

Back to the question, I don’t think the representation system is a good one because in the EU most of the countries are small ones, they are not stable, they are never going to be stable, because the EU is too large, you have a lot of countries and there are two or three big countries. So, small countries don’t feel represented. That is what the Greek people says – the decisions made on the EU level, they are not their decisions they are the decisions of Germans. So, they feel like German slaves.

*Additional question: Is the current system of representation better in terms of effectiveness?*

I don’t think so. If you have a good plan, you could be effective. This kind of representation gives more power for solving the problems to those who even don’t need a plan, if they are stable. If they listen to those who have problems and maybe their ideas, that would be effective. But if you look at Greece and the strategies of the different funds and the conditionality to get them, this is not a way to solve problems of the poor countries, because they are not involved in the process of decision making.

3. *Is the total lending capacity (that is 500 bln euros) of the ESM sufficient, given that the whole Eurozone's needs are much higher (considering the whole Italy's debt is about 1.5 trillion euros)? Maturing of Debts*

I think that the idea of the European Union in solving the crisis is to give money, not to give any ideas how to do it, how to cope with it. Because I think that none of the European institutions have an idea about how to cope with the crisis. The only idea is to give money, to survive and maybe we will find a plan. Giving money to financial institutions, whose purpose is to earn money is bad idea.

4. *The economic treaties (such as Fiscal pact, the treaty establishing the ESM etc.) were not ratified by referendum. Do you think that such treaties should be legitimized by popular vote (referenda)? How does this refer to the problem of so-called democratic deficit?*

If we talk about democracy, this [referenda] is the best solution. If you have a democratic country, I think that the voice of the citizens is the most important.

*But what about the populist discourse?*

In the democratic system, populism is always there.

The more you understand, the better decisions you will make. Secondly, and this is an idea from history, when you ask a poor person what he is thinking of the future he would say that everything is good for him is good for the country, that's why you have the populists. They can say everything and if you believe them you will say it's a good idea. If you have a very good education system, from primary school, you will create a very conscious society. Then the democratic system is the best solution.

When you have authoritarianism the things work, people have jobs. In Russia, you have oligarchy and it doesn't work. This is a cultural question. Not asking the citizens is not a good idea. You need to ask them.

5. *Private banks became very influential in the aftermath of the economic crisis. For instance, the aid given to Greece was initiated by France (because the French banks were strongly involved in financing Greece's public debt). Do you think that banks' influences in Europe might be reduced (considering the slogan 'too big to fail')?*

Not the financial system in itself, but the system of financial institutions. When you look what happened with the European countries, Greece, Spain, Portugal, we have the rating agencies, which are financial institutions and rate the economies. In the case of Greece, the rating was so low that the country couldn't get a loan anywhere. European Union gave money to the financial institutions, not to the country. These institutions became stronger and the rating went up. After the report of the European Union, the rating went down again, at the point which EU gave even more money and the rating went up again. For me, this is a strategy for financial institutions. The stategy is creating a strong financial system of financial institutions, not strong countries.

6. *The treaty establishing the banking union was signed in 2012. How will the member states react to the transfers of authority from them to the European institutions such as the ECB, the European Resolution Authority?*

As far as I know, Poland has the strongest system of monitoring and controlling the banking system. Rules that are presented in the banking union are not that strong and don't give so much power to the European institutions. If you would like to supervise the banking system, you would have to create strong norms to control it.

*Additional question: Why only the big banks and not the medium banks?*

The big banks have the biggest influence. The banking system is created for controlling all banks, but when you look at the Polish system for example, 70% of banks are not Polish, they are especially from within the European Union. If we don't sign the banking union treaty, we will lose the control over 70% of banks. If we sign it, we will have control over all the banks, but the control would be I think less effective. If we create a quite good system to control the banking system, maybe we will prevent the influence of the financial institutions.

*Can a European ranking system, such as that proposed by the president Sarkozy, be an option?*

Yes, but it takes 20 years to create it. All the institutions that create the ratings are from the United States, but they are not connected to the USA, being transnational. I think that their aim is not national stability, but earning money. So creating such ranking would be an option. But after the creation of the system it would be quite difficult to maintain a new public or private institution. And most times it could give a similar rank as the American institutions. It could be a good option to do it, but I would ask about the conditions, how will be the rating created.

7. *Do you think economic policies of the EU are adequate solutions for the emerging social conflicts (the occupy movement)? Should the EU's future approach focus more on social instead of financial affairs (unemployment, lower salaries)?*

One of the solutions of the European Commission was to socialize the public tasks. What are they creating right now is a system of not private but social enterprises that would support the social policy and social institutions of the European Union. There is a focus on social issues in the European Union. The problem still is money, how to do it and who can do it. If not the public institutions, because they don't have money due to country debts as in the case of Spain, Greece, Portugal, which for a long time would not have money to create programs focused on social problems and to support those programmes there is a need for some institutions which would be useful and which would help the institutions to focus on the social issues. The problem is money for strategy. I think good examples are Spain and Greece, because they are the only countries which have created a pact of social enterprises because the biggest problem is the flexible labour market. So if there are not small and medium enterprises which could create new jobs, we need to create a new sector which could be quite good for implementing solutions and would create new jobs.