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The Eurozone Crisis:
Implications for Central and Eastern Europe

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The eurozone crisis in perspective: causes and implications

Abstract: The eurozone crisis, apart from revealing serious institutional weaknesses in the structural design of the Economic and Monetary Union (EMU), has also highlighted the limits of the EU and its member-states to act efficiently, swiftly, and comprehensively to address the problems at hand. A number of vicious feedback effects that the crisis fuelled resulted in unwelcome political and economic developments spreading beyond the eurozone. The objective of this paper is to shed some light on the causes and the ways of addressing the crisis in the euro area. Against this background, the diverse correlated implications of the eurozone crisis for the EU member-states, for the EU institutions, and possibly for the future of the EU itself are discussed.

Keywords: eurozone, crisis, EU, economic governance, CEEs

The eurozone crisis that has been unfolding for more than two years now attracts enduring attention worldwide. The situation of emergency and the need of addressing it forced the European Union (EU) leaders to seek ways of navigating the crisis. As time passed and the crisis spread, the limits to the current form of governance and policy coordination in the EU became striking. In this sense, the eurozone crisis, apart from revealing serious institutional weaknesses in the structural design of the Economic and Monetary Union (EMU), has also highlighted the limits of the EU and its member-states to act efficiently, swiftly, and comprehensively to address the problems at hand. This incapacity to act efficiently is reflective of a number of problems inherent

in the current design and ways of functioning of the EU, whereby the most important of them is poor governance structure. The poor structure of governance fuels a number of vicious feedback effects resulting in diverse unwelcome political and economic developments spreading beyond the eurozone.

As a means of introducing the reader to the following papers included in this volume, the objective of this essay is to shed some light on the causes and the ways of addressing the crisis in the euro area. Against this background, the paper dwells on the diverse correlated implications of the eurozone crisis for the EU member-states, for the EU institutions, and possibly for the future of the EU itself. The argument is structured as follows. In the first section the overlapping causes of the crisis are outlined. In the following step, the actions devised at the EU-level aimed at addressing the manifestations of the crisis are mapped. A discussion on the variety of implications of the crisis follows.

1. The overlapping causes of the crisis

It is quite common in the literature to seek a direct connection between the global crisis of 2007-2008 and the crisis in the eurozone. Although the global financial crisis has had a profound impact on the euro area, it has merely unveiled the pre-existing problems nurturing the European economies and made the weaknesses inherent in the design of the EMU more apparent. It is not to say that the EMU is a failure; quite the contrary. The EMU proved resistant to a number of external shocks that it has incurred since its inception. Moreover, "the EMU actually delivered what it promised: price stability for a long period, i.e., over 13 years. Criticisms blaming the single currency for what it is not constructed for, or which is not to be influenced by monetary policy, are therefore misdirected"[1]. In this view, what matters in a discussion on the causes of the crisis in the euro area is what kind of weaknesses the global financial crisis has exposed and what the connection between them is.

1 L. Csaba, *Perspectives for the eurozone: Consolidation, Collapse or Muddling Through?*, [in:] E. Latoszek et al. (ed.), *European integration process in the new regional and global settings*, University of Warsaw Press, Warsaw 2012, pp. 77-78.

On a country-specific level the global financial crisis exposed a number of diverse long-standing economic policy problems. Here the contrasting cases of Greece and Ireland could be mentioned[2]. At the eurozone-level, the crisis revealed structural imbalances that exist among the European economies, divergence in their economic performance and competitiveness, as well as grace balance-of-payment imbalances. At the EU-level finally, the global financial crisis revealed, on the one hand, that the economic growth model pursued by the majority of the EU member-states is unsustainable and does not promote growth. On the other hand, it proved that serious drawbacks in the implementation of the single market agenda halt back the European economy as a whole and limit the elasticity of markets to react to situations of distress.

That the weaknesses exposed by the global financial crisis led to a full-scale crisis in the eurozone has to be attributed to faults in the institutional design of the EMU. Five factors should be mentioned here. First, since its inception, the EMU did not fulfil the requirements for an optimal currency area, and according to many commentators it should have failed a long time ago. Second, that the monetary union was not accompanied by a fiscal union[3] was considered a major weakness of the EMU. Third, the implementation of institutional solutions instated to balance up the lack of a fiscal union, such as the Stability and Growth Pact and the accompanying surveillance mechanisms, was spotty, inconsistent and thus inefficient. Fourth, the euro-area banking system remained very fragile and overly exposed to government debt and to the risk of under-capitalization. What made the four correlated root-causes of the crisis break out simultaneously is, fifth, a poor structure of governance[4] in the euro area, and possibly in the EU as a whole. The poor structure of governance could be defined as an "insufficient ability to make authoritative policy and political decisions for the region as a whole"[5]. As the practice of handling the crisis suggests this inability to

2 See e.g., A. Visvizi, *The crisis in Greece and the EU-IMF rescue package: determinants and pitfalls*, Acta Oeconomica, Vol. 62, No. 1, pp. 15-39; and: K. Regling, M. Watson, *A Preliminary Report on The Sources of Ireland's Banking Crisis*, Government Publications of the Republic of Ireland, May 2010.

3 P. Subacchi, S. Pickford, *The Euro on the Brink: 'Multiple' Crises and Complex Solutions*, Research Paper, January 2012, Issue 7, Nomura Foundation Publication.

4 P. Subacchi, *Merkel on steroids won't work*, The World Today, August-September 2012; A. Dukes, *The Euro Crisis: Preservation of Dissolution? An existential crisis for the euro*, Working Paper 11, 2012, Institute of International and European Affairs.

5 N. Veron, *The Challenges of Europe's Fourfold Union*, Bruegel Policy Contribution, August 2012, Issue 13, p. 2.

make authoritative decisions is aggravated by an inability to recognize that country-specific political, cultural and economic circumstances and different causes underlying their respective crises beg for different approaches toward addressing the crisis.

In this sense, although feedback effects between all of the five components enumerated above exist, the poor structure of governance constitutes the most powerful factor that contributed to the escalation of the crisis in the euro area and let it spread beyond the eurozone. Greece represents a good case in point here. Even if the sovereign-debt crisis is to be associated with structural and institutional weaknesses inherent in the Greek economy and its failed state-apparatus[6], since it has not been addressed by the EU-leaders adequately, on time, and with the political sensitivity and wit required, it has definitely added to the scale and dynamics of the crisis in the euro area[7].

In short, the eurozone crisis represents a complex set of weaknesses detectable at the micro-level (domestic economic problems of the member-states), at the mezzo-level (the institutional set-up of the EMU) and at the macro-level (the economic model promoted by the EU). These weaknesses gave rise to three concurrent crises that the Euro area is struggling with at the moment. These include: a banking crisis, a sovereign-debt crisis, and a growth crisis[8]. The political crisis (or a crisis of governance) complements this list. These four crises translate in turn into four basic challenges that the EU has to deal with, i.e. the challenge of establishing a banking union, a fiscal union, a competitiveness union and a political union[9]. It remains to be seen whether the measures devised at the EU level and by the EU member states themselves will prove sufficient to pave the way toward facing these multiple challenges. The following section sheds some light on this issue.

6 K. Featherstone, *The Greek Sovereign Debt Crisis and EMU: A Failing State in a Skewed Regime*, Journal of Common Market Studies, Vol. 49, No. 2, pp. 193-218.

7 A. Visvizi, *Addressing the crisis in Greece: the role of fiscal policy*, [in:] B. Farkas (ed.), *The Aftermath of the Global Crisis in the European Union*, Cambridge Scholars Publishing, Cambridge 2012, pp. 210-239.

8 J. C. Shambaugh, *The Euro's Three Crises*, Brookings Papers on Economic Activity (BPEA), Spring 2012, Brookings Institution, Washington DC.

9 N. Veron, *The Challenges of Europe's...*, p. 2.

2. Ways of addressing the crisis

The responses devised by the EU leaders to address the eurozone crisis can be divided into three groups, i.e. financial assistance and support measures; measures aimed at enhancing economic governance in the eurozone and in the EU as a whole; and measures targeting the financial sector in the EU.

2.1. Financial assistance and support measures

Three qualitatively different sets of measures aimed directly at providing financial assistance to the EU member-states in financial distress have been implemented in the EU, initially as a response to the global financial crisis, and eventually as a means of addressing the sovereign-debt crisis (see Table 1. for details). On the one hand, prior to 2012, several member-states benefited from multilateral financial assistance programmes provided to them by the EU, the IMF and other creditors. In each case, the objectives and the economic circumstances behind the assistance varied considerably. On the other hand, faced with a lack of an independent European financial stability mechanism, and thus challenged with the (politically contingent) need to resort to the IMF's support, the EU leaders established the European Financial Stability Mechanism (EFSM) in May 2010. It was replaced by the European Financial Stability Facility (EFSF) in 2011. The European Stability Mechanism (ESM) in 2012[10], a form of a 'self-insurance' arrangement for the EMU members, complemented the EFSF in 2012.

Irrespective of the hopes and prospects that the ESM generates in view of restoring stability and confidence in the euro area, analysts stress that it may prove a double-edged sword for the EMU. "If the stability mechanism proves simultaneously too little to be effective and too large to sit easily on the political economy basis of the countries that formed it, it may ultimately become subject to the very contagion it was set up to prevent"[11].

10 A. Leipold, *Making the European Stability Mechanism Work*, Lisbon Council Policy Brief, Vol. 6, February 2012, No. 1, The Lisbon Council, Brussels.

11 A. Leipold, *Making the European Stability...*, p. 2.

Table 1. Addressing the crisis: financial assistance & support measures

Type of measure	Eligible countries	Value in billion €	Time-line	In force
Permanent measures				
European Financial Stability Facility (EFSF)	euro area member-states	440	2010, revised October 2011	2011
European Stability Mechanism (ESM)	euro area member-states	700	signed July 2011, revised June 2012	October 2012
Financial assistance programmes				
	Latvia (Dec-2008/€7.5bn), Romania (May-2009/€20bn), Greece (May-2010, €110bn), Ireland (Dec-2010/€85bn), Portugal (May-2011/€78bn), Hungary (2009/€20bn), Spain (Jul-2012/€100bn), Italy*			
Enhanced credit support by the ECB				
Securities Markets Programme (SMP)	Greece, Ireland, Portugal, Italy, Spain	211	May 2010, August 2011	
Covered Bond Purchase Programme (CBPP2)	credit institutions and enterprises	40	until October 2012	
Outright Monetary Transactions (OMTs)	member-states in need	no ex ante limits		

* European Commission, *Financial Assistance to the EU member-states*, DG Economic & Financial Affairs, http://ec.europa.eu/economy_finance/assistance_eu_ms/index_en.htm

Source: Adapted from: European Commission, *European Financial Stability and Integration Report 2011*, Commission Staff Working Document, April 2012, Brussels, 13.4.2012, SWD (2012) 103 final, pp. 47-49.

The European Central Bank (ECB) acquired a significant, yet contested, role in mitigating the sovereign debt crisis in the eurozone. Already in May 2010, via the Securities Market Programme (SMP), the ECB purchased Greek sovereign bonds, otherwise rated as 'junk'; Ireland and Portugal followed. Italy and Spain were included in the programme in August 2011. Until October 2012, the ECB run the so-called Covered Bond Purchase Programme (CBPP2) designed to improve funding conditions for credit institutions and enterprises across the euro area, and thus ease lending across the eurozone.

Finally, in what has been referred to as a desperate move to rescue the eurozone and reduce the market pressures on Italian and Spanish

bonds, in August 2012, the ECB President, Mario Draghi announced the introduction of Outright Monetary Transactions (OMT), i.e. the purchase of government bonds in the secondary market. The purpose of OMT, designed to address many of the problems of the SMP, is to safeguard an appropriate monetary policy transmission and the singleness of the monetary policy[12]. "The OMTs will cover government securities purchases, focused on the shorter part of the yield curve. Importantly, the ECB will accept the same treatment as private or other creditors with respect to bonds purchased through the OMT programme"[13]. Governments wishing to resort to OMT will be required to follow either a macroeconomic adjustment or precautionary programme negotiated with and supervised by the EFSF/ESM.

2.2. Measures aimed at enhancing economic governance in the eurozone

Given the fact that poor governance structures have been repeatedly pointed to as the major culprit behind the eurozone crisis[14], since the beginning of the crisis significant effort has been directed at enhancing economic governance in the EU (see Table 2. for details). In late 2010, the European Commission came forward with a pack of six legislative proposals (the so-called Six Pack) that aim at strengthening fiscal and macroeconomic surveillance in the EU. Supplementary regulations will apply to the eurozone member-states only. The Six-Pack has been complemented by the so-called European Semester. The objective of this policy instrument is to integrate the various surveillance procedures already in place into one policy framework allowing, on the one hand, coordination of economic policies of the EU MS, and on the other hand, ex-ante policy guidance on the member-states' budgets and structural reforms.

Careful observers of the developments in the euro area will recall the havoc caused by the Franco-German plan on – what later became – the

12 U. Dadush, *The ECB Can't Rescue Europe*, National Interest, 12.10.2012.

13 IMF, *World Economic Outlook: Coping with High Debt and Sluggish Growth*, October 2012, International Monetary Fund, p. 23.

14 See: P. Subacchi, *Merkel on steroids...*; A. Leipold, *Making the European Stability...*

Table 2. Addressing the crisis: enhancing economic governance in the EU

Measure	Objective	Applicable to euro/non-euro MS	Agreed	In force
"Six-Pack"	fiscal surveillance	All (but special provisions for the euro-MS)		Dec-11
	macroeconomic surveillance	All (but special provisions for the euro-MS)		Dec-11
European Semester	surveillance: fiscal and macroeconomic policy framework	All		Mar-11
Euro Plus Pact	economic policy coordination & improved competitiveness	Euro MS & Bulgaria, Denmark, Latvia, Lithuania, Poland, Romania	Mar-11	
Treaty on Stability, Coordination & Governance in the EMU / (incl. Fiscal Compact)	greater budgetary discipline & better coordination of fiscal policies across the EU	All (but UK & Czech Rep.) / Fiscal Compact applies only to the euro-MS	Mar-12	target: Jan-13

Source: Adapted from: European Commission, *European Financial Stability and Integration Report 2011*, Commission Staff Working Document, April 2012, Brussels, 13.4.2012, SWD (2012) 103 final, pp. 49-53.

"Euro Plus Pact"[15]. Proposed in early 2011, the Pact was adopted by the eurozone MS and several non-euro countries. The Pact's major objective is to strengthen economic policy coordination and, through a range of commitments regarding the labour market and fiscal discipline, to improve the competitiveness of the countries involved. An equally debated intergovernmental agreement, misleadingly named "*Treaty* on Stability, Coordination and Governance in the EMU", of which the most important element is the so-called "Fiscal Compact", builds directly on other European legislation already in existence. It introduces the notion of "debt breaks", obliges the member-states to a fiscal balance or surplus, and strengthens the execution mechanisms underpinning the existing fiscal surveillance procedures[16]. The variety of measures and legislative

15 See also: D. Gros, *Competitiveness Pact: Flawed Economies*, CEPS Commentaries, 18.03.2011, Center for European Policy Studies.

16 For an interesting discussion on the Fiscal Compact, see: S. Dullien, *Reinventing Europe: Explaining the Fiscal Compact*, ECFR Commentary/Analysis, 01.05.2012, European Council on Foreign Relations.

proposals aiming at improving the (economic) governance in the eurozone, notwithstanding the efficiency of the measures, remains an open question.

2.3. Measures targeting the financial sector in the EU and its reform

The eurozone crisis exposed the fragility of the European financial system, i.e. it exposed the vicious feedback loop that exists between the banks and sovereigns[17]. In order to address this weakness, the European Commission came forward with a series of legislative proposals aimed at improving financial supervision, coordination, as well as stability and governance of financial institutions in the EU. Table 3. highlights the major objectives of the Commission's legislative proposals and the institutional framework that will be put in place once the Commission's proposals have been accepted by the EU member-states[18]. Overall, the objective of the reforms depicted in Table 3. should be considered in terms of confidence-building measures. The specific institutions and mechanisms proposed or already in place seek to stabilize the financial sector, make it more transparent, more resistant to potential future shocks, and thus capable of mitigating future crises. The credibility and effectiveness of these institutions still needs to be established.

In this view the success of measures proposed by the Commission to a large extent depends on the domestic regulatory approaches to the reform of the banking system across the EU. Until now, progress toward putting banks on a sounder footing has been uneven. For instance, countries such as the United Kingdom, Sweden, and Switzerland expressed their preference to go beyond the Basel III minimum requirements to reinforce capital as a way to strengthen their banking system and reduce associated fiscal risks. In Ireland, on the other hand, "institutions are unwinding noncore assets while nonviable banks are being resolved – ultimately leading to a much leaner banking sector. Meanwhile, other euro area regulators are pushing to soften somewhat

17 IMF, *Global Financial Stability Report*, International Monetary Fund, April 2012, pp. 9-10.

18 For an insightful discussion on the design, efficiency, credibility and prospects of the new institutions underpinning the EU financial sector architecture, see: T. Tressel, *Macro-prudential Reforms in the EU: Objectives and Progress*, [in:] IMF, *Regional Economic Outlook Europe: Navigating Stormy Waters*, World Economic and Financial Surveys, International Monetary Fund, October 2011, pp. 19-21.

Table 3. Addressing the crisis: major financial sector reform

Field		Objective	Institution	Established/re-vised/proposed
financial institu-tions	financial super-vision	European Supervisory Authorities (ESAs)	European Banking Author-ity (EBA)	2011
			European Insurance & Occupational Pensions Authority (EIOPA)	2011
			European Securities Mar-kets Authority (ESMA)	2011
	macro-pruden-tial supervision	systemic risks to financial stability	European Systemic Risk Board (ESRB)	2011
	stability & gov-ernance (Basel III) of financial institutions	capital-requirements for banks & invest-ment firms	Capital Requirements Directive (CRD)	2011 (revised)
		economic risk-based solvency requirements in insurance firms	Solvency II	2013 (expected)
		mitigation of risks related to the func-tioning of the rating business	Credit Rating Agencies (CRA III) (legislative proposal)	2011 (proposed)
		problems related to financial conglomer-ates	Directive of financial conglomerates	2011 (review proposal)
		dealing with distressed credit institutions	EU bank resolution regime (legislative proposal)	2012 (expected)
		veracity of financial statements of compa-nies etc.	Statutory Audit Directive (legislative proposal)	2011 (proposed)
		statutory audit ser-vices/single market	legislative proposals	2010-2011-2012

Field		Objective	Institution	Established/revised/proposed
financial markets	efficiency, integrity, liquidity & transparency	securities markets: transparency, efficiency, security	Regulation on Market Abuse	2011 (proposed)
			Markets in Financial Instruments Directive (MiFID)	2011 (proposed revision)
		Over-The-Counter derivatives markets	European Markets Infrastructure Regulation (EMIR)	2010 (proposed)/ in force end 2012
	safety & efficiency to securities settlement	addressing settlement fails & creation of a true internal market for national CSDs	Central Securities Depositories (CSD) Regulation	2012 (proposed)
		increasing transparency	Short Selling and Credit Default Swaps (CDSs) Regulation	2011 (adopted)
Protection and inclusion of customers				
Protection and inclusion of investors				

Source: Adapted from: European Commission, *European Financial Stability and Integration Report 2011*, Commission Staff Working Document, April 2012, Brussels, 13.4.2012, SWD (2012) 103 final, pp. 53-59.

the capital quality standards and see no need to go beyond Basel III"[19]. Parallel to the regulatory effort, the idea of a "banking union" has been floated during the 18-19 September 2012 EU Summit Meeting. At the time of writing, however, it is too early to make any valid observations regarding the design, functioning and efficiency of this possible future construct.

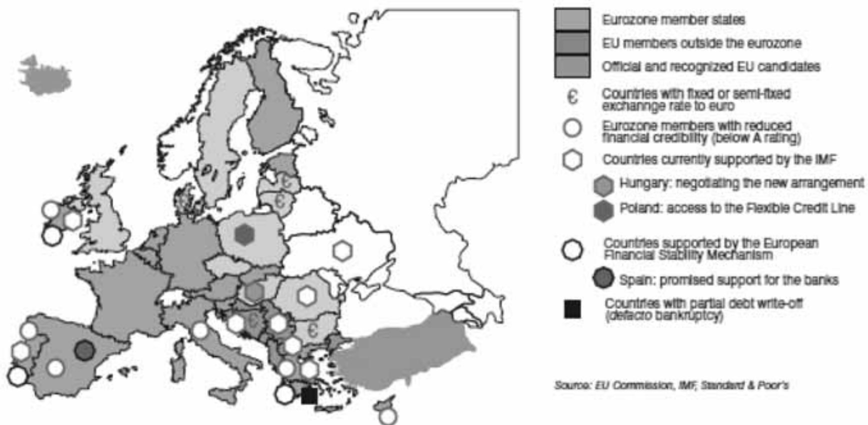
19 IMF, *Regional Economic Outlook Europe: Navigating Stormy Waters...*, pp. 3-4.

3. The variability of implications of the crisis

The eurozone crisis has had a number of implications for specific members of the euro area, for the eurozone itself, as well as for the rest of the European Union. As Graph 1. indicates, very few members of the EU have managed to avoid financial troubles being the result of either directly the global financial crisis or the four crises that beset the Euro area specifically.

While some countries found themselves on the brink of insolvency (Greece, Ireland, Portugal) and extra-ordinary measures were needed to assist them, several other countries saw their credit ratings deteriorating (Spain, Italy, Cyprus), thus causing substantial strain on external financing. As the financial troubles are not the only ones that the crisis caused, the implications of the eurozone crisis can be divided into two broad groups. These include: the economic implications of the crisis as well as its impact on the institutional structure of the EU and the balance of power among the EU member-states. The following subsections shed some light on these issues.

Graph 1. Financial troubles in Europe



Source: PWC, *Approaching storm. Report on transformation. Central and Eastern Europe and the eurozone crisis*, September 2012, p. 5.

3.1. Economic implications of the eurozone crisis

Different countries were affected by the crisis differently. Apart from the countries that were forced to request full or partial international assistance to avoid insolvency, other countries were affected either through their banking sector exposure (via the financial channels) or via secondary implications of the crisis in the form of falling demand for their exports. Whereas Greece, Italy and Spain found it either impossible or increasingly difficult to secure access to affordable external financing, countries such as Austria, Finland and Germany as well as Sweden, Switzerland and the UK have benefited from increasingly low, and sometimes even negative, interest rates[20].

As Table 4. depicts, overall the euro area is currently in recession with the eurozone unemployment hitting a record level of 11.6% in September 2012. Although a very modest recovery is in sight, the risks to the eurozone economy have not been bypassed yet. On the one hand, the results of the ECB's latest bank lending survey (Q3) suggest that credit growth is not going to support economic recovery in the euro area any time soon. On the other hand, the uncertainty related to the developments in the eurozone periphery may cause renewed negative effects on the confidence of consumers, bankers and investors in the eurozone's core. Finally, weaker global growth will cause additional strain on growth prospects in the centre of the euro area. Clearly, a more detailed analysis than the one presented here is required to assess the diverse implications of the eurozone crisis for specific economies of the area. Essentially, however, the picture that emerges gives more reasons to worry than to be optimistic about the prospects for the euro area economies.

The economic and financial condition of the euro area core has serious implications for the growth prospects in the ten Central and Eastern European countries (CEEs) that joined the EU in 2004/2007. Following a disastrous year of 2009, the CEEs have been showing positive growth tendencies (Table 5.). Still, due to their exposure to the euro as well as due to their dependence on the eurozone as their major export market, the CEEs remain highly vulnerable to the developments in the euro area. Thus, irrespective of the encouraging statistics of economic growth (Table 5.), fiscal indicators (Table 6.) call for caution when as-

20 K. Schwab, *The Global Competitiveness Report 2012-2013*, World Economic Forum, Geneva 2012, p. 24.

Table 4. Euro area: Macroeconomic indicators (% annual real changes unless otherwise stated)

	2009 (€bn)	2010	2011	2012 p	2013 p	2014 p
Private consumption	5,128	0.9	0.2	-0.8	-0.4	0.3
Government consumption	1,987	0.7	-0.3	0.2	-0.9	-0.8
Fixed investments	1,735	-0.2	1.6	-3.0	1.1	2.4
Stock-building*	-48	0.7	0.3	-1.2	-0.1	0.5
Exports	3,272	11.0	6.3	1.6	4.9	1.6
Imports	3,155	9.4	4.1	-2.3	2.9	1.4
Net exports*	-0.8	0.7	1.0	1.6	1.0	0.2
GDP		1.9	1.5	-0.4	0.6	1.7
Nominal GDP, €bn	8,917	9,155	9,410	9,512	9,725	9,804
Unemployment rate, %		10.1	10.2	11.3	11.6	10.6
Industrial production, % y/y		4.3	2.7	-2.6	2.9	5.8
Consumer prices, % y/y		1.6	2.7	2.2	1.6	1.6
Core inflation**		1.0	1.7	1.6	1.2	1.0
Hourly earnings, % y/y		1.6	2.2	2.3	2.2	2.1
Current account, bn EUR		-3.2	-1.1	33.1	21.0	17.0
Current account, % of GDP		0.0	0.0	0.3	0.7	1.0
General government budget balance, % of GDP		-6.2	-4.1	-3.7	-3.0	-2.5
General government gross debt, % of GDP		85.3	87.2	90.9	93.9	96.4

* Contribution to GDP growth (% points)

Source: Nordea Bank, *Economic Outlook: Euro area*, Nordea Markets, September 2012.

sessing the implications of the eurozone crisis and the prospects of the CEEs' economies. Domestic and external structural and political factors add to the CEEs' vulnerability vis-à-vis the developments in the EU's core.

Since their accession to the EU, the CEEs have become highly integrated with its economic and financial structures. With the eurozone serving as their major export market, the CEEs are highly susceptible to the falling demand in the euro area that may cause recessionary pres-

Table 5. The CEEs: real GDP growth (percentage change on previous year)

	2008	2009	2010	2011	2012 (f)	2013 (f)
Bulgaria	6.2	-5.5	0.4	1.7	0.5	1.9
Czech Republic	3.1	-4.5	2.5	1.9	0	1.5
Estonia	-4.2	-14.1	3.3	8.3	1.6	3.8
Latvia	-3.3	-17.7	-0.9	5.5	2.2	3.6
Lithuania	2.9	-14.8	1.5	5.9	2.4	3.5
Hungary	0.9	-6.8	1.3	1.6	-0.3	1
Poland	5.1	1.6	3.9	4.3	2.7	2.6
Romania	7.3	-6.6	-1.6	2.5	1.4	2.9
Slovenia	3.4	-7.8	1.2	0.6	-1.4	0.7
Slovakia	5.8	-4.9	4.4	3.2	1.8	2.9

Source: Eurostat, last updated 31.10.2012.

sures. In terms of their vulnerability to financial shocks originating in the eurozone, one should bear in mind two issues. Firstly, out of the ten CEEs that joined the EU in 2004/2007, three have adopted the euro (Slovakia, Slovenia, Estonia) and two (Latvia and Romania)[21] have set the national target dates to adopt the single currency. The remaining countries have their currencies linked to the euro either via currency board arrangements or via currency baskets. Secondly, the banking sector in the majority of the CEEs is closely connected to the West European banking groups. As a result, the CEEs were already affected by the deleveraging of western European banks as well as by the declining capital inflows from Western Europe[22]. Given the fact that the financial crisis in the eurozone is far from being over and recognizing the CEEs' investment needs, the declining capital inflows to the CEEs may add to the recessionary pressures. These can be aggravated by structural problems in the banking sector of the CEEs.

21 01.01.2014 and 01.01.2015, accordingly.

22 IMF, *Global Financial Stability Report: Restoring Confidence and Progressing on Reforms*, International Monetary Fund, October 2012.

Ironically, rather than making the CEEs more immune to economic and financial shocks, the single market has served as a transmission belt of the financial and economic troubles that beset the eurozone. Four major threats resulting from the euro area crisis have been identified as particularly challenging for the CEEs' economies. These include: the recessionary impact of the crisis in the eurozone, the limited room for the macroeconomic policy to manoeuvre in counteracting the recession, possible problems with foreign debt, and potential problems in the banking sector[23]. These four threats should be complemented by a fifth one concerning the risk of political reform drift as the examples of Romania and Bulgaria indicate.

On a positive note, "given the still large income differences between emerging and advanced Europe, there remains significant scope for further catching-up with advanced Europe, but it will not be automatic. It is contingent on a combination of sound macroeconomic policies and structural reforms that help ensure balanced growth and rising potential"[24]. This is particularly true as the CEEs lag behind the countries of Northern and Western Europe in terms of competitiveness. Nonetheless, as the most recent Competitiveness Report indicates, "the traditional distinction made between the 15 original members and the 12 countries that joined after 2004 does not hold from a competitiveness point of view"[25], thus indicating a relative improvement of the CEEs' position vis-à-vis the South of Europe[26].

3.2. The eurozone crisis and the EU's (institutional) balance of power

As the preceding discussion on the measures undertaken at the EU-level to contain and to address the crisis suggests, an 'emancipation' of the ECB is apparent. Although at the early stages of the crisis fears were voiced that the ECB would lose its independence, today it is obvious that the ECB has not only succeeded in defending its unique status but it has also extended the space of the politically possible in its political

23 PWC, *Approaching storm. Report on transformation. Central and Eastern Europe and the eurozone crisis*, September 2012, p. 22.

24 IMF, *Regional Economic Outlook Europe: Navigating Stormy Waters...*, pp. 29-31.

25 K. Schwab, *The Global Competitiveness Report...*, p. 25.

26 See also: K. Żukrowska, *The global financial crisis, the eurozone crisis and their consequences for the Polish economy*, in this volume.

Table 6. CEEs: fiscal indicators (general government deficit, debt, fixed investment) % GDP

		2008	2009	2010	2011
Bulgaria	deficit/surplus	1.7	-4.3	-3.1	-2.0
	debt	13.7	14.6	16.2	16.3
	fixed investment	5.6	4.9	4.6	3.4
Czech Republic	deficit/surplus	-2.2	-5.8	-4.8	-3.3
	debt	28.7	34.2	37.8	40.8
	fixed investment	4.6	5.1	4.3	3.6
Estonia	deficit/surplus	-2.9	-2.0	0.2	1.1
	debt	4.5	7.2	6.7	6.1
	fixed investment	5.4	5.1	3.9	4.2
Latvia	deficit/surplus	-4.2	-9.8	-8.1	-3.4
	debt	19.8	36.7	44.5	42.2
	fixed investment	4.9	4.3	3.7	4.2
Lithuania	deficit/surplus	-3.3	-9.4	-7.2	-5.5
	debt	15.5	29.3	37.9	38.5
	fixed investment	4.9	3.9	4.6	4.4
Hungary	deficit/surplus	-3.7	-4.6	-4.4	4.3
	debt	73.0	79.8	81.8	81.4
	fixed investment	2.9	3.1	3.4	3.0
Poland	deficit/surplus	-3.7	-7.4	-7.9	-5.0
	debt	47.1	50.9	54.8	56.4
	fixed investment	4.6	5.2	5.6	5.7
Romania	deficit/surplus	-5.7	-9.0	-6.8	-5.5
	debt	13.4	23.6	30.5	33.4
	fixed investment	6.6	5.9	5.7	5.2
Slovenia	deficit/surplus	-1.9	-6.0	-5.7	-6.4
	debt	22.0	35.0	38.6	46.9
	fixed investment	4.4	4.6	4.4	3.6
Slovakia	deficit/surplus	-2.1	-8.0	-7.7	-4.9
	debt	27.9	35.6	41.0	43.3
	fixed investment	2.0	2.3	2.6	2.3

Source: Eurostat, *Government finance statistics: main tables*, Eurostat, last updated: 31.10.2012.

conduct. A significant role in this regard was played by the ECB's president, Mario Draghi. Although opinions on Draghi's policy approach and efficiency of the measures he suggests are split, commentators describe him as the "commanding general in the battle to rescue the euro"[27]. It was also stressed that Draghi succeeded in establishing a division of labour between politicians and the central bank policy makers, i.e. "He has managed to tell governments: you do your job, I do my job"[28].

The central role of the ECB in managing the banking crisis as well as the sovereign-debt crisis revives the tension between the European Parliament and the ECB. As the Parliament has a strong track record as a chamber demanding more control over EU decision-making and the decision-makers themselves, it is to be expected that it will seek greater influence on the ECB in managing the crisis, especially given the prospect of the creation of a banking union in the Euro area[29].

From a different angle, the Eurozone crisis, and the responsibility attached to decisions needed to address it, in particular as regards the notion of economic governance in the EU, caused a shift in the balance of power from the Council (of Ministers) to the European Council. Referred to in the literature as "deliberative intergovernmentalism"[30], the term captures the fact that "growing policy interdependencies motivate more co-operative intergovernmentalism that relies on deliberative processes of policy co-ordination"[31]. Notably, however, the underlying logic of this form of policy co-ordination is that it is "about the representation of national interests as much as about the search for collective policy responses"[32]. In this sense, the nascent deliberative intergovernmentalism bears a promise of improving the efficiency of EU economic governance. At the same time, it is reflective of further weakening of the European Commission and a move toward forms of governance specific to federalism[33]. These developments seem to confirm the findings of the post-Lisbon research into the EU institutional structure. In this strand

27 M. Steen, *Draghi expands role in fight to save euro*, Financial Times, 31.10.2012.

28 Ibidem.

29 B. Fox, *Parliament is starting to bare its teeth on ECB*, Analysis, EU observer, 22.10.2012, http://euobserver.com/political/117946 – retrieved 23.10.2012.

30 U. Puetter, *Europe's deliberative intergovernmentalism: the role of the Council and European Council in EU economic governance*, Journal of European Public Policy, Vol. 18, 2011, Issue 8, pp. 1-18.

31 Ibidem, p. 15.

32 Ibidem.

33 See also: L. Csaba, *Hungary and the eurozone crisis: a comedy of errors?*, in this volume.

of scholarship it is suggested that the traditional balance between the supranational and the intergovernmental has been weakened in favour of the intergovernmental[34]. The crisis in the euro area has only added to this process.

In the light of the above, the questions are: what is the role of the EU member-states in managing the crisis? Has there been any change in the intergovernmental balance of power in the EU following the member-states' involvement with managing the crisis? Initially Germany was all too often blamed for taking the lead in attempting to address the crisis, with the German Chancellor Angela Merkel being the addressee of the majority of criticisms. In fact, supported by Sarkozy's France, Germany played a very active role particularly in the initial stages of the crisis when the decision on the IMF's involvement in Greece was discussed[35]. Although the German leadership did not necessarily produce the most adequate policy responses to the crisis, until 2012 very few actors on the EU political scene seemed to be able or willing to challenge the role assumed by Germany. It was not until June 2012 that Italy's Prime-Minister, Mario Monti, made a very clear attempt to build a new coalition for Europe going beyond the, by that time somewhat weakened, Franco-German tandem. In this way, in a strategic manner, Monti succeeded in opening up the space for alternative solutions (as compared to German and French views) in the debate on the future of the eurozone. In this way, the voices of the European "South" could be articulated at last in the EU-level discourses.

The way the eurozone crisis was handled at the EU-level and especially the role ascribed to the Council and the Eurogroup in the process, raised serious questions about the role and position of the non-eurozone member states in the EU decision-making process. The CEEs, remaining outside the eurozone, were particularly affected by the modus vivendi that emerged vis-à-vis the question of EU economic governance. In essence, the so-called "outs" seemed to have lost a significant part of their influence in Brussels. Overall, for the ten non-euro EU member-states – that nevertheless supported the Fiscal Compact – the

34 J. Monar, *The European Union's institutional balance of power after the Treaty of Lisbon*, [in:] European Commission (ed.), *The European Union after the Treaty of Lisbon: Visions of leading policy-makers, academics and journalists*, Brussels 2011, pp. 60-89.

35 A. Visvizi, *Rola Niemiec w Europie: od zjednoczenia do kryzysu w Grecji* [Germany in Europe: from reunification to the Greek crisis], [in:] K. A. Kłosiński (ed.), *Japonia, Niemcy – Odzyskany honor w rozwoju gospodarczym* [Japan and Germany – honour and economic growth], KUL, Lublin 2011, pp. 109-128.

worry is that they will be marginalized in the increasingly multispeed Europe[36]. "The necessary measures to save the eurozone will lead to its closer political integration. Unfortunately, from the point of view of the Poles, Czechs, Swedes and others outside the block it means the EU is becoming a two-tier club"[37].

Clearly, and it should be seen as yet another of its implications, the euro area crisis brought the politically inconvenient question of "multispeed Europe" to the surface of the political debate across the EU. Interestingly, although a defining feature of the European integration process, the pace variability inherent in the EU since its creation was a 'taboo' in the political discourse on Europe. One would expect that the eurozone crisis, and the variety of suggestions on how to address it, would force the EU leaders to engage with the meaning and the implications of the "multispeed Europe question" for the future of the European integration process. As the practice of the EU Summit Meetings suggests, the tendency remains nevertheless to sweep the question under the carpet.

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As the crisis in the euro area is taking its toll in the eurozone and beyond, several questions about the nature of the integration process itself, about the institutional structure that underpins it and about the future of the EU still need to be addressed. In this context, a more cohesive and more inclusive approach to the question of how to handle the crisis – that by now does not concern only the euro area – is urgently needed.

36 See also: K. Gebert, *Reinventing Europe: Poland and the euro crisis*, ecfr Paper, 07.02.2012, European Council on Foreign Policy, Warsaw 2012.

37 Mikołaj Dowgielewicz, vice-governor of the Council of Europe Development Bank and a former Europe minister, quoted in: The Economist, *Augustinian delay: The European Union's sixth-biggest country has a hard choice over the euro*, The Economist, 18.08.2012.