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Bachelor Thesis

(B.A./B.Sc.)

Austerity Politics in the EU:

What is Germany's impact on current Austerity politics in Europe?

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List of Abbreviations

EC	European Commission
ECB	European Central Bank
EFC	European Fiscal Compact
EFSF	European Financial Stability Facility
EFSM	European Financial Stabilization Mechanism
EMU	European Monetary Union
ESM	European Stability Mechanism
EU	European Union
GDP	Gross domestic product
IMF	International Monetary Fund
MS	Member State
RR	Reinhart and Rogoff
SGP	Stability and Growth Pact
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union
TSCG	Treaty on Stability, Coordination and Governance in the Economic and Monetary Union
VAT	Value added tax

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1. Introduction

"The experiment – German designed, German engineered and German exported – with austerity has failed." These are strong words of the journalist Larry Elliott published in The Guardian in last October. Besides the fact that not everyone within the eurozone actually is of the opinion that austerity – the current savings programs of European states in crisis - really failed and on the contrary estimates it as the only measure to get out of the crisis, by reading his statement, one might gain the impression that Germany alone is to blame for current Austerity measures prevailing in the European Monetary Union (EMU), which already caused a lot of protest especially within the southern European countries.
Before stepping further into the topic, it is useful to explain the term 'austerity'. The Cambridge dictionary defines it in general as "the condition of living without unnecessary things and without comfort, with limited money or goods, or a practice, habit or experience that is typical of this" (Cambridge dictionaries). An economic meaning of this definition can be found in the Financial Times lexicon as it describes austerity measures to "refer to official actions taken by the government, during a period of adverse economic conditions, to reduce its budget deficit using a combination of spending cuts or tax rises." (Financial Times lexicon) As already stated above, theses measures caused a lot of protest, because they led to "hefty cuts in public spending and employment, pensions and salaries imposed in […] eurozone countries struggling to contain their sovereign debt." (ibid.)

Given these negative effects, protests and Germany in the center of the accusation, it is therefore the aim of this thesis to find out, what impact Germany really had on austerity and if one actually can say that it is "German designed, German engineered and German exported". It is yet not the aim of this work to analyze austerity in general in order to find out, whether it failed or not. This discussion has the potential to fill a lot more pages. Instead, it sheds a critical light on the actual role of Germany in implementing austerity politics. The main research question thus reads as follows:

What is Germany's impact on current austerity politics in Europe?

In order to answer this question, three steps with regards to content are necessary. These steps will be made in chapter two, three and four of the thesis.
The first part is dealt with in chapter two and factual information about austerity is given. What does it actually mean and how did it come to a shift to austerity in European economic policy? As already stated above, it is not the aim of this thesis to analyze the outcomes of austerity and if it really did fail. Thus, the first part responds to the question:

Question 1: How did austerity develop since the start of the EMU and as answer to the crisis?

The second step in chapter three, which serves to answer the question on Germany's impact on austerity in Europe, is an analysis of the German position within the EMU. Hereby it is interesting to analyze its interests during the formation process of the European integration to understand its position within the eurozone, which in a further step may help to explain its position and interests during the crisis. As second question therefore it is asked:

Question 2: What are the German interests and its position regarding the EMU and the crisis?

In a third step, conclusions from the first two questions are drawn. By a combination of the factual information about austerity and the German interests and position inside of the eurozone, in chapter four it can be analyzed whether these interests had an impact on the shift to austerity in Europe after the crisis and whether Germany was able to enforce its interests. To come back on the initially mentioned quote about the German designed austerity it gets therefore asked:

Question 3: Is current austerity in Europe really German led?

Chapter fives serves as conclusion and final response to the main research question and contains a critical part on the already undertaken austerity measures, but as already stated above, more research and time is necessary to analyze the actual outcomes of austerity.

Social and scientific relevance

From a social perspective, many citizens but also governments from the periphery countries of the eurozone, which suffered most from the crisis, blame austerity and Germany's role in it to be counterproductive and forcing them into poverty by reducing the social welfare sector and causing raising unemployment. The Time states that "Germany has declared war on the eurozone" (The Times, November 23, 2011). The Spanish journalist Javier Cercas warned that the economical conditions, which Merkel forces upon his land, are unrealizable and evoke sentiments of anger and humiliation. (FAZ, July 2, 2012) As Thomson Reuters stated in the cbc News from the 30th June 2015, the "Greek economy has shrunk by more than 25 per cent since 2009 and unemployment has soared to over 25 per cent" and "the Tsipras government blames German-driven austerity for this economic disaster" (Reuters 2015). But it is not only relevant from a social perspective. From the beginning of the crisis, there is an on-going discussion among economists about the best way out of the crisis, which did not yet stop as one can see on the current case of Greece. Not a single day passes without at least a little notice about it appearing in the newspapers. It is evident that no one did find the best solution yet or at least, scientists and influencing policy makers did not come to an agreement about the best plan for the eurozone, otherwise Greece might be already out of the crisis. The purpose of this thesis is not to find the solution for the crisis, but to understand what impact Germany really had on austerity. Whether it can be blamed or blessed for its behavior can only be estimated by further analyses and some timely distance to the current policy making and economic stage of the eurozone.

Methodology

Before coming to the theoretical and analytical part of the thesis, it is necessary to describe and explain the methods, which are used to achieve the outcomes that these parts will generate. They consist of a methodology mix as a document analysis serves to answer the questions in general, which in some parts is supported by the consultation of empirical data.

Document analysis to answer the sub-questions

To answer the single questions launched in the introduction, a document analysis with qualitative approach to the documents is used. As Punch puts it, it is a method of interpretative understanding; the texts get 'directly' analyzed for meaning. (Punch 2005, p. 227) The analyzed documents are primarily scientific articles and books but also a literature review is consulted by taking in consideration newspaper articles, statements of the Government and speeches of politicians in a discursive analysis. For a better understanding of the German interests and position within the EMU and the crisis, it is necessary to analyze its economic-political behavior after the launch of the Euro and how it affected the situation of divergence within the eurozone by consulting empirical data. It helps to understand the possible motivations of the German influence on austerity.

Supporting empirical data

The data gets collected from several countries. The countries are of course Germany and in addition to it periphery countries suffering from the crisis like Italy, Spain, Greece, Portugal and Ireland.
The method to analyze the economic performance of the cases is based on quantitative data in different categories and mainly consists of describing the different economic performances of the chosen countries.
Adducted data regards the government bond spread, the Gross Domestic Product (GDP), competitiveness and current account surplus of the several countries.
The time slot chosen for the analysis lies between the beginning of the Euro in 2000 and 2014, with a special attention to what happened after the beginning of the crisis and the implementation of austerity measures in 2010. While it was tried to cope with the crisis by national measurements like for example the 'Abwrackprämie'[1] in Germany in the first years after its beginning, "[b]y the summer of 2010, then, a full-fledged austerity orthodoxy had taken shape, becoming dominant in European policy circles" as the US-American economist Paul Krugman stated in 2013.

As last point in this introduction, I want to remark that the citations used in this thesis, which originally are composed in German, are translated by me.

[1] The 'Abwrackprämie' in englisch 'car scrappage scheme' was part of a German stimulus package launched in 2009 in form of a governmental bonus for the purchase of a new car in combination with the simultaneously scrapping of the old car. In addition to its ecological benefits it was its purpose to slow down the drastic slum in the economy of the automobile industry. (Gabler Wirtschaftslexikon)

2. The development to austerity

In order to achieve an answer to the main research question '*What is Germany's impact on current austerity politics in Europe?*' the next chapters serve to answer the sub-questions developed in the introduction. The first step sheds light on the development of austerity as answer to the crisis but goes also already back to measurements regarding the beginning of the EMU. Thus, the question answered in this chapter is:

How did austerity develop since the start of the EMU and as answer to the crisis?

The Treaty on Stability, Coordination and Governance in the Economic and Monetary Union - sometimes and also here in the following called the 'Fiscal Pact' - which by some critics is commented as 'austerity forever', can be seen as the most recent decision in European policy making regarding the integration of the EMU. It stands at the end of the coordination of the European economic policy, which began with the Treaty of Maastricht and went over the Stability and Growth pact (SGP), which got revised in the Lisbon Strategy. In order to understand current austerity politics, in this section, these regulations, which served to build up and deepen the EMU, get depicted in their historical succession. Starting with the Treaty of Maastricht it goes over to the SGP and the Lisbon Strategy as measurements before the crisis. After a short section about the crisis, which gave also way to the Europe 2020 Strategy, the Fiscal Pact gets exposed.

Treaty of Maastricht

The treaty of Maastricht got signed as the 'Treaty on European Union' (TEU) on February 7, 1992. It was placed on the side of the Treaty of Rome from 1957, whose name got changed to 'Treaty on the Foundation of the European Union' (TFEU) and the EU was founded as superior alliance for the European communities, a common foreign and security politics and collaboration in the areas of justice and internal policy. (Stützle 2013, p. 245) The EMU was determined in art. 2 TFEU: The EMU, a common market and common politics should act as measurements in order to achieve the goals of the community, which as formulated in art. 2 TFEU contain of the harmonic, well-balanced and sustainable development of the economic activities. (ibid. p.245f) In addition to general claims of the treaty like the liberalization of money and capital flow and the arrangement of independent central banks in the MSs, concrete convergence criteria had to be followed. (ibid. p. 247f.) They consist of a 'continuing low' inflation rate, not 1.5 percent above the ones of the three countries with the lowest inflation rate, a 'planned or public' deficit not higher than three percent of GDP and a debt level not exceeding 60 percent of GDP. (Dyson/Featherstone 1999, 439f)

Stability and growth pact

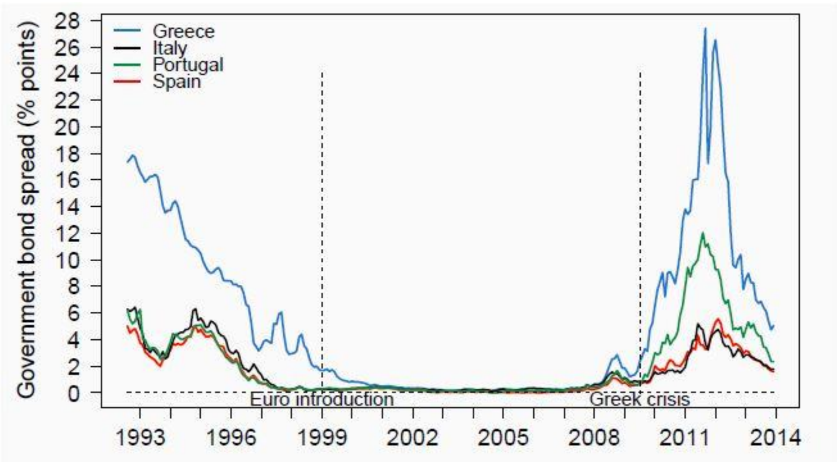
The SGP was passed in 1997 in Amsterdam and contained restrictions and directives for economic political decisions. According to Mortensen it was launched because by introducing the Euro in 1999, "some member states became increasingly concerned with the possibility of irresponsible budgetary behavior by governments once admitted in the EMU club." (Mortensen 2013, p. 7) It is based on art. 126 of the TFEU and provides the coordination of the national economic policies, which should warrant the stability of the EMU, concretizes the Maastricht criteria and determines sanctions, if these criteria get violated. (Illing 2013, 28) Thus, it is also its aim to limit public debt, but it "goes considerably beyond the Maastricht Treaty by giving the Council the competence to impose sanctions if a participating member state fails to take the necessary steps to bring an excessive deficit to an end." (Mortensen 2013, p. 7) These sanctions can be imposed, if a MS's budget deficit goes above a three percent reference value and if the MS does not take immediate corrective actions required by the Council. (ibid., p. 8) This mechanism of sanctions yet remained "a political process with only limited influence on national policy-making" as when France and Germany violated the three percent reference and ran general budget deficits in excess of this limit in 2003, "the required majority for applying sanctions was not reached" in a vote of the Council on 25 November 2003. (ibid., p. 10f)

Lisbon Strategy

The Lisbon strategy was elaborated in 2000 and envisages the strengthening of competitiveness. (Illing 2013, p. 28) It is its aim "to make the EU 'the most competitive and dynamic knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion', by 2010." While the SGP is based on the Treaty, the Lisbon Strategy is "essentially a common set of objectives to be pursued by member states within the framework of the Open Method of coordination"(OMC) (Mortensen 2013, p. 12). The OMC is an intergovernmental method, which should create peer pressure as MSs are evaluated one by another. (Summaries of EU legislations) It also contains some other differences in respect to the SGP like the fact that the European Commission (EC) got strengthened compared with the MSs and newly can enunciate premonitions in case of economic misbehavior. (Stützle 2013, p. 304) But as Stützle states, the crisis could not be impeded and a common strategy for Europe could not be elaborated so that reactions to the crisis were dominated by national solo attempts. (Stützle 2013, p. 304f)

Crisis

Figure 1



As first measures against the great recession from 2007 to 2009, when "US and Europe were hit by the financial crisis and subsequent collapse of private wealth and spending, deficit-financed government spending was the most effective tool for injecting demand back into the economy." (Pollin and Ash 2013) "The leading central banks flooded the financial system with liquidity", institutions of 'systemic' importance were rescued often through temporary nationalization and these measures were accompanied by fiscal stimuli which, according to the International Monetary Fund (IMF), raised government deficits by circa 2.5 percent of GDP in the advanced economies in 2009. (Callinicos 2012, p.66) But when in October of 2009 the new elected Greek government published drastically corrected amounts of public deficits, the nervousness and proneness to crisis of the financial markets rose as can be seen in figure 1. The

government bond spread[2] in percentage points compared to the German bonds did rise significantly not only in Greece, but also in other periphery countries after a long period of being on the same level like the German bonds after the launch of the Euro.
As the corrected amount of the Greek deficits caused this nervousness of the financial markets, the crisis got interpreted as a result of unsound state finances, which therefore led to the use of fiscal discipline and austerity to legitimize the - as Stützle calls it - 'belt tightening' in the scope of the help for Greece and to put the public finances under European control (Stützle 2013, pp. 331, 348) This help, which was not only provided for Greece, existed in form of the European Financial Stability Facility (EFSF) and the European Financial Stabilization Mechanism (EFSM), launched in May of 2010 and got replaced by the permanent European Stability Mechanism (ESM) in December of 2010. (Bundesregierung 2015) Germany here acts as the single biggest guarantor and guarantees for 190bn Euro of the fund containing 700bn Euro in total. (Federal Ministry of Finance 2015) These mechanisms were connected with commitments to reforms for the receiving MSs.

Austerity measures in countries in crisis

These reforms got implemented to different extents in MSs, which because of external pressure by the fear that they may become insolvent or illiquid proceeded "faster and further than agreed in their stability and growth programmes." (Bongardt/Torres 2010) Another fear that prevailed in the eurozone and can be adducted to the explanation of the implementation of strict reforms is the fear of "moral hazard"[3]. (Monastiriotis et al. 2013, p. 5) The costs of the ESM have scilicet been that incentives for fiscal consolidation got weakened. (Bofinger/Ried 2010, p. 203) In their article about austerity measures in crisis countries the Greek Monastiriotis and others give an overview on implemented reforms in Greece, Ireland, Italy, Spain and Portugal. As going out of the definition stated above, austerity measures consist primarily of tax raises and spending cuts. The following paragraph gives some examples for spending cuts and raised taxes in the above mentioned countries collected by Monastiriotis and other authors from the several MSs.

Greek received a loan of 110bn Euro in May 2010 from the eurozone and the IMF. With this and subsequent loans it had to implement a broad range of reforms and actions of fiscal consolidation. In the first Memorandum of May 2010 these were for example that wages in public utilities were cut initially by three percent, value added tax (VAT) rates increased to 23 percent, additional tax hikes were imposed on property, luxury consumption like imported cars and on inelastic expenditures like alcohol, cigarettes and fuel. The pension system got reformed and the retirement age was raised from 60 to 65 years, penalties for early retirements were introduced and replacement rates fro new retirees were capped at 65 percent. In June and August 2011 the Greek government introduced further austerity measures like a higher income tax rate at the upper income scale, a levy on own account workers, a new property tax and it lowered the tax-free income allowance. Additionally it introduced further cuts in pensions and bonuses. In February 2012, following the negotiations for a

[2] Bond spreads describe the differences between the yields of two bonds, which have different credit ratings. Hereby a standard risk-free Treasury Bond (in this case Germany) is compared with corporate bonds with a certain amount of risks. The spread indicates the additional yield that can be earned from the bond with the higher risk. (Investorwords 2015)
[3] Moral hazard in insurance does mean the chance that the insured may increase the potential of claims on the provider by being more careless and taking more risks because he or she is protected. (Financial Times Lexicon) In the crisis context states in crisis which got loans from the eurozone and the IMF might stop cutting public spending because they are secured by the rescuing money.

second bailout package, the reforms foresaw a cut in public sector employment and further taxes on property and a cut of a number of social benefits in key sectors such as health and social security were introduced. All in all according to Monastiriotis, "between January 2010 and January 2013, pensions and public sector pay have declined by over 25% on average, effective tax rates have increased perhaps by more than 20%" (Monastiriotis 2013, p. 4ff) In the current debate around the "Grexit" – the exit of Greek from the eurozone – new austerity measures in order to achieve the last rate of the second bailout package are in the center of the discussions between the Greek government and its creditors. With the announced referendum for the Greek population on the 5th July 2015 and the discontinued negotiations on the 26th June 2015 it remains dubious whether there will be further austerity measures implemented.

Ireland entered to the troika's[4] loan program in December 2010. The troika's requirements are an addition to an "ex ante fiscal effort undertaken by the Irish government between 2008 and 2012". Especially through indirect measures like an increase in VAT, the average tax take has increased for all households, in 2009 and 2010 public sector pay of the government was cut by a total of 15 percent on average as well as social welfare payments at a comparable rate. This was due to a reduced number of employees with the biggest losses in the health and education departments. (Monastiriotis et al. 2013, p. 9ff)

In May 2011 Portugal took part in the EU and IMF loan program by 78bn Euro and in return signed the Memoranda of Understanding after negotiations with the troika. It included 222 action items to which more austerity measures were added by signing several new Memoranda since then. These austerity measures were for example increases in VAT rates, property taxes and personal income taxes, increases in fees to access public services like hospitals, the court and public highways, and spending cuts in the educational systems by trimmed school curricula and increasing school class seizes because there were nearly 10.000 fewer school teachers in 2012/2013 than in 2010/2011. In addition, public employee and pensioner wage were cut by 14 percent. (ibid. p. 28f)

Not only the states that take part in loan programs, but all "countries of the EU periphery that are currently in crisis [are required] to undertake sharp fiscal corrections within a tight framework" by the official EMU policy. (ibid. p. 13) This was due to the fact that in 2009 most of the countries within the eurozone exceeded the deficit ceiling of three percent determined in the convergence criteria and the EC made recommendations for the periphery countries to consolidate their budgets. (ibid. p. 23)

In Italy therefore pension reforms were implemented in December 2011, whereby the statutory retirement age increased and the amount of pension benefits got reduced. The VAT increased by one percent and the taxes on real estate exalted. Spending cuts were made in all sectors. Education and health care contributed to rationalization efforts in public spending mainly through efficiency gains. (ibid. p. 14ff)

In May 2010, the fiscal adjustment measures started in Spain. Measures were for example the rise in VAT, the suppression on the salary bonuses for public employees, a pension reform, the reintroduction of the wealth tax and a "reducing of expenditure mainly via the reduction of public investment, which has decreased by 60%" from 2009 until 2013. (ibid. p. 23ff)

The above listed austerity measures in some of the periphery countries of the eurozone have been implemented because of the acute crisis prevailing in these countries and as required reforms in

[4] The troika consists of the three institutions European Commission, International Monetary Fund and European Central Bank (Monastiriotis 2013, p. 9)

order to get money from the ESM in the cases of Greece, Ireland and Portugal. However, as answer to the crisis, the EU launched a bunch of regulations to reinforce the economy, which get exposed in the next section.

Measurements in crisis: Europe 2020 Strategy, ‘Six-pack’, ’two-pack’, and European Fiscal Compact

To exit the global economic and financial crisis, the Europe 2020 Strategy has been designed and received go-ahead from the Spring European Council in 2010. Its aim is it to promote sustainable growth in the EU by reinforcing economic policy coordination and as the revised Lisbon strategy of 2005, it builds on the objectives and toolbox regarding growth and jobs and makes use of the same governance framework. The nature of growth envisaged by the EU is smart growth, sustainable growth and inclusive growth in the areas of employment, education, social inclusion, research and development and climate and energy. A combination of the different types of growth with the five headline targets leads to seven flagship initiatives for Europe’s long term growth. (Bongardt/Torres 2010)

On the regulative level of the eurozone, the EC presented the ‘six-pack’ on 29 September 2010, which got finalized by the Council, the EC and the European Parliament on 20 September 2011 and consists of a package of five regulations and one directive “aiming at reforming economic governance and strengthening the framework for preventing excessive imbalances and excessive deficits. It entered into force on 13 December 2011. The ‘six-pack’ was topped by the EC proposal of two new regulations to strengthen budgetary surveillance and monitoring on 23 November 2011, the so-called ‘two-pack’. (Bruegel 2012)

With the crisis, it became “obvious that the stipulations of the Stability and Growth Pact (SGP) did not deter EU member states from unsustainable fiscal policies” (Bofinger/Ried 2010, p. 203). Austerity measures like the ones described in the section above only have been an attempt to consolidate public finances which suffered from imbalances partly because of the crisis, partly because of financial behavior of the MSs before the start of the crisis. As can be seen in figure 2, debt-to-GDP ratios did rise in most countries of the eurozone with the beginning of the financial crisis in 2008, but has already been above 100 percent of GDP before the crisis in the cases of Greece and Italy and above the required 60 percent in Portugal, France, Germany and the Euro area in general.

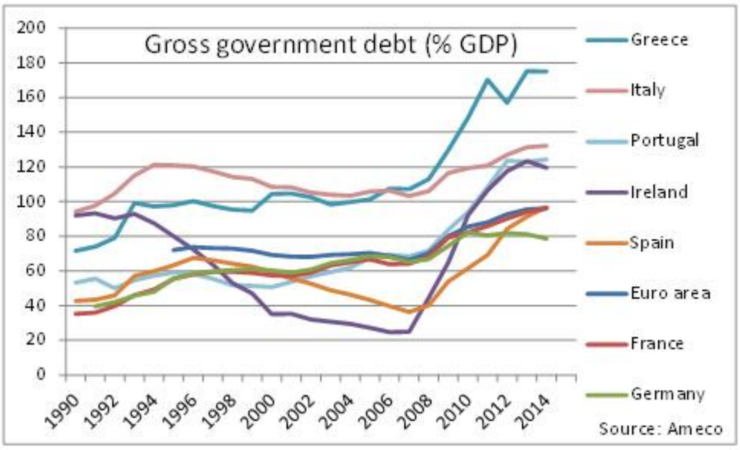


Figure 2

The aim of the fiscal pact, which came into force in January 2013, was therefore to “introduce strict observance of the quantitative criteria in the Maastricht Treaty and the SGP and to introduce more rigorous rules for budgetary discipline” (Mortensen 2013, p. 14). “According to article 3 para. 1 (a) of the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG), […] the contracting parties introduce a ‘European debt brake’ by obligating themselves to a national budget, which is either balanced or exhibits a surplus.” (Oberndorfer 2012, p. 170) Art. 3 para. 1 (b) TSCG states that paragraph 1 (a) is respected “if the annual structural balance of the general government is at its country-specific medium-term objective […] with a lower limit of a structural deficit of 0.5 percent of gross domestic product at market prices." In addition to that, art. 4 TSCG clarifies that [w]hen the ratio of a Contracting Party's general government debt to gross domestic product exceeds the 60 percent reference value […], that Contracting Party shall reduce it at an average rate of one twentieth per year as a benchmark". The contract also specifies in article 3 that these new instruments of austerity have to get anchored in the national legal systems not later than one year after the legal validity of the contract. (ibid., p. 171) Competencies for monitoring over the compliance of the treaty and the implementation of mechanisms to correct eventual deviations got transferred to the EC. (Pühringer 2014, p. 6 and art. 3 para. 2 TSCG)

The European Semester

The six-pack, the two-pack and the fiscal pact are grounded in the EU's policy-making calendar, the European Semester. This is an integrated system which ensures clearer rules, better coordination of national policies, regular follow-up and swifter sanctions for breaching the rules. Hereby "Member States discuss their budgetary and economic plans with their EU partners at specific times during the year." Plans get peer reviewed and the Commission gives recommendations to MSs in good times before they finalize decisions on the national level. MSs are also enabled to work towards the targets of the Europe 2020 Strategy. (European Commission)

Interim conclusion

Having started with the Treaty of Maastricht, over the SGP, the Lisbon Strategy, the austerity measures to cope with the crisis, the Europe 2020 Strategy, the six-pack and the two-pack, now arrived at the fiscal pact, one can extinguish the main line in all of these measures, which consists in preventing MSs to create excessive deficits. As the previous measures have not been able to keep member states public debt under the limit of 60 percent, in addition to austerity measures during the crisis, the fiscal pact got determined. It might be seen as the most binding among those measures: In addition to the transfer to national legal systems, its ratification and compliance are requirements in order to achieve money from the ESM. (Oberndorfer 2012, p. 178) Hence, the goal of budget consolidated of the SGP was not only established within the European regulations, but also as a part of the MS's national law systems in the MSs signing it. The EFC can only be brought to an end by an agreement between all contract parties because there is no regulation to stop it. (ibid. 181)
Because of the absence of such a regulation, one can talk about 'austerity forever' (ibid, p. 180). This evaluation is apparently also shared by Angela Merkel: "[T]he point is that the debt brakes get integrated permanently in the legal systems in order to prevail obligatory and forever!" (ibid, p. 181)

3. Case selection: Germany’s role in the European monetary Union

This section is attended to the interests of Germany in the EMU and the crisis. The critique on Germany does not only concentrate on its impact on the implementation of austerity, but also on its behavior after the launch of the euro. Therefore the question that is going to be answered is Q2 ‘What are the German interests and its position regarding the EMU and the crisis?’

3.1 German interests regarding the EMU

Formation of the EMU

In his book ‘Austerity as a political project’ Stützle talks about the Europeanization of the German stability culture. He describes this stability culture as a general principle concerning ‘wealthy governmental finances’ and according to him Germany used its political influence to implement it in form of the SGP for the entire EMU. One aspect hereby is the fact that the independent ECB was build up according to the example of the German Central Bank and monetary stability acts as its main goal. (Stützle 2013, pp. 292 + 294) Geppert states that this conditions and Frankfurt as the domicile of the ECB were services in return to Germany giving up the strong D-Mark in contrast to the weaker euro. (Geppert 2013, p. 69)
Regarding the convergence criteria, it is also partly due to Germany that they became less important for governments, because Germany, but also France violated the criteria of the new indebtedness of only three percent of GDP, but did not get restricted, as already mentioned above. (Illing 2013, p. 27)

Behavior after launch of Euro

One can talk about the ‘construction error’ in the process of the European integration as divergences between MSs did not get considered enough in the implementation of the convergence criteria and the missing instruments for governmental central banks to alter interest and exchange rates in order to adjust their economic processes did additionally enlarge the divergences. These divergences concern the differently developed economic potentials of the MSs within the EMU. The ‘construction error’ according to Geppert means that these differences in administration, tax and social welfare systems, the different consumer behavior and attitudes towards inflation, working, paying and tax moral have been ignored within the regulations for the EMU. (Geppert 2013, p. 67f) These differences are also reflected in the capacities to compete of the extremely efficient countries of the northern Europe and the less competitive economies of the south. (Illing 2013, p. 13) “Because the northern European states do export permanently and southern Europe imports analogically, divergences develop, which as structural disavowals led to the Euro-crisis.” (ibid.) This was fostered by the common interest rates set by the ECB, as they are by definition below what would be optimal for some MSs and above the optimum for other states. (Dullien & Fritsche 2009, p. 438f)
Indeed, the low interest rate had the effect that southern countries took a lot of cheap credits, which led to a growth in their economy wherein loans and prices rose faster than in other European countries. As it was cheaper for them to import from foreign countries, their imports raised. Through the low interest rate, credits became cheaper for southern countries and economic bubbles on pump were generated, which crashed down in the financial crisis. (Thorsten 2013, p. 34 and Scharpf 2011,

p. 326) According to Illing it is due to the high developed divergences that financial markets do not rate them sustainable anymore, what therefore led to increased interests. (Illing 2013, p. 15)

The formerly delineated gap between northern and southern countries can yet especially been formulated as the gap between Germany and the European periphery countries.
The journalist Larry Elliott states that “Europe has a problem and it is called Germany” and Heiner Flassbeck argues that “Germany strengthened its competitiveness without showing respect for damages.” (Elliott 2014 and Wehr 2010, p. 129) By these statements, they intend the behavior of Germany after the launch of the euro. Caused by the low rate of inflation, the real interest rates owing to the influence of inflation increased and the already contracting economic cycle fell to a recession. (Scharpf 2011, p. 327) Germany was yet able to raise its competitiveness: Through cuts in the systems of social assurance and measurements to stimulate the demand, the ability to compete was raised and in addition to that strengthened through declining real wages. These declining real wages led also to a raise in the exports and to less demand and therefore to less imports and a surplus was generated. (Illing 2013, p. 14) Figure 3 shows the development of competitiveness in Germany and the periphery countries Greece, Spain, Ireland and Portugal. Germany’s competitiveness was able to rise due to constantly sinking unit labor costs from the beginning of the Euro. The periphery countries yet experienced a raise in loans and prices, as the economy grew due to cheap credits as described above. This effect reached the summit with the bursting of the credit bubbles with the beginning of the crisis. The following austerity measures had the effect that unit labor costs scaled also in the periphery countries.

Figure 3

In Germany the effect of scaling unit labor costs were achieved through the policy of the Agenda 2010. In contrast to the countries with a traditional weak currency which experienced raises in loans and prices, Germany introduced longer working ours combined with partly declining real wages. (Geppert 2013, p. 71)
We might go back to the statement of Flassbeck and ask what damage he does mean that was created by Germany. Vogel names the German behavior as ‘a dumping on costs of its neighbors’. (Vogel 2013, p. 90) Boyer points this out, when he states that “the surpluses of some countries are the strict counterparts of the deficits of others.” These different levels of surpluses can be seen in figure 4. It is notably that only Germany is performing a constant positive surplus from 2002 on, which arrived at almost 8 percent in 2014. Unfortunately data for Greece and Ireland is not continuatively available, but as can be seen, they experienced negative surpluses comparable to the ones of Spain and Portugal, which had the lowest point in 2008 and afterwards raised because of the implementation of austerity measures.

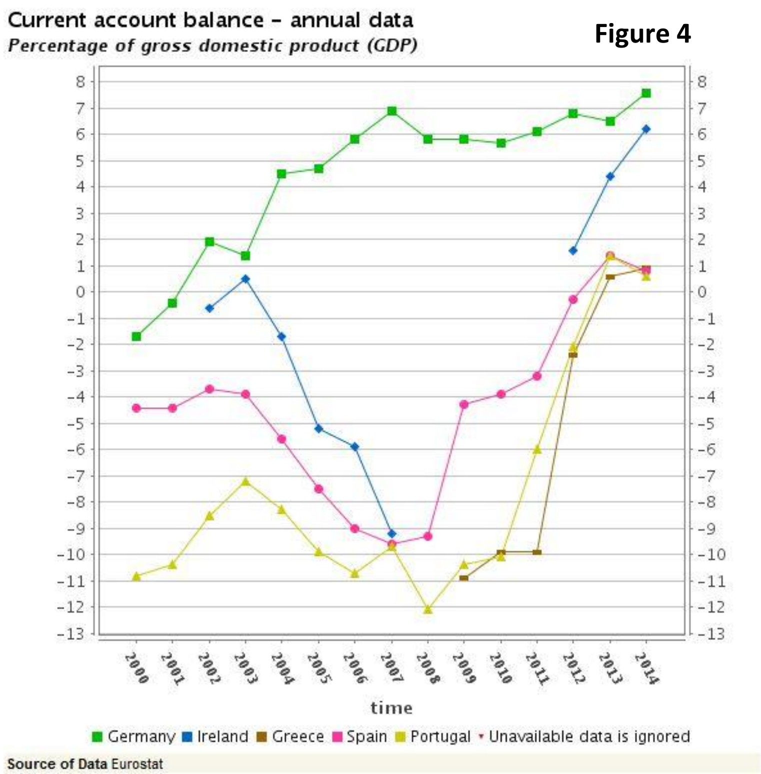


Figure 4

These differences in the current accounts might be explained by different fiscal pressure imposed on the MSs of the eurozone. Hereby it is important to notice that one of the aims of the EU is also to simplify and promote a positive competition in order to trade goods and services across the European territory in order to reflect efficiency and effectiveness in the internal market and even more on the external ones as it is stated in the Treaty establishing the European Economic Community. Fair behavior and equality in laws and regulations are a must in order to do not create market distortions and advantages for a single member due to a more favorable regulating environment. This does yet not occur considering the tax burden and the consequent inequality in costs affecting prices for the final user.

As Italy had a tax burden of 42.5 percent (Eurostat, considering both direct and indirect taxes) in 2012 and Germany had an overall of only 37.5 percent, goods considering the parity in costs of production did have a different final price. This did inevitably advantage German industries in operating business giving a considerable and consistent margin spread to be obtained and reinvested in R&D, acquisitions and expansions. This could be considered even more unfair looking at the acquisition campaign acted by German companies versus other EU member's businesses and supported from the underperforming results also due to the crisis. Thus, German productivity was able to rise and have positive effects on German exports and current account.

German can of course not be blamed for its behavior, as it did its best to become competitive through more productivity and in economic interests achieved best goals. Instead of raising loans and with them unit labor costs, periphery countries could have acted like Germany to raise their competitiveness since the launch of the Euro, but they did not. Boyer yet argues that the German strategy has only been sustainable because there existed dynamic domestic demands in the EU and the rest of the world that created space for German exports. “If all European countries were to simultaneously adopt similarly drastic austerity policies, they would only succeed in keeping the level of activity by gaining trade shares at the world level, for example with respect to the USA or Asia.” (Boyer 2012, p. 300) But the shift to austerity also in other countries, namely the periphery countries, to impose budget ‘discipline’ already started to contradict the German interest in maintaining exports: “Germany’s exports jumped sharply in April 2012, but nearly all of this went to countries outside the EU (up over 6% from last year), while sales to eurozone countries shrank 3.6% on the year.” (Hudson 2012, p. 315)
With his statement that Europe has a problem, which is called Germany, Elliott does intend that the German behavior causes the current faltering recovery of the eurozone: “[I]f Spanish, Italian and

Portuguese consumers lack spending power, they can't afford a spanking new BMW or a Miele washing machine. That means weaker German exports, lower German growth and in turn less demand for Spanish, Italian and Portuguese exports." (Elliott 2014) This problem did not only appear after the launch of the euro. Already in 1989, the former German chancellor told the former US president George Bush that the true problem is that the scissors of the economical power between Germany and the other countries of the European community are opening steadily further. (Deutsche Einheit 1998, p. 603)

It is not the aim of this work to blame Germany or the divergences prevailing in the eurozone and which were not smoothened by the European integration for causing the crisis. There are definitely also other causes, but one cannot deny the fact that the lacking European integration and economic behavior within the eurozone did have an influence on the crisis and the fact that it is still not solved.

3.2 German interests regarding the crisis

Geppert accuses the German chancellor Angela Merkel to having followed a policy of little passes and having identified Europe with the Euro by sentences like "if the euro does collapse, Europe does with it." According to him, this sentence implies that the German politics is tied to the preservation of the eurozone on all costs. (Geppert 2013, p. 133f) But it is of course not only this statement of Angela Merkel that composes the interests of Germany in the crisis.

Tranquillization of the bond market

In the course of the crisis, the bond market in Europe got more and more fragmented with periphery countries facing much worse conditions for governmental bonds than states like Germany. When the ECB decided to buy government securities on the secondary market for not violating the no-bail out clause, Germany accepted this measure so that the market became quiet again. This acceptation of the unusual measure of the ECB by the German government can be explained by the fact that it lead to a more quiet market and less financial burden for the eurozone as it would have been in the case of a collapse of southern bond markets which would also have affected Germany. (Thorsten 2013, p. 74ff.)

Interdependencies

Other interests arise from the fact that German banks and also banks of other MSs did invest in Greece and should be saved from losses. (Vogel 2013, p. 87) Therefore the possibility of restructuring Greek sovereign debt was met with total opposition of other eurozone countries, "since much Greek debt is held by euro-area banks (mainly France and Germany), which invested heavily in higher-yielding peripheral bonds" and a restructuring of the debt could create contagion effects because of large interdependencies between the banking sectors of eurozone members. (Darvas/Pisani-Ferry/Sapir 2011, p. 3) These interdependencies might break down like a house of cards in the case of a banking crash in Greece.

Stable Euro

Another concern of Germany is that it needs a stable Euro for global affairs. (Vogel 2013, p. 87) Vogel hereby intends that southern countries had less demand because of austerity programs in the crisis. This was threatening for Germany, which is after China and the USA the third biggest export nation. (Destatis 2015) German exporters therefore made more affairs with countries outside the eurozone, for which a stable euro is useful. (Vogel 2013, p. 90)

Rise in competitiveness

Not only periphery countries in crisis did implement austerity measures, but also Germany announced a fiscal consolidation package in June 2010 with the aim to cut the federal deficit by circa 1.3 percent of GDP until 2014. It is designed to reduce the deficits to a new target level by mainly expenditure-based measures, but also by additional revenues from new levies and taxes. (Roeger et al. 2010, p. 364) Through these measures Germany improves its trade competitiveness, which in the context of intra-euro area account imbalances in 2010, according to Roeger puts other eurozone MSs under the pressure to follow with structural reforms and fiscal consolidation. (ibid. p. 369) As can be seen in figure 4, the effects of austerity measures started in 2010 have indeed been that the periphery countries experienced a raise in their current accounts.

Interim conclusion: What are the German interests and its position regarding the EMU and the crisis?

As analyzed in this chapter, the main German interests and position in the EMU have been to achieve favorable conditions for its exports in the eurozone, but also to its worldwide partners. Through the policy of the Agenda 2010 it was able to become more competitive by scaling unit labor costs. The effect was that a steadily raising current account surplus was generated. As the crisis threatened to also affect Germany because of the interdependencies between the European banks and unstable financial markets, it was in the German interest to calm down the markets through implemented reforms in order to consolidate deficits in the MSs in crisis and to rescue banks in crisis to prevent that the whole system would crumble down like a house of cards.

4. Impact on implementation of Austerity

German refusal to proposed alternative measures

When the crisis hit the eurozone, a political dispute about the direction of the EU politics to manage it erupted: Southern countries expected European help and northern countries wanted the Europe of the SGP and the orientation on exports to be preserved. (Stützle 2013, pp. 322f)
During the first years of the crisis, the solution of Eurobonds got proposed. This would be "assets, which would be emitted by a European institution, for instance the European investment bank, in order to be able to grant credits for heavily in debt euro countries at a unitary and low rate" or common assets of several countries. (Wehr 2010, p. 125) Through these options, weaker countries could participate in the better conditions of stronger countries. In the case of Germany and Greece, the returns would probably lay only marginally above the favorable return on German governmental assets. (ibid.) Yet, in the beginning of 2009 the former German financial minister, Peer Steinbrück and the German government refused this solution, because it would mean considerable additional costs for Germany. (Spiegel 2009; Vogel 2013, p. 2013 and Elliott 2014) "I will not accept approvingly the degradation for German governmental assets", was his statement regarding the suggestion to create these Eurobonds. (Berger 2011) The discussion on Eurobonds was met with harsh opposition from Germany by referring to the 'no bail-out clause', formulated in art. 125 of the Lisbon Treaty, according to which it is illegal that one member assumes the debts of another. (Felber 2012, pp. 48f and Financial Times lexicon) The German influence in this debate cannot be denied, as despite many supporters of Eurobonds, they did still not get implemented due to the German opposition. But Germany was not the only state opposed to Eurobonds. The French President Nicolas Sarcozy agreed on the German chancellor Angela Merkel in August of 2011 by rejecting Eurobonds "as a short-term solution to the crisis, saying that they may come only at the end of the process of European integration." (Bruegel 2012)

Europeanization of the German 'debt brake' and pressure on other MSs to take austerity measures

Here the German apprehension of moral hazard of states in crisis can be consulted as an explanation for the harsh opposition to Eurobonds. If they would have been established, pressure for reducing government deficits would have been taken away from states in crisis at an early stage. In this case yet, Germany would not have been able to get ranged these states to austerity measures, which were in the German interests: Because of that the German government sticks to pressure on MSs in crisis. According to Vogel the German government „reigns with the markets in order to alter the societies on these markets according to its own conception." (Vogel 2013, p. 107)
As measurement against the crisis, Germany forced the budget consolidation and the German federalism commission decided in 2009 about the already above mentioned 'debt brake', which is a regulation, entrenched in the German constitution with the goal to limit government debts and which provided binding guidelines for Bund and federal Lander to reduce their budget deficits. (Stützle 2013, p. 327) This 'debt brake' was transferred to Europe, regarding the regulation that public households have to be balanced with new credits and help mechanisms get only guaranteed with the restrictions for governments to cut debts. (Vogel 2013, p. 97) These conditions are formulated in the EFC, as "only countries, which ratified the EFC and introduced national debt brakes, receive help from the ESM." (Bundesregierung 2015)
In a debate at the European University Institute the fiscal pact was widely criticized and has been characterized as a 'legal monster', but there are also more ‚balanced' views on it like the one of

Miguel Maduro, professor of European Law at the Institute, who accredits it with a political value, as according to him, European political leaders genuinely “believed that this may have a political legitimating function with respect to the national public opinions, notably in Germany.” (Mortensen 2013, p. 16) Hereby he intended the sometimes harsh opposition of the German population, which did not agree with the willingness of the federal government to provide more money for the ESM.

The argumentation with Reinhart and Rogoff

In the argumentation in favour of a shift to austerity in form of conditions for the rescue mechanisms and the debt brakes entrenched in the EFC, not only the new crisis in Greek in early 2010 after the new elected government published the corrected data on public debt is of importance. The Nobel laureate Paul Krugman states that “[i]f Greece provided the obvious real-world cautionary tale, Reinhart and Rogoff (RR) seemed to provide the math.” (Krugman 2013, p. 6) In their 2010 published study ‘Growth in a time of debt’, where the two Harvard professors Carmen Reinhart and Kenneth Rogoff measured GDP growth across varying levels of debt for twenty advanced countries over the period of 1946 to 2009, they found out that there is “no obvious link between debt and growth until public debt reaches a threshold of 90 percent.” (Reinhart & Rogoff 2010, p. 7) Beyond this threshold, according to their study, median growth is roughly one percent lower, mean growth levels are almost four percent lower. (ibid.)

But the argumentation to interpret the crisis as a crisis of sovereign debt and therefore legitimize the reduction of debt as an empirical demonstrated inevitable instrument did not just come from RR: “It is based significantly on the widespread neo-classical argumentation under mainstream economists that there exists an absolute, economic endangering highest position of debt.” (Pühringer 2014, p. 7) Yet, it was primarily RR’s research, which became influencing on the political level. (ibid.) They have been repeatedly cited by the German finance minister Wolfgang Schäuble, the president of the German ‘Bundesbank’ Jens Weidmann, the leading member of the Commission, responsible for Economic and Monetary Affairs and the Euro, Olli Rehn, the US Congressman Paul Ryan, the UK chancellor of the Exchequer George Osborne and authoritative experts such as Vito Tanzi. (Herndon et al. 2014, p. 261; Nuti 2013, p. 5; Pühringer 2014, p. 7 and Pollin 2014) Paul Krugman estimates that “Reinhart-Rogoff may have had more immediate influence on public debate than any previous paper in the history of economics” and Pühringer states that the study of RR was “one of the central fundaments of the scientific coverings of the EU austerity.” (Krugman 2013, p. 1; Pühringer 2014, p. 7) As political recommendation, RR themselves state in their study that “[e]ven countries that are committed to fully repaying their debts are forced to dramatically tighten fiscal policy in order to appear credible to investors and thereby reduce risk premia.” (RR 2010, p. 23)

In 2013 however, the student Thomas Herndon from the University of Massachusetts, supported by two of his professors, found out “that selective exclusion of available data, coding errors and inappropriate weighting of summary statistics lead to serious miscalculations that inaccurately represent the relationship between public debt and GDP growth among 20 advanced economies.” (Herndon et al. 2013, p. 257) Thus “when properly calculated, the average real GDP growth rate over 1946-2009 for countries carrying a public debt/GDP ratio greater than 90% is actually positive 2.2%, not negative 0.1% as RR claim.”(ibid. 259) Whereas the mean GDP growth rate in the calculations of RR falls from 2.8 to negative 0.1 percent when a country comes beyond the ‘threshold’ of 90 percent public debt/GDP ratio, in the recalculation of Herndon et al. it only declines from 3.2 to 2.2 percentage points. This means a miscalculation of almost two percentage points, comparing the decline of 2.9 in RR calculations in contrast to 1.0 percent in the recalculation of Herndon.

Thought the connection between low economy growth and a high amount of public debt does persist also according to the recalculated study, it is not as harsh as RR depicted it and therefore Herndon et al. conclude their paper by stating that "policy makers cannot defend austerity measures on the grounds that public debt levels greater than 90% of GDP will consistently produce sharp declines in economic growth." (Herndon et al. 2013, p. 278)
Yet, austerity policy did not change as this "final discrediting of the alleged expansionary […] fiscal contraction approach […] does not appear to have had much impact on actual policies" with the EMU countries tied to the SGP and the EFC. (Nuti 2013, pp. 8f) With the statements of the German finance minister Wolfgang Schäuble and the president of the German 'Bundesbank' Jens Weidmann in favor of the findings of RR, Germany acted as an advocate for austerity measures, which were based mainly on a flawed study of two Harvard professors.

Rejection of a global 'economic stimulus plan'

Another suggestion as a reaction to the crisis was a global 'economic stimulus plan'. According to Zinn, Europe is lacking of a willingness to approach the problem of the weaknesses in development through a governmental politic that stimulates demand. On a 'fiscal summit' in April 2009 it were especially Germany and France, which opposed such a global stimulus plan. (Zinn 2010, p. 22)

Payments for ESM

The agreement of the European leaders on setting up the ESM as permanent crisis mechanism to safeguard the financial stability of the eurozone as a whole on 28/29 October 2010 was initiated by Germany and France, as Nicolas Sarkozy and Angela Merkel on 18 October 2010 met in Deauville to agree on a permanent Treaty change, thus the future ESM, which also provided the possibility of sovereign debt restructuring. (Bruegel 2012) On 30 March 2012, the overall ceiling for EFSF/ESM lending got increased to 700bn Euro from previously 500bn Euro. (ibid.) The ESM consists of 80.5bn Euro paid-in capital of which Germany with 21,7bn Euro and guarantees of 624.3bn Euro of which Germany takes part by 168.3bn Euro and therefore acts as the single biggest guarantor and guarantees for more that one quarter of the crisis fund. (Bundesregierung 2015) With the obligated commitment to reforms in form of the signing of the EFC, Germany was confirmed that the statement of Angela Merkel about the debt brake, which should prevail obligatory and forever (Oberndorfer) was maintained. But in addition to that, by providing such a big part of the rescue mechanism, Germany can be attributed the merit of having helped the countries of the eurozone in crisis.

Interim conclusion: Is current austerity in Europe really German led?

As chapter two and three served to give factual information about the development to austerity and the German economic position and interests in the eurozone, chapter four aimed to analyze the impact that Germany really had on austerity. In combination with the previous chapters it can be asked, how the German interests do cope with austerity measures and the German impact on it.

Austerity measures have not only been undertaken by states receiving money from the ESM, but were required from all periphery countries in crisis by the official EMU politics in order to get out of the crisis. They ranged from tax increases like raises in the VAT or on property to government spending cuts for example in the health and education sector and reforms of the pension systems.

The German interests regarding its exports have already existed before the crisis. As an export nation it was its aim to become competitive by the policy of the Agenda 2010 with only low raises in wages, which became obvious in the falling unit labor costs. When the crisis also hit Germany, the federal government decided on the debt brake in 2009 and a consolidation package was introduced in 2010. By these measurements Germany was able to maintain its high level of competitiveness and receive a permanently rising current account balance, which in 2014 almost reached eight percent of the German GDP. Germany's interests during the crisis yet did not only regard the performance of the German economy, but also the eurozone as a whole. On the one hand the crisis in the periphery countries did lead to large spreads and insecurities on the bond markets, which might have also affected Germany on the long run also with regards to its global affairs. It was therefore necessary to reduce public debt through austerity measures to recreate confidence in the highly indebted countries and calm down the financial markets. On the other hand, German banks did invest a lot in periphery countries like Greece and should be saved from losses. This should be obtained by the ESM for which Germany provided more than one quarter of its funds.

Comparing the implementation of austerity measures and rescue mechanisms with the German interests, one can say that Germany was able to enforce its intensions. It successfully opposed to alternative measures like the introduction of Eurobonds or a global stimulus plan and was able to implement its debt brake to the other members of the eurozone. Hereby it is not said that Germany alone obtained its interests. Like in the case of Eurobonds, France was likewise opposed and in the debates for a second round of the ESM for Greece in January 2012 also for example also the Netherlands claimed controls for the monitoring of the national Greek budget. (Reuters 2012)

As a last point, I would like to point out the role of Angela Merkel in the matter of austerity. It seems that when writing about Germany it is often the German chancellor, which it actually of importance in decision making. The journalist Thomas Mayer calls the decision against a 'Grexit' in 2012 which was confirmed by Angela Merkel and Mario Draghi in a press conference, the president of the ECB, the 'Angela-and-Mario-Show' and credits Merkel with the role of the cook and Draghi only the role of the waiter. (Mayer 2015) In the current Greek crisis with discontinued negotiations on the 26th June 2015 and Greece not paying back the loan to the IMF on the 30th June 2015, EC president Jean-Claude Juncker made a last offer to the Greek government. "The offer would be conditional on a letter to Juncker, Eurogroup chairman Jeroen Dijsselbloem, German Chancellor Angela Merkel and French President Francois Hollande arriving in time to arrange an emergency meeting of the Eurogroup on Tuesday" (cbc News 2015). Peter Hintze, a member of her party gave the following statement in the Tagesthemen:

"One notices in Brussels, in meetings, when she enters the hall. Suddenly the other partners in Europe orientate themselves very heavily, what does she have to say in the matter? And this is partly due to Germany and its magnitude, but to a very big part due to Merkel and her ability, to create consensus just by simple, plain words." (Hintze, in the Tagesthemen 2015)

5. Conclusion

Summary of findings

The main research question on the impact of Germany on current austerity measures in Europe was split into three sub-questions which got answered in the chapters two, three and four.
In chapter two the development to austerity was analyzed. As already the regulations of the EMU contained measurements for budget consolidation like the convergence criteria o the Treaty of Maastricht, the crisis exposed the problem that there were still divergences between member states, which should be smoothened by further implementation of structural reforms in form of austerity measures. These commitments to reforms became binding for all MSs signing the EFC.
Chapter three dealt with Germany and its interest and position regarding the EMU and the crisis. Germany as an export nation is mainly interested in being competitive. It therefore needs a stable financial market, which was threatened by the crisis and the high levels of debt in the periphery countries. It was therefore in its interest to calm down the market and in addition to that rescue the money that German banks did invest for example in Greek banks before the crisis.
Chapter four then specified the impact that Germany had on austerity measures and by combining the answers to the previous two questions come to the conclusion that Germany really could follow its own interests by implementing austerity measures as it was able to transfer it's debt brake on the other MSs and did successfully oppose to different solutions like Eurobonds or an economic stimulus plan. This was not least achieved due to the leading capacity of Angela Merkel, as one of her party member fellow stated.

Reflection and suggestion for further research

When I started to think about the writing the thesis, I wanted to address the topic austerity in a more detailed way, its ideological and scientific backgrounds, its contradiction and critiques and even the outcomes of current austerity measures in Europe. This was yet not possible, on the one hand because of the limited scope of this thesis, but on the other hand also because of a lack of economic knowledge for my part. Thus, I limited the research question on only the German impact on current austerity in Europe without analyzing the outcomes of austerity and whether it was a blessing or a curse for the countries in crisis. There exists already literature addressing this question, but further time passing by is necessary to fully being able to analyze the real outcomes of the measures undertaken in the last years. Only in combination with such research, a judgment on the role of Germany in implementing austerity measures can be rendered.

Policy implications

Even if just having stated oppositional, the policy implications given at the end of this thesis contain a critique on austerity and suggest a possible way out of the crisis regarding Germany and without too severe austerity measures.

Critique on austerity

As already stated, it is not the aim of the thesis to estimate austerity. But as some European countries, especially Greece, still do not seem to recover well from the crisis, at this point a short overview about the prevailing critique on austerity should be given.

Boyer argues that austerity does not deal with the origins but only with the symptoms of the doubts of the financial community about sovereign debt levels of governments hit by the crisis. He interprets these symptoms as the "consequence of the absence of any significant redesign of European and domestic institutions after the launch of the euro." (Boyer 2012, p. 290) By the launch of the euro the rate of interest declined for countries with a formerly weak currency, firms and households had easy access to credit, what led to a fast growth. But as the instrument of adapting interest and exchange rates was not longer available, governments could only use measurements of public spending and taxation to respond to domestic imbalances, which in consequence led to persisting public deficits. Austerity policies aim to fight this symptom of public deficits, but they "do not address the underlying productive imbalances created by real-estate bubbles" and even exacerbate the gap between potential production and effective demand, while they cause social and political opposition by forcing governments to reduce welfare and public services and argument direct or indirect taxes. (ibid. pp. 290f)

Another point of critique is that austerity started too early. As already described above, during the great recession from 2007-2009 deficit-financed government spending was the most effective tool for injecting demand back into the economy. (Pollin & Ash 2013) In the end of 2009 one might have expected a second round of stimulus, because the situation had stabilized, but Krugman states that the "crisis was deeper than policymakers had acknowledged, and likely to prove more persistent than they had imagined." But the newly aggravated crisis in Greece in early 2010 and the research from RR led to a shift in policy-making towards austerity. MSs in crisis got only admitted to receive European rescuing money, when it goes along with measurements for the consolidation and monitoring of their public finances. (Stützle 2013, p. 327) Later on, this commitment to austerity found its entrance to the constitution of every MS which signed the EFC.

Even if Herndon et al. found out that RRs research is not reliable because of the illustrated errors, they don't suggest that governments should be free to borrow and spend profligately, but they state that "government deficit spending, pursued judiciously, remains the single most effective tool we have to fight against mass unemployment caused by severe recessions." (Pollin & Ash 2013)

Based on RR's research, Germany and also other advocates of austerity were able to introduce structural reforms to the MSs in crisis.

However, one cannot blame RR alone for austerity policies. As Charles Eliot puts it, "[t]he political leaders advancing austerity measures made their choice of policy first, and then cast about for intellectual buttresses." (Eliot 2013) And RR are not the only ones that had to correct their assumptions on debt and growth within the crisis of the euro: Also the chief-economist of the IMF, Olivier Blanchard, admitted that the IMF underestimated the negative effects of austerity on growth. (Kaiser 2013)

Obviously it is not possible to estimate the potential outcomes, if a second round of stimulus would have started after the first period from 2007 and 2009, but as Herndon et al. demonstrated, there had been space for it and national economies might currently experience a better performance, if the shift to austerity would not have been so harsh and if a second round of stimulus would have been awaited first.

The question of solidarity

In the end of the thesis I would like to give a little outlook on possible solutions for the crisis. Different options are widely discussed in the existing literature. Almost all authors agree that the best solution would be a common economic policy in Europe with the coordination not only of the monetary, but also of the fiscal policy of the MSs. Almost in the same degree as literature is aware that this actually is a necessary step for successful European integration, it is estimated as the most difficult step to achieve, as national governments have to yield important competencies to the European level.

But there is one solution discussed in the literature, which occurs especially in the context of Germany. This solution consists of the purpose to Germany and other well-performing economies to impose the principle of solidarity. Mortensen argues that "[n]evertheless the Financial Stability Mechanism proved to be insufficient to cope with the increasing problems of sovereign debt for some of the European countries, giving rise to enhanced pressures for stronger efforts of solidarity. However, some important eurozone countries firmly resisted new solidarity measures without increasing commons constraints on the national budget policy." (Mortensen 2013, p. 14) Hudson points out that the ECB is on the wrong side by demanding bailouts for banks, because when "debts cannot be paid, some party must lose – either creditors or debtors" (Hudson 2012, p. 315). 99 percent consist of debtors, which are taxpayers and one percent are creditors, which made 'remarkable giant gains' during the Bubble decade. But the ECB follows a pro-bank policy because of which taxpayers have to be the ones who lose while according to him it seems that "German exporters may be swept along in the austerity waves." (ibid.) In the opinion of De Grauwe and Ji "a more symmetrical fiscal adjustment – whereby the creditor nations agreed to stimulate their economies – would have reduced the price the periphery had to pay (in terms of lost output) to achieve a given improvement in their government budget balances." (De Grauwe/Ji 2013, p. 4) Because of the low labor expense in Germany, national demand is also low and reduces sales potentials of foreign goods. By a stimulation of labor expense, Germany would in consequence import more goods from its neighbors, reduce its surpluses and work towards an equilibrium. (Illing 2013, p. 15)

In their report on the completion of the EMU, which was released on the 29 June 2015, the presidents of the EC, Jean-Claude Junker, of the European Council, Donald Tusk, of the Eurogroup, Joroen Dijsselbloem, of the ECB, Mario Draghi and of the European Parliament, Martin Schulz claim both: More solidarity and risk-sharing between the MSs and a centralization of the Monetary union. It remains exiting what will be the outcomes of this new report, as Germany and France militated already some weeks before the publication of the report against further centralizations. (Mussler 2015)

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Figure 4: Current account balances. Retrieved from: ec.europa.eu/eurostat/tgm/graph.do?tab=graph&plugin=1&pcode=tipsbp11&language=en&toolbox=data (29 June 2015)

Statement of authorship

I hereby certify that this bachelor thesis has been composed by myself, and describes my own work, unless otherwise acknowledged in the text. All references and verbatim extracts have been quoted, and all sources of information have been specifically acknowledged. It has not been accepted in any previous application for a degree.

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