# THE IMPLICATIONS OF EUROPEAN DEBT CRISIS ON EU ENLARGEMENT

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## Abstract

Debt crisis in the European Union is the result of the inability of some countries to gain control over growing debt, which created tremendous pressure on the stability and survival of process for further European enlargement. The continued financial support (from the IMF, ECB, and EU) for southern European countries such as Greece, Portugal, and Spain has until now not produced the desired effects. Additionally, the high degree of dependence and relation of the Greek financial market from Cyprus's banks put the country and EU in an extremely difficult position. The current crisis has, however, posed serious challenges and doubts regarding the cohesion and future integration of the Union. Two factors have contributed to that: (a) the uneven distribution of its impact and (b) the three different levels on which resolutions have been sought: national, EU-wide and Eurozone. These divisions have spurred debates not only on the possibility of further integration, but also on the form that this integration will assume.

**Key words:** European Union, Eurozone, debt crisis, integration, financial system.

## Introduction

The EU is a unique economic and political partnership between 27 European countries that together cover much of the continent. The EU was created in the aftermath of the Second World War. The first steps were to foster economic cooperation: the idea being that countries who trade with one another become economically interdependent and so more likely to avoid conflict. The result was

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the European Economic Community (EEC), created in 1958, and initially increasing economic cooperation between six countries: Belgium, Germany, France, Italy, Luxembourg and the Netherlands. Since then, a huge single market has been created and continues to develop towards its full potential.[4]

What began as a purely economic union has evolved into an organization spanning policy areas, from development aid to environment. A name change from the EEC to the European Union (EU) in 1993 reflected this. The EU is based on the rule of law: everything that it does is founded on treaties, voluntarily and democratically agreed by all member countries. These binding agreements set out the EU's goals in its many areas of activity.

The EU has delivered half a century of peace, stability and prosperity, helped raise living standards, and launched a single European currency, the euro. Thanks to the abolition of border controls between EU countries, people can travel freely throughout most of the continent. And it's become much easier to live and work abroad in Europe.

The single or 'internal' market is the EU's main economic engine, enabling most goods, services, money and people to move freely. Another key objective is to develop this huge resource to ensure that Europeans can draw the maximum benefit from it. One of the EU's main goals is to promote human rights both internally and around the world. Human dignity, freedom, democracy, equality, the rule of law and respect for human rights: these are the core values of the EU. Since the 2009 signing of the Treaty of Lisbon, the EU's Charter of Fundamental Rights brings all these rights together in a single document. The EU's institutions are legally bound to uphold them, as are EU governments whenever they apply EU law.

As it continues to grow, the EU remains focused on making its governing institutions more transparent and democratic. More powers are being given to the directly elected European Parliament, while national parliaments are being given a greater role, working alongside the European institutions. In turn, European citizens have an ever-increasing number of channels for taking part in the political process.

[4] EU website: How the EU works http://europa.eu/about-eu/index_en.htm, approached 20.04.2012.

## The evolution of the European Union

The founding fathers[5] of EU were a diverse group of people who held the same ideals: a peaceful, united and prosperous Europe. European Union is not made all at once, or according to a single plan. It is built through concrete achievements which first create a de facto solidarity between the nations of Europe, which would lead to gradual political integration, a form which we have today. Further we give brief view of historical sequences in this gradual development.

*A peaceful Europe – the beginnings of cooperation (1945-1959).* The European Union is set up with the aim of ending the frequent and bloody wars between neighbours, which culminated in the Second World War. As of 1950, the European Coal and Steel Community begins to unite European countries economically and politically in order to secure lasting peace. The six founders are Belgium, France, Germany, Italy, Luxembourg and the Netherlands. The 1950s are dominated by a cold war between east and west. Protests in Hungary against the Communist regime are put down by Soviet tanks in 1956; while the following year, 1957, the Soviet Union takes the lead in the space race, when it launches the first man-made space satellite, Sputnik 1. Also in 1957, the Treaty of Rome creates the European Economic Community (EEC), or 'Common Market'.

*The 'Swinging Sixties' – a period of economic growth (1960-1969).* The 1960s sees the emergence of 'youth culture', with groups such as The Beatles attracting huge crowds of teenage fans wherever they appear, helping to stimulate a cultural revolution and widening the generation gap. It is a good period for the economy, helped by the fact that EU countries stop charging custom duties when they trade with each other. They also agree joint control over food production, so that everybody now has enough to eat - and soon there is even surplus agricultural produce. May 1968 becomes famous for student riots in Paris, and many changes in society and behavior become associated with the so-called '68 generation'.

*A growing Community – the first Enlargement (1970-1979).* Denmark, Ireland and the United Kingdom join the European Union on 1 January 1973, raising the number of member states to nine. The short, yet brutal, Arab-Israeli war of October 1973 result in an energy crisis and economic problems in Europe. The last right-wing dictatorships in Europe come to an end with the overthrow of the Salazar regime in Portugal in 1974 and the death of General Franco of Spain in 1975. The

[5] Altiero Spinelli; Paul-Henri Spaak; Robert Schuman; Jean Monnet; Sicco Mansholt; Walter Hallstein; Alcide De Gasperi; Winston Churchill; Johan Willem Beyen; Joseph Bech; Konrad Adenauer.

EU regional policy starts to transfer huge sums to create jobs and infrastructure in poorer areas. The European Parliament increases its influence in EU affairs and in 1979 all citizens can, for the first time, elect their members directly.

*The changing face of Europe - the fall of the Berlin Wall (1980-1989).* The Polish trade union, Solidarność, and its leader Lech Walesa, become household names across Europe and the world following the Gdansk shipyard strikes in the summer of 1980. In 1981, Greece becomes the 10th member of the EU and Spain and Portugal follow five years later. In 1986 the Single European Act is signed. This is a treaty which provides the basis for a vast six-year programme aimed at sorting out the problems with the free-flow of trade across EU borders and thus creates the 'Single Market'. There is major political upheaval when, on 9 November 1989, the Berlin Wall is pulled down and the border between East and West Germany is opened for the first time in 28 years, this leads to the reunification of Germany when both East and West Germany are united in October 1990.

*A Europe without frontiers (1990 – 1999).* With the collapse of communism across central and Eastern Europe, Europeans become closer neighbours. In 1993 the Single Market is completed with the 'four freedoms' of: movement of goods, services, people and money. The 1990s is also the decade of two treaties, the 'Maastricht' Treaty on European Union in 1993 and the Treaty of Amsterdam in 1999. People are concerned about how to protect the environment and also how Europeans can act together when it comes to security and defence matters. In 1995 the EU gains three more new members, Austria, Finland and Sweden. A small village in Luxembourg gives its name to the 'Schengen' agreements that gradually allow people to travel without having their passports checked at the borders. Millions of young people study in other countries with EU support. Communication is made easier as more and more people start using mobile phones and the internet.

*Further expansion (2000 – 2009).* The euro is the new currency for many Europeans. 11 September 2001 becomes synonymous with the 'War on Terror' after hijacked airliners are flown into buildings in New York and Washington. EU countries begin to work much more closely together to fight crime. The political divisions between east and west Europe are finally declared healed when no fewer than 10 new countries join the EU in 2004, followed by two more in 2007. A financial crisis hits the global economy in September 2008, leading to closer economic cooperation between EU countries. The Treaty of Lisbon is ratified by all EU countries before entering into force on 1 December 2009. It provides the EU with modern institutions and more efficient working methods.

*Recent changes (2010 – today).* In March 2010 at a European Council meeting in Brussels, EU leaders adopt Europe 2020 targets and all 16 Eurozone countries back a plan to help Greece deal with its deficit. This year, heads of State and Government within the euro area agree to deeper fiscal consolidation, stronger economic coordination and budgetary surveillance to defend the euro. At a European Council meeting in Brussels, EU leaders adopt a 10-year strategy for smart, sustainable and inclusive growth: Europe 2020. 91 European banks undergo stress tests to assess their resilience to economic shocks. All but seven pass the tests. G20 leaders at the Seoul summit commit to a joint Action Plan to encourage more balanced growth within the global economy.

In 2011 three new European financial supervisory authorities begin operating: the European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority. A comprehensive package of measures to strengthen the European economy is finalised at the spring European Council in Brussels. The Euro Plus Pact was set up to reinforce economic policy coordination in the Economic and Monetary Union. Euro area countries sign a treaty creating a European Stability Mechanism, able to lend up to €500 billion to euro area countries in crisis. The results of a round of bank stress tests are published, revealing banks' ability to withstand a new recession. Some 83 out of 91 banks pass. A summit of Heads of State and Government from the euro area puts in place a comprehensive strategy that ensures fiscal consolidation, growth, support to countries in difficulty, and stronger euro area governance. The Economic and Financial Affairs Council adopts a package of six legislative proposals aimed at strengthening economic governance in the EU. It includes rules for more responsible management of banks. At the European Council, 17 members of the euro area and several other EU countries agree to participate in a new 'fiscal compact' and to coordinate their economic policies more tightly.

In January 2012 At an informal summit of the European Council, a new treaty on stability, coordination and governance in the economic and monetary union is agreed by all EU countries with the exception of the Czech Republic and the United Kingdom. The treaty aims to strengthen fiscal discipline through automatic sanctions and stricter surveillance and, in particular, the 'balanced budget rule'. As part of the 'European Semester', the Commission adopts recommendations for each of the 27 EU countries, offering guidance on 2012-2013 national budgets and economic policies. The country-specific recommendations take account of each country's economic situation and provide advice on stimulating economic growth and job creation. They are later adopted by the European Council. At the end of the year At the European Council, EU leaders take the first step towards implementing a banking union with the decision, in principle, to create a 'single supervisory mechanism' (SSM), allowing the European Central Bank to supervise large euro area banks directly.

In January 2013 the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (popularly known as the 'fiscal compact') enters into force. It aims to strengthen fiscal discipline in the euro area through the 'balanced budget rule' and a correction mechanism.

**European debt crisis and EU enlargement**

The European debt crisis has been a dominant topic in politics, economics, and the media of late. One cannot ignore the deafening sound of questions being raised about what will become of the European Union and whether the concept of European integration has taken a backseat or moved beyond our reach. [6]The IMF has been encouraging all of its member states to enact policies that could collectively help pull the world economy out of its weak state in an effort to reignite growth and boost employment. Despite some efforts that have already been made during the current crisis, the European Union should continue with structural reforms and budget consolidation. European policymakers have a responsibility to put key elements in place in order to restore market and consumer confidence. A banking union is one of these elements, and it has been created in a short span of time. However, a long-term vision of the European Union is another important element that still has to be developed.

Literature on the effect of crises on European integration has led scholars to argue that, in a rather counterintuitive manner, crises tend to push integration forward (Handley 1981; Tsoukalis 1992, Schmitter 2011). As early as 1981, and in spite of noting a stalling of integrative efforts during the 1970s economic crisis, Handley presented evidence that collective crisis resolution empowered discourses of European's within the European public. The current crisis has, however, posed serious challenges and doubts regarding the cohesion and future integration of the Union. Two factors have contributed to that: (a) the uneven distribution of its impact and (b) the three different levels on which resolutions have been sought: national, EU-wide and Eurozone. These divisions have spurred debates not only on the possibility of further integration, but also on the form that this integration will assume.

[6] www.ecem.gr "Economic Crisis and the Future of European integration: Preliminary Thoughts"

While the solidarity test is ongoing, the setting in motion of the architecture of European economic governance and the appeasement of the debates on the exit of Greece from the Euro, which would allow it to re-nationalize its monetary policy and use traditional instruments, such as currency devaluation, to face the crisis, suggest that – willingly or unwillingly – the EU has stood up for its members. Scenarios about the "end of the Euro" have, at the time of writing, been left behind and the agreement seems to be that the EU, as a whole, will construct, once again, the solution to this crisis[7].

Dr. Linzert reviewed the architecture of the European Monetary Union, which was launched in 1998 and now includes 17 member states. He outlined the importance of further reforming European governance and the urgent need for a euro area crisis management mechanism—such as the European Stability Mechanism—to foster European integration. Due to Europe's deeply interconnected banking sectors, he presented the financial union – including the introduction of a Single Supervisory Mechanism overseeing the credit institutions in the euro area—as an indispensable part of the future economic and monetary union. Dr. Linzert also addressed the alleged conflicts of interest within the ECB as being responsible for both monetary policy and—in the future—banking supervision, and emphasized that the proposals now on the table would take account of this by having a clear separation of the two functions within the ECB. This should also be accompanied by a strong European bank resolution framework. He also stressed that the ECB's policies alone would not be sufficient to deal with the current crisis. In the domain of fiscal policy, governments have to act responsibly at the national as well as the European level.

## Conclusion

Currently, with various conflicting forces struggling for the leading position, the development of the EU has reached a critical point. As member states are forced by the crisis to coordinate their economic and fiscal policies, power is gradually shifted to the EU level. During this process, inter-governmental forces will be considerably increased. Although certain consensuses have been formed during the crisis on accelerating structural reforms to increase competitiveness, such reforms would be constrained by political and social boundaries and struggles and compromises between different forces would eventually determine the pattern and trend of European integration. In any case, the process of European integration would have been profoundly changed by the euro crisis.

Every ten years the EU sets out an agenda to be achieved within the decade. In 2000 the agenda agreed upon in Lisbon (better known as the "Lisbon Strategy")

[7] "Debt Crisis and Power Redistribution Among EU States", China Academic Journal, 2012

set out to make the EU "the most competitive and dynamic knowledge-based economy in the world”. By 2009, successive EU Presidencies (Sweden first, followed by Spain) admitted to the failure of this vision. Given the current state of the economy, the strategy for the next decade, the “EU 2020” strategy has identified stronger economic governance as the main goal. But, as the crisis has exemplified, only through political unity will this be achieved. So, we have to hope for the best.

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