

The euro zone is in crisis. Here are the four most important lessons to take away.

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State of the 2016 race

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By Mark Copelovitch, Jeffrey Frieden and Stefanie Walter March 31

The European Union (E.U.) is facing its most serious [economic crisis](#) since the first steps towards European integration in the 1950s. Since 2010, the countries that have adopted the [euro](#) — the single currency shared by 19 of the 28 E.U. member states — have wrestled with a financial and debt crisis that has now caused [more lasting economic damage](#) to some parts of Europe than the Great Depression of the 1930s.

The economic crisis has turned into a serious political crisis, with conflict among and within E.U. member states threatening both European integration and domestic stability. In 2014, we convened a transatlantic group of leading scholars of international and comparative political economy to collaborate and present research on the political economy of the current crisis. [Comparative Political Studies](#) (CPS) has just published our findings as a special issue. So [what did we learn??](#)

Lesson 1: The euro zone crisis looks a lot like other balance of payment crises

The euro zone crisis is unusual. It involves a single currency shared by many countries with widely divergent macroeconomic conditions and little centralized financial regulation. The E.U. has no [fiscal policy coordination](#) — and it lacks a credible no-bailout commitment. These factors came together to bring the [euro zone close to collapse](#).

But the crisis played out in pretty much the same way as other [balance-of-payments crises](#) over the past two centuries. Here's the typical pattern. A country borrows heavily from abroad and uses the money for current consumption rather than investment. Then the economy expands rapidly, creating a bubble that eventually bursts.

That's what happened in Europe.

The countries of Northern Europe lent massive amounts of capital to less-wealthy countries on the periphery. There was a boom in some countries — Ireland, Spain, and other countries built a lot of [housing](#), for instance — and overspending in others, such as Greece and Portugal. As the 2007-2009 global financial crisis accelerated, this bubble burst, triggering the euro zone crisis and leaving peripheral countries owing far more money to Northern European creditors than they could pay off.

Politics during the euro zone crisis have also followed the patterns seen in past financial crises. Countries and groups have squared off in bitter domestic and international conflicts. They have battled over how to share the [burden of adjustment](#). At the domestic level, the crisis has [polarized public](#) debate, fueled tensions over reform, and increased support for [extremist parties](#).

At the international level, the crisis triggered harsh debates over [International Monetary Fund](#) (IMF) and E.U. bailouts, about the need for common banking regulation for the entire euro zone, about [immigration](#), and over how debtor and creditor countries can make the necessary sacrifices to resolve the crisis and restore economic growth. The authors of the CPS special issue analyze these conflicts using the tools of comparative and international political economy.

Lesson 2: Monetary union raises the political stakes

What's really different in the euro zone is that the crisis occurred within the context of monetary union and European integration. The response to the crisis, both by individual countries and by the E.U. as a whole, has unleashed bitter debates over the future of the euro. As others have noted in the [Monkey Cage](#), the [European Central Bank](#), European Council, and other [central authorities](#) have now taken on a more powerful role. And creditor countries such as [Germany](#) now wield far more power within the E.U.

The crisis has also fueled broader debates about "[Grexit](#)" and "[Brexit](#)" — the possibility that Greece might leave the euro zone and the U.K. might pull out of the EU altogether — which would rattle the very foundations of European integration.

Lesson 3: The underlying problems of European monetary union never went away

The economic and political problems of adopting a single currency were [largely predictable](#) and [broadly foreseen](#) prior to the launch of the euro. These problems have once again come to the fore. In the run-up to the introduction of the euro in 1999, domestic politics in the E.M.U. member states made it impossible to get an agreement on the policies and institutions that might have avoided the crisis — such as deeper fiscal policy and regulatory cooperation. The third lesson is that ignoring those earlier warning signs was a mistake.

Since 2010, European and national policymakers have pursued piecemeal responses to try to prevent a collapse of the euro zone, but they have been unable to resolve the basic causes of the crisis. Member countries face wildly differing macroeconomic situations and opposition to further integration (including the rise of new "[Euroskeptic](#)" parties) is widespread.

The euro zone is at an impasse. It now seems to be on track to emulate Japan, which has been stagnating since the 1990s. Japan still struggles with the impact of its "lost decades" — too much debt, an aging population, and persistent deflation. The euro zone's problems today appear disturbingly similar.

In addition to Europe's debt problems, "[secular stagnation](#)" is the other big threat. Many member states face decades of grinding deflation, long-term unemployment, and [stagnation](#). There's no easy way to kickstart economic growth. The future

threatens to bring not just lost decades, but lost generations.

None of this bodes well for the future of European monetary integration. Economic stagnation and the refugee crisis will [increase political support](#) for anti-euro and anti-E.U. parties throughout Europe. Jones, Kelemen, and Meunier argue in the concluding paper of the CPS special issue that “[failing forward](#)” through half-baked policy responses to the most pressing euro zone problems will not fix this crisis.

Lesson 4: Monetary union doesn't work without fiscal and regulatory coordination

The final lesson is that European policymakers need to make some major changes to ensure the euro's viability. To maintain the monetary union, the euro zone needs a true lender of last resort, deeper coordination on fiscal policy, and increased labor mobility among E.M.U. members. Will this mean the members move towards a more formal [fiscal and political union](#)? Clearly, the euro will not survive if nothing changes.

Current political and economic debates in Europe [closely mirror those of the United States](#) from the 1790s through the 1860s. Alexander Hamilton and Thomas Jefferson clashed over whether the federal government should take on [state debts](#); the country split over the First and Second Banks of the United States; and American monetary union was not completed until the 1870s. The U.S. experience shows that crafting a functioning economic and monetary union is a long, hard road, requiring regions and groups to make difficult compromises.

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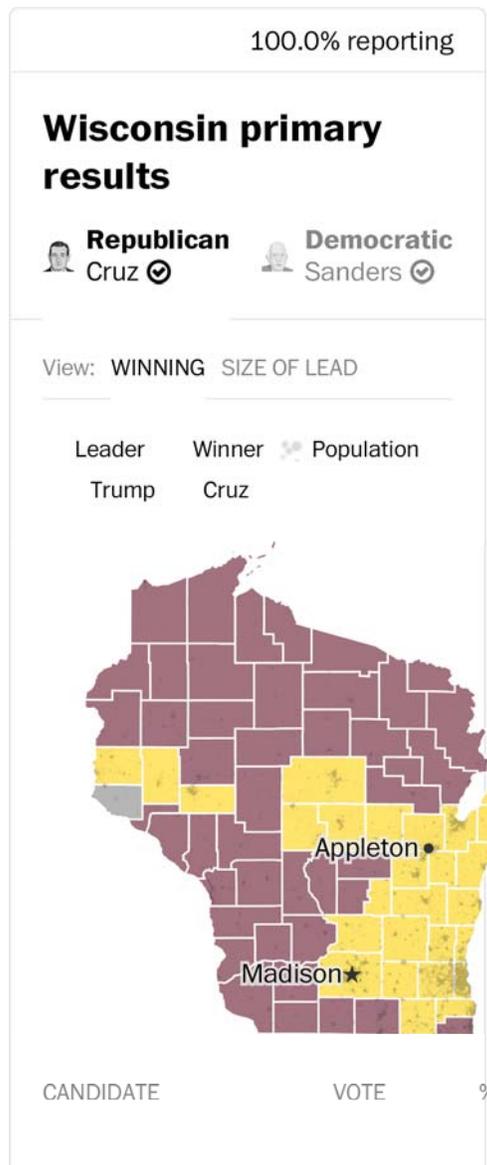
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European policymakers may not be able to solve the continent's current problems. The major obstacles are political rather economic. There are no technical barriers to any of the solutions to the euro zone crisis: debt restructuring, coordinated fiscal stimulus, harmonized financial regulation, just as a start. But until there's political agreement on how to proceed, the euro zone's long-term future remains uncertain.

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CANDIDATE	VOTE	%	DEL*
 Cruz 	531,129	48.2%	36
 Trump	386,370	35.1%	6
 Kasich	155,200	14.1%	0

42 delegates Source: AP

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