On Origins and Implications of the Sovereign Debt Crisis in the Euro Area

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Abstract

The current crisis in the Euro Area is mostly a serious crisis of confidence. Its solutions have to be systematic and consistent. Our paper discusses its main systematic reasons while keeps in mind the European integration and globalization issues of the world economy and economic financial markets. Recent problems in the Euro area are based on the diagnostic of the origins of the balance of payments and self-fulfilling crisis, and discussed in the context of suggested remedies and solutions based on diversification of the monetary policy management in the Euro Area to eliminate the moral hazard from its financial sector, creation of a functioning system of fiscal transfers and finding a compromise between centralization and decentralization and government interventionism and "laissez faire".

Keywords: Euro, Euro Area, economic crisis, fiscal policy, monetary policy

JEL Classification: E58, E62, F15, F32

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1. Introduction

The current Euro Area crisis has revealed certain flaws of the Euro Area, such as its vulnerability to asymmetric shocks and its inability to act as assumed by the optimum currency area theory (Jager and Hafner, 2013). It has highlighted the serious lack of confidence in the ability of the Euro Area to face challenges resulting from political and economic development in the Euro Area countries and in the world economy (Goméz-Puig and Sosvilla-Rivero, 2012). It has emphasized the influence of serious system failures of the global economic and political order and of serious structural failures of the "Euro project" on success and economic growth in the Euro Area. Consequently, it has stressed the need to find a systemic and consistent solution to the current problems of the Euro Area. Also Eichengreen (2012) supports this statement and argues that the Euro Area had been designed with some serious flaws, which are still underestimated. Moreover, Verdun (2012) adds that the current European sovereign debt crisis has put on the agenda the need to redesign the Euro Area due to the lack of symmetry between “economic” and “monetary” union because the main problem is the asymmetrical Euro Area and its mistaken institutional structure (Buti a Carnot, 2012).

The international financial globalization and the integration of financial markets are supposed to lead to a more effective distribution of resources in the global economy and to increase the performance of real economies. The result of related liberalization of global trade and foreign currency regime, inefficient regulation on world’s financial markets and the gradual emergence of new technologies and innovative financial instruments on these markets are mainly cumulating the risks in the world financial system and on the world economical market and their destabilization. Each country is under influence of these aspects and becomes more sensitive on financial turbulence and due to their high interdependence; they are more liable to financial spillover effects and other problems (Bekaert et al., 2006; Cubillas and Gonzáles, 2013; Croci Angelini et al., 2014; Eichacker, 2015).

At the same time, in the terms of Economic and Monetary Union (EMU), the politically pursued and often economically unpremeditated spreading of European integration seems as global support of moral hazard in the financial sector. It motivates the private sector and governments to “consciously gamble for redemption” from their problems by making decisions based on morally unjustifiable and economically harmful deficit economy and creates conditions for the implementation of policies like “too-big-to-fail” not just on national, but also on international level, which supports and basically legitimizes indebtedness of subjects of private and public sector including their members (Arellano et al., 2012; Bratis et al., 2015).

Consequently, the result of above mentioned facts is general support and acceptance of debt politics in the Euro Area and their current expression is the European sovereign debt crisis. The crisis also results from reactions of governments and central banks of the Euro Area member countries on previous private debt crisis in their national economies and in the world economy and from different economic levels and performances of the Euro Area members, from unsustainable public debt of the peripheral Euro Area countries and from the incompleteness of the Euro project (Aizenman et al., 2013; Lothian, 2014). According to Baimbridge et al. (2012) the crisis is a product of fiscal indiscipline, of too expansive budgetary and fiscal policy and of the fact that economies in Euro Area are too competitively inflexible. It is thus not a crisis caused only by inability of southern European countries to maintain their budget expenses, but it is mainly a result of imbalances in the Euro Area and in the global political economy (Brancaccio, 2012). Its main causes are systemic and their core is in the general system failures of global economic and political order and in serious structural failures of the Euro Area and of Euro as the projects (Detlef, 2012; Lothian 2014).

To ensure the proper progress of European integration and for successful fulfillment of its goals it is necessary to take into consideration the nature and the complexity of the causes of the recent crisis in the Euro Area. The crisis is in fact a serious crisis of confidence (Goméz-Puig and Sosvilla-Rivero, 2012) which creates a demand on systematic and consistent solutions to eliminate it. The aim of this paper is therefore to identify systematic sources of this crisis and design some of its possible solutions, or more precisely to identify the facts that are necessary to take into consideration when creating adequate and efficient solutions, while keeping in mind the European integration issue and the globalization of world economy. Regarding this ambition, our paper emphasizes that the crisis is the balance of payments crisis and self-fulfilling crisis. Considering identified issues, suggested remedies and solutions are based on diversification of the monetary policy management in the Euro Area to eliminate the moral hazard from its financial sector, creation of a functioning system of fiscal transfers and finding a compromise between centralization and decentralization and government interventionism and "laissez faire".

To achieve the stated objectives, the rest of this paper is organized in the following way: the first section clarifies basic relations of the transition of the debt crisis in the Euro Area from the private sector to the public sector. The second section discusses selected causes of the current European national debt crisis that are connected with the globalization of world economy. The third section is focused on selected sources and origins of the crisis which are related to the question of ongoing integration in Europe and the last section summarizes recommendations that should be considered when proposing adequate and effective solutions.

2. From the Debt Crisis of the Private Sector to the Serious National Debt Crisis

European debt crisis is in fact continuation of the recent American mortgage crisis (2007) (Ureche-Rangau and Burietz, 2013) and the following global financial (Reinhart and Rogoff, 2011; De Bruyckere et al., 2013) and economic crisis (2008) (Gennaioli et al., 2010; Claessens a Kose, 2010; Ureche-Rangau and Burietz, 2013). As their result, governments of many developed countries were "forced" to introduce rescue plans and actions to restore confidence of investors, to avoid panic on financial markets and to prevent or reduce the effects of ongoing recession. Using these and other excuses, the following action was made: capital injections and guarantees were provided to bankrupting entities that were considered to be systematically important, e.g. too big to fail. However, introduction of the "too-big-to-fail" policy resulted in creation of huge deficits of public finances and extreme increase of countries national debts that have become unbearable in relatively short time. Problems with repayment of exploded levels of sovereign debts experienced selected Euro Area member countries already at the beginning of 2010 (Ureche-Rangau and Burietz, 2013). This fact was confirmed by several studies, i.e. by Cuestas and Steahr (2014) who analyzed and compared the dynamics of the national debts in the Euro Area before and after the global financial crisis. Significant impact of the crisis on fiscal variables in individual countries was also investigated (Cuestas et al., 2014). De Grauwe (2010) adds that the growth of the deficit in all Euro Area member countries was due to the three to the financial and credit crisis of 2007-2009 related aspects: "1) the rescue operations of the national banking systems and the stabilization funds; 2) the stimulus packages to prevent a further meltdown of the type experienced in the Great Depression of the 1930s; and 3) the extensive tax revenue losses due to the meltdown of the real economy, the rise of unemployment, and decline in incomes" (Young and Semmler, 2011).

It seems obvious that the governments of Euro Area countries with the help of the central bank and multinational institutions partially managed to "transform" the previous private sector debt crisis to the current public sector debt crisis in the Euro Area (Lothian, 2014; Beirne and Fratzscher, 2013; Grammatikos a Vermeulen, 2012). The main channels that enabled this transition were stock markets and the mentioned government interventions that have influenced the expenses and the national debt of many Euro Area member countries which caused serious problems with its financing (Gennaioli et al. 2010; Ureche-Rangau and Burietz, 2013; De Bruyckere et al., 2013; Pisani-Ferry, 2013).

Despite the obvious negative consequences of the bailout, it is still possible to find supportive arguments. For example Bordo and Eichengreen (1999) are convinced that the government and the central bank are obliged to use all their resources to avoid loan crisis in the economy, and therefore they have the right to conduct any saving actions. However, they also warn that the interest of the government to keep the investor's confidence in the solvency of the country can lead to a significant increase on its debt burden and increase the risk of failure when financing the debt (Diaz-Alejandro, 1985; Reinhart a Rogoff, 2011; Ureche-Rangau and Burietz, 2013). Moreover, the government acts are also justified by other arguments, i.e. two theoretical reasons explaining the possibility of connecting two types of crises in the economy. The first reason is today's perception of government as the lender of the last resort (Kindleberger, 2005), which is responsible for maintaining the confidence on the financial markets in the country (Bordo and Eichengreen, 1999; Laeven and Valencia, 2010) and the second is the effect of government bonds on the financial markets as risk-free assets (Ureche-Ranga and Burietz, 2013).

An important cause of the debt crises and their movement along economy sectors, e.g. also the reason of the European national debt crisis is the loss of confidence of investors in the ability of debtors and intermediaries to fulfil their obligations and the related uncertainty in the financial markets (Lothian, 2014). Therefore, a government that wants to stop its increase has to be able to issue its debt without a rapid increase of the risk of its failure (Ureche-Rangau and Burietz, 2013; Wehinger, 2010).

3. Selected Global Causes of the European National Debt Crisis Related to the Globalization of the World Economy and World Financial Markets

While taking into account the phenomenon of globalization of world economy and financial markets, it is possible to identify several system resources of the current European national debt crisis that can be classified into four groups.

Deformed Monetary and Bank Systems

The first group of causes is related to the current deformed monetary and bank systems. The main cause of manipulation with the economic calculations of market participants, significant systematic support of moral hazard and debt growth of the private and public sector, prolonging and deepening of cyclical fluctuations in the economies and financial crises are the current centrally planned, centrally controlled and significantly deformed monetary and bank systems based on unsecured symbolic fiat currencies and on system of fractional reserve banking (Gonda, 2012; Detlef, 2012).

These arguments can be supported by the fact that the central banks and also significantly involved commercial banks are nowadays live together with governments in some sort of financial-debt symbiosis. Central banks are also not completely independent and are sometimes acts even together with commercial banks to help the government to meet their interests. On the other hand, commercial banks are gaining significant financial resources and guarantees from central banks and governments that leads to a global support of irresponsible reliance of market participants on others to cover the losses of commercial banks and other entities.

A good example of fatal conceit of the governing to design the fates of others to achieve their specific economic and political interests is also the change of character of monetary policy that happened in the Euro Area after 2008. Its result was mostly price deformation on the financial market and inappropriate stimulation of lending activities and associated debt accumulation in the Euro Area. In low interest rates environment fueled by excessive money supply, amount of real investments is increasing even if there is not adequate increase in savings and there is also no increase in demand for goods. Under such circumstances an increase in inflation is generally expected together with a burst of asset price bubbles. As a result, interest rates reduction and introduction of related nonstandard monetary policy actions does not seem to be a proper way of solving problems in the Euro Area. Such activities may result only in slowing down the market, increased inefficiency and postponing the solution of the crisis to the future.

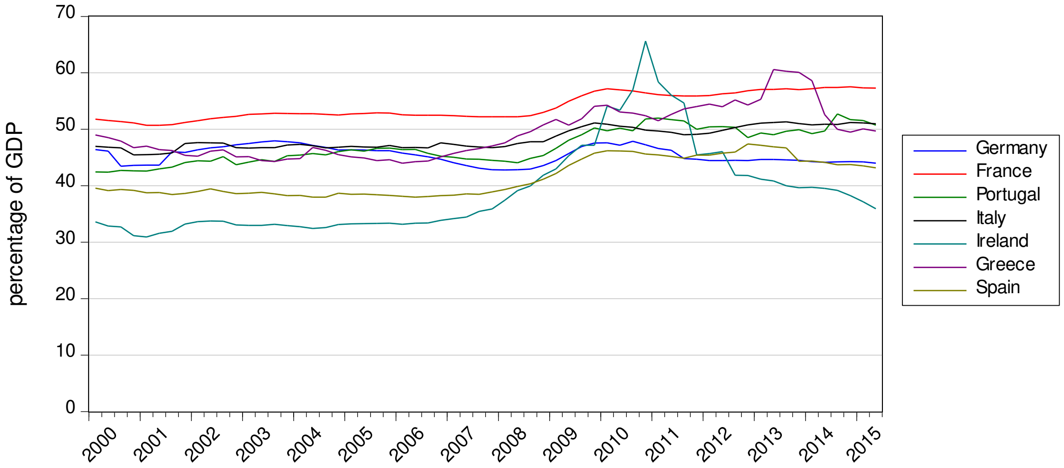
Similar effect is also achieved by bailing of indebted entities from bankruptcy, e.g. introduction of the „too-big-to-fail" policy that has a side effect of creating the precedent eligibility of bailout for all entities that are going to have similar problems in the future, without taking into consideration the origins of the problems (Detlef, 2012).

Deformed Public Finances

The second major group of the current Euro Area crisis sources is today's public finances from the aspect of globalization and financial integration. The public spending of many Euro Area member countries are in long term excessive and their finances are usually deficient. The fact of consensual acceptance of deficit guarantees to the market players high reliance on the state and the tax payers of other countries. Culture of eligibility and dependence are built on misinterpreted application of the social justice policy which results in growth of public redistribution in many countries, while the development of real economies is being ignored (Gonda, 2012; Balcerowicz, 2014).

The above mentioned idea is also valid the Euro Area. Many of its countries, even during the financial and economic crisis, have not started to reduce their spending, moreover, they have even continued to raise their public expenditures. It is shown on Figure 1 and we can see that even during the crisis years, the rate of redistribution in the selected Euro Area countries, except Ireland, has grown or slightly decreased.

Figure 1 Level of Redistribution through Public Spending within the Euro Area



Source: Compiled by author based on data taken from IMF - International Financial Statistics (November 2015).

Frequently mentioned cause of today's Euro Area problems is also fiscal irresponsibility of many its members, falsification of statistics and usage of questionable practices such as creative accounting (Reinhart and Rogoff, 2011).

Deformed Moral Principles of the Society

The third important group of system causes of the recent European national debt crisis arises from its global, social, economic and political background and is related with deformed moral principles of the society. The current global economic and political system and further centralization and government interventionism in the Euro Area on transnational level are creating economically pervert motivation for economic calculations of market players that strengthens their mentality of requiring and culture of relying and depending on countries. At the same time, they also deform the traditional society values, its moral conventions and they are less applying the reciprocity of the market. For example, even Adam Smith in his work the "Theory of moral sentiments" (1579) emphasized the importance of strong moral habits for the society that, according to him, should have clear business ambitions, but should also respect the basic moral values. Only belief in moral principles and reciprocity ethics of the market can preserve the effectiveness of allocating company resources, freedom and prosperity (Gonda, 2012).

Financial Markets, Speculations and Credit Ratings

The fourth, and the last group of the Euro Area crisis sources originates in the principles and processes associated with globalization and financial integration, such as the architecture of financial markets, speculations of entities operating on these markets, and the questionable reliability of credit ratings from rating agencies that represents the essential pillar of activities on these markets. Securitization and speculations that are today part of financial markets and actually allow relocating the risks from irresponsible borrowers on other entities that are interested in not transparent and hazardous financial products (Cohen and Villemot, 2014).

Whyte (2010) argues that the creditworthiness judgements of the third-party raters had attained the force of law and he warns about a huge impact of credit ratings on the cost of funding, regardless of whether the rated subject is a private borrower or a sovereign borrower. Moreover, Pagano and Volpin (2010) points out the impact of credit ratings on the achievements of implemented austerity measures in the Euro Area. Also, Afonso et al. (2011a), Afonso et al. (2011b) and Eijffinger (2012) note that credit ratings are the key part of the financial markets, but they conclude that rating agencies lag behind markets, that they are notoriously bad at predicting currency crises, that their business model is flawed, and that the existence of a lack of competition between three rating agencies on the financial markets is the reason for their too strong market position. De Haan and Amtenbrink (2011) criticize business model of rating agencies too and they warn about the herd behavior of investors. Therefore, prudential regulation and accounting standards and more competition and transparency are needed to increase the quality of credit ratings.

Moreover, Wolfgang Schäuble, the German politician, argues that according to the recent problems in the Euro Area the financial markets do not understand the unique and specific construction of the euro and states: "We have a common monetary union, but we don't have a common fiscal policy. We need to convince the international public and international markets that this is a new form, very specific to meeting the demands of the 21st century" (Young and Semmler, 2011).

The mentioned issue can be clarified by Cohen and Villemot's (2014) theory. They distinguish two types of debt crises: those that are the result of external shocks and those that were made endogenously, either as a result of self-fulfilling panic on financial markets, e.g. as the effect of self-fulfilling expectations of investors operating on these markets, or as a result of predatory behavior of "Panglossian" borrowers.

Self-fulfilling crisis that is caused by self-fulfilling panic on financial markets happens, when investors expect that the government of the specific country will have a problem with repayment of its own debts and if they act on financial markets according to these expectations. It is also the same in case if their expectations are positive about the risk of failure with the fact that they are helping them to refinance their liabilities, and in fact they are supporting them in their further indebtedness (Arellano et al., 2012). In such a situation, the most important role is objectivity and truth of information that determine expectations of investors, and thus the reliability of countries by the credit rating they receive from rating agencies.

Key factor that influences the formation of such type of debt crisis is by Arellano et al. (2012) also represented by the current level of debt of the government. As a result, government is obliged to optimize its indebtedness policy in order to avoid its exposure to an excessive risk of failure.

The formation of the self-fulfilling debt crisis that is caused by predatory behavior of "Panglossian" borrowers, who are characterized by Krugman (1998) as borrowers who focus only on their best prospects for growth and success, while they consciously expect their own failure while paying their own debts. Arellano et al. (2012) blames countries that are in recession, but have motivation to lower their government expenditures very slowly, or even raise them and at the same time, raise their public debt. Such entities would consciously "hazard with their survival", in the belief of recovery of their economy relying on increased tax incomes and economic growth. In case of persistence of their problems, they would become vulnerable to the sort a self-fulfilling crisis of their national debt and they would be exposed to the risk of a bankruptcy.

An essential factor, that motivates governments to hazard about their survival, is the development of expenditures on their indebtedness. It also depends on the activities of the particular government. For example Arellano et al. (2012) has marked the anti-crisis policies and actions of EU and MMF, as explicitly harmful and supporting indebtedness of other members. In fact any policy, that increases the countries bond prices (reducing the income from them) or reduces the cost of its failure, motivates to gamble for redemption and helps to increase its indebtedness. It is necessary to emphasize the influence of the “Euroilusion” that arose after the creation and introduction of Euro, on the expenses of the GIIPS countries (De Grauwe and Yueimei, 2013). As a result, the governments tend to employ deficit spending policies even if they are going to have even more debts, e.g. it is worth for them to gamble for survivor. Therefore, in the context of the Euro Area issues, it is appropriate to evaluate the fiscal discipline rules that are laid down in the Pact of Stability and Growth in the Fiscal compact (Eijffinger, 2012). The key role in the Euro Area's crisis is represented not only by those four universal systematic global causes of debt crises, but mostly by the specific system failures of the project.

4. Selected European Integration Related Causes of the European National Debt Crisis

European national debt crisis was caused mostly by specific systematic failures of the Euro Area and euro projects, e.g. causes related to the European integration issue, while for simplification purpose we can again divide this issue into four groups.

Questionable Goals of European Integration

The first group of the causes is related to the goals of the current progress in the European integration. Based on Winston Churchill's words from 1946, basically the aim of integration in Europe is supposed to preserve the peace on European soil and to ensure freedom, prosperity and wealth of its inhabitants (European commission, 2015). These objectives are also defined by Article 3 of the Consolidated version of the Treaty on the European union and the Treaty about the functioning of EU. More specifically, the primary EU’s goal is to preserve peace in Europe, its values and the wealth of its nations on this continent, and puts much less stress on the economic aspects, such as ensuring the economic growth, price stability, full employment, strengthening the competitiveness of its members and so on (ECB, 2011). Therefore, the Union’s principle cannot be described as primarily economic, but rather political. It is also confirmed by later progress of European integration, which has been significantly influenced with geopolitical reasons.

Also Cesarano (2013) writes about the dominance of the political objective of European monetary unification and as well as Hall (2012) adds that the Euro Area was in fact a large political project, initiated by French President François Mitterrand and supported by

German Chancellor Helmut Kohl in the line with "une certaine idée de l'Europe" in order to bind a newly unified Germany to Europe. Hall (2012) additionally stresses the conditionality of inception of the Euro Area and euro on French agreement to German unification and on creation of the Stability and Growth Pact. He also gives two important aspects of the new economic doctrines which were deciding in the case of the "Euro project": Firstly, he argues that mainstream economics moved away from the Keynesian view that fiscal policy is crucial tool for stabilizing the economy, towards the monetarist view that fiscal policy is not stabilizing tool for the economy and that monetary policy has few lasting effects on the real economy, and states that the implication of this opinion in the context of European integration was that fiscal policy should remain roughly neutral and diversified and that monetary policy should be rule-based, targeted on inflation and unified. At the same time, the disputable limits placed on debt and deficits of the Stability and Growth Pact were found as adequate. It turned out to be questionable (Hall, 2012; Weeks, 2014). Secondly, he argues that in keeping with the opinion that demand management is essentially irrelevant to economic growth, the new economic doctrines held that economic growth depends largely on structural reform to the supply side of the economy targeting the more intensive competition in markets for goods and production factors, concrete for labor and capital, and states that the implication in this case was that all the Euro Area member countries should use the same approach and the same formula to protect economic growth. According to his opinion, the problem was the belief of responsible persons that competition under the new stringent conditions imposed by a single market and by a common currency but without any better fiscal integration or coordination would force suitable structural reform on the Euro Area member states and lead to gradual institutional convergence in their political economies (Hall 2012).

Therefore, the principle of the European integration cannot be described as primarily economic, but rather as definitely political. It is also confirmed by later progress of European integration, which has been significantly influenced with geopolitical reasons and whose economic aspects have been largely marginalized or taken in to account only very superficially. Namely Klaus (2004) argued that the largest and the most important part of the positive economic impact of the European integration on its members has come only through the liberalization of trade and investment and has been already obtained. The cause of this is according to him the fact that the role of the exchange rate risk as a factor determining the cost of capital and the cost of foreign investment is really relatively small and therefore trade is not important to have the same currency on both sides of the realized transaction (Klaus, 2004; Jager and Hafner, 2013).

On the other side, some economists argue that the euro project have an important economic objective, thus that it “was conceived as a way of completing the single market” (Grant, 2013). He and McNelis (2013) point out that the euro was not only a political project but he also admits that the economic expectations related to this project were mistaken. They state that the euro was a project with the goal to enhance political cohesion in Europe which begun with the creation of the Common Market in 1957. McNelis (2013) also emphasizes that an important economic argument for the inception of monetary union in Europe “is enhanced price competition, since goods and services would be priced in a single currency, which in turn would lead to greater transparency about relative costs across borders, thus increasing the efficiency of making financial decisions” (McNelis, 2013). He argues that all of this, the countries hoped, would pave the way toward greater convergence in economic growth and economic performance across the Euro Area. However he also states that the introduction of the euro was connected with waiver of countries’ independent monetary policies and of option of currency devaluation to regain their competitiveness, relative to other countries. Thus the assumption that a common currency would generate economic convergence and political unity was unfortunately misleading and had a contrary effect (Baimbridge et al., 2012). A good example is the divergence between peripheral Eurozone countries and Germany. The GIIPS countries have extraordinarily high unemployment rates and their ratios of debt to gross domestic product are at least unpleasant (McNelis, 2013).

In order to prevent that any country or group of European countries gains a strategic advantage in weapon production with the intention to create a common market for that particular commodity, the Treaty establishing the European Coal and Steel Community has been signed as first step on the way towards free and prosperous Europe. With the ambition to ensure the control of nuclear energy in Europe, in 1957 the European Atomic Energy Community has been formed and in order to strengthen the economic cooperation between the signatory countries, the Treaty establishing the European Economic Community was signed within the same year with objective to ensure economic and social progress of participating countries, the constant improvement of living and working condition for the people living in those countries, to ensure and strengthen piece and liberty in Europe by implementing common actions when removing barriers that divide it.

While the objective of the Treaty establishing the European Economic Community was supposed to create a common European market, according to the Single European act that has been signed in 1986, the common European market should be created. The positive aspect of the ongoing integration has been, for example upholding the principle of four freedoms -

free movement of goods, services, capital and labor, but its serious negative aspect has been the strengthening of aggressive European political integration that leads towards the creation of European economic and political union (European commission, 2015).

An important milestone of the primarily politically motivated European unification has been the signing of the Treaty on European Union in 1992 that included an agreement of the signatory countries about establishing a single common currency - the Euro. Although this step has been justified by politicians and political scientists as a necessary step for the proper functioning of the single market in the Euro Area, in fact it has been more a political than an economic decision. It is confirmed by the divergence in opinions of economists about the possible positive impact of this decision on the social, economic, structural and institutional group of heterogeneous countries, as the Euro Area undoubtedly is. Also the economists had concerns about the establishment of conditions of the common currency, later also about the rules for countries joining the new Euro Area and about the constantly changing and increasingly riskier conditions for its members. As a result, the closer integration and harmonization in the Euro Area has been pursued, but in fact there were few exceptions when approving acts in the Union, depending on the situation and individual interests of particular countries.

An important sign of the dominance of political objectives of European integration was also ignoring the opinion and the willingness of the citizens of member countries to form the proposed monetary union, respectively to enter such monetary union with strongly heterogeneous members and acknowledging rational reasons against its creation. Recent crises and problems that Euro Area challenges in the last years, they support the belief that the unity and solidarity of its members require the conduction of a variety of common economic policy actions to preserve stronger mutual economic convergence among member countries. This is also confirmed by many studies that are emphasizing significant economic disparities in the Euro Area, classifying its countries to several significantly different groups (Artis and Zhang; 2002; Nechio, 2011; Holinski et al., 2012; Monford et al., 2013) and claiming that the economic divergence of the Euro Area member countries is significant, and it’s not decreasing over time.

The Design of the Euro Area

The second relevant group of the sources of current Euro Area crisis is, taking into account the aspect of European Integration, a group of causes related to the issue of the Euro Area design according to the Optimum Currency Area Theory. As stated in the previous part of this chapter, a basic and really important asymmetry was built into the Euro Area from its inception (Hall, 2012). Although Ishiyama (1975, p. 378) concluded his review with the following obituary: "the theory of optimum currency areas is primarily a stochastic discussion which contributes little to practical problems of exchange rate policy and monetary reform" (Tavlas, 2009). Thus also use of the OCA theory related arguments can be disputable as well.

In general, the Euro Area is namely what is well known as a currency area. A number of independent nations share a common currency, have a common monetary authority and a common monetary policy and also have debts denominated in the common currency but still have their own independent fiscal policies for government spending and taxation. Thus, the countries do not have political accountability to the currency union about how they tax and spend. And this is the reason why they run up their debts. Therefore just "this combination of complete monetary union with little or no fiscal coordination or accountability is the Achilles` heel of the euro zone" (McNelis, 2013). In the case of Euro Area is also the problem the common monetary authority, that have in the monetary union a function of a lender of last resort to banks but which have in the individual Euro Area member states only a limited supervisory authority over other banks, thus its activities in the area are relatively limited. It means, while the ECB has the responsibility to be a lender of last resort to the banks in the euro zone, each country has its own banking supervision laws and its own national accounting practices and standards. Also the too late reaction of the ECB to the debt problems in the Euro Area was criticized. Therefore it is easy to state that the introduction of the euro was probably premature for many actual Euro Area countries and that the Euro Area is obviously not an optimum currency area, or a region for which it is optimal to have its own currency and its own monetary policy, while the optimality is defined in terms of the attainment of both internal balance and external balance (Tavlas 2009; McNelis, 2013).

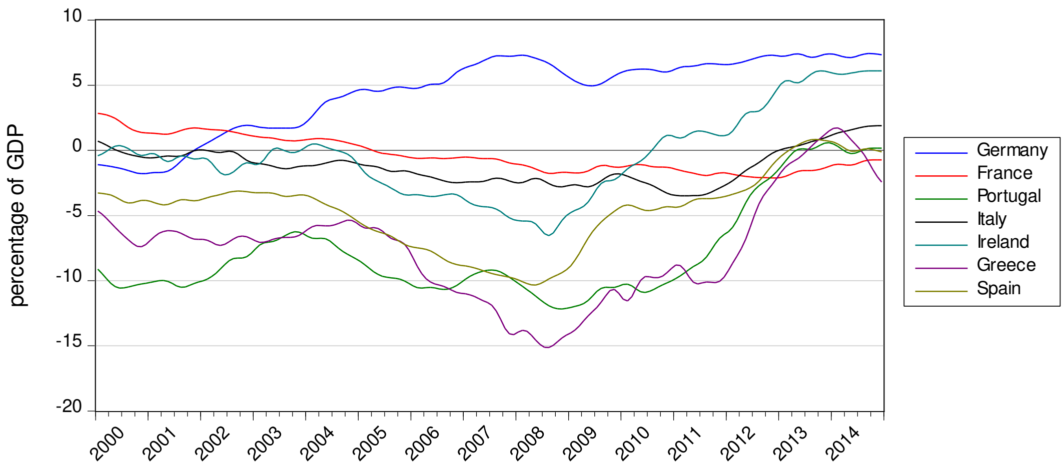
Also the analysis of the ability of the Euro Area to fulfil the criteria of the Optimum Currency Area theory for creation of an optimum currency area requires highlighting various discrepancies (Jager and Hafner, 2013). Mundell together with McKinnon and with Kenen recognized that forming a monetary union requires giving up the ability to realize an independent monetary policy and the ability to adjust the exchange rate of a national currency. They stressed that separate currencies among economies increased the transactions costs and information costs of money, and resulted in relatively thin foreign exchange markets, raising both the volatility of prices in those markets and the ability of speculators to influence prices. To help guide the decision whether a country should join a monetary union, those authors namely proposed criteria that could help alleviate the loss of an independent monetary policy and the exchange rate tool among countries participating in a monetary union Mundell (1961). emphasizes the importance of the factor mobility, which can help take the place of exchange-rate adjustments, especially he made it clear that it can be the labor mobility as well as the capital mobility. Also Eichengreen (1997) explored the importance of the capital mobility in the short run. Their idea was that, where such mobility exists, adjustments to shocks can be spread out over a longer time period than otherwise. McKinnon (1963) put the accent on the openness of the economy. Kenen (1967) considered fiscal integration as a key criterion. He also argued that economies with either similar, but narrow, production structures or with diversified production structures are suited to form a monetary union. Mussa et al. (2000) pointed out that the quantity of reserves should be a factor guiding the choice of exchange-rate regimes (Tavlas 2009). Thus, while Eichengreen (1991) and Krugman (1998) highlight the increase in regional specialization and the reduction in income correlation under a common currency, Frankel and Rose (1998) point out greater trade integration leading to more correlated business cycles, results that speak against and for optimality respectively (Cesarano, 2013).

It is therefore clear that the set of criteria of suitability for membership in a currency union includes two groups of criteria. The first group consists of criteria that reduce the exposure of member states to asymmetric shocks. This group includes similarity of economic structure, intraregional trade and a really low degree of specialization. The second group contains criteria that facilitate the adjustment of the member states to asymmetric shocks and includes homogeneity of preferences of the member states, factor mobility and good functioning system of transfer payments. It is also important to add that the authors of the OCA theory defines an asymmetric macroeconomic shocks as a shocks “if only one part of the currency union is hit by the shock while the other part is spared or if member countries differ widely in terms of the shock`s impact on their economies” (Jager a Hafner, 2013).

Krugman (1979) defines a balance of payments crisis as the government's inability to defend fixed parities due to the limitation of its power and according to the authors of the Optimum Currency Area Theory (OCA Theory: Fleming, 1971; Kenen, 1967; McKinnon, 1963; Mundell, 1961), the money is an economic instrument which has, in the case of an independent state with its own currency, a key role in the absorption of economic imbalances (such as loss of competitiveness, or unemployment). Thus, when a countries decide to abandon its currency and to join a monetary union, they deprive themselves of an important instruments used to smooth out the internal and external imbalances emerging in the currency union (Guerreiro, 2014; De Grauwe and Yueimei, 2013; Calice et al., 2013).

As such, the proponents of OCA theory are talking about the existence of certain "trade-off" between the homogeneity of countries belonging to a monetary union and the existence of real adjustment mechanisms that would operate in the currency union. A very close similarity of the union members should, in fact, prevent from the occurrence of asymmetric shocks caused by imbalances in the union, and the presence of functional adjustment mechanisms should preserve that the currency union and its members will recover from these asymmetric shocks in the case that their homogeneity is not sufficient. As a result, a monetary union in which none of the above mentioned conditions are present is considered (by the creators of the OCA theory) to be a suboptimal monetary area. In such a case, fixed exchange rate, representing the rule "one-size-fits-all" accompanied by the single monetary policy is by no means an adequate regime for preserving its current internal and external balance. In such a monetary union, a non-compliance of PPP can happen among its members, which in turn leads to external imbalances. Persistence of such imbalances can easily turn into the crisis of balance of payments and, finally, even a sovereign debt crisis (Guerreiro, 2014; Cuestas and Steahr, 2013).

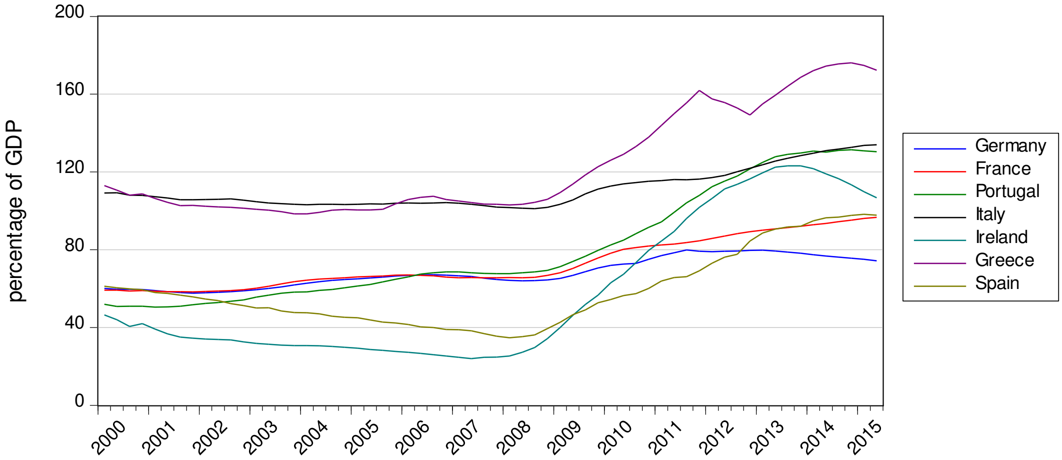
Figure 2 Current Account Imbalances within the Euro Area



Source: Compiled by author based on data taken from IMF - International Financial Statistics (November 2015).

Non-optimality of the Euro Area is also confirmed by Manolopoulos (2011), saying that the design of the Euro Area differs significantly from the design of optimum currency area, which was based on criteria of OCA theory. The above mentioned scenario describing the origin of the sovereign debt crisis in the Euro Area is further supported by Figure 2 (large current account imbalances) and Figure 3 (significant accumulation of sovereign debts). Countries with a higher and faster growing public debt are also experiencing large current account deficits (Gros, 2012; Sklias et al., 2014). Due to low labor force mobility, lack of fiscal transfers, artificial suppression of the German unit labor costs, politics, inflationary policy that serves mainly the countries with surpluses, and low level of diversification of the economies of its members, we must consider the idea of introduction of a single currency by the Maastricht Treaty in 1992 as relatively irrational decision (Detlef, 2012; Persson, 2011). Therefore also Jager and Hafner point out that euro area is „a combination of rapid capital migration and limited labor migration" rather than an economically well-integrated currency union (Jager and Hafner, 2013).

Figure 3 Government Debt in the Euro Area



Source: Compiled by author based on data taken from IMF - International Financial Statistics (November 2015).

Bonatti and Fracasso (2013) state that since the establishment of the Euro Area, intra-European current account imbalances have grown significantly. It reflects diverging trends in competitiveness between core countries and periphery countries of the Euro Area. Introduction of the single currency and the single monetary policy significantly contributed to this divergent trend. Similarly, Cesaratto (2015) insists that the Euro Area sovereign debt crisis is a balance of payments crisis, tied to current account deficits and capital outflows (Lavoie, 2015). De Grauwe (2013) supports this opinion and he argues that the absence of a sovereign central bank caused a liquidity crisis followed by a solvency crisis in the Euro Area. He states that Euro Area member states had to issue debt in a new currency that is not under their control (De Grauwe, 2013; Caseratto, 2015).

Additionally, Weeks (2014) argues that when the global financial and economic crisis struck the continent in 2008, the trade-based deficits of the periphery countries of the Euro Area proved unsustainable. "With the exception of Greece, neither public debts nor fiscal deficits represented a major problem among Euro Area countries prior to 2008" (Weeks, 2014). However, for example Brancaccio (2012) states that internal imbalances in the Euro Area are an integral part of a monetary union attributable to the greater degree of financial integration between the Euro Area member countries and thus it depends only on by the individual country followed theoretical approach to the issue how to secure economic growth.

However, Lavoie (2015) argues that although the continuous loss of foreign reserves must lead to some adjustment, Euro Area member countries can never run out of TARGET 2 balances, because TARGET 2 balance can take unlimited negative values. Therefore, the evolution of the balance of payments cannot be considered as the source of the current crisis in the Euro Area. He sets a parallel between Keynes's proposal of an International Clearing Union and TARGET 2, but he states that TARGET 2 is less constraining than Keynes's Plan because TARGET 2 has no limits as to the size of advances that can be taken by national central banks from the ECB, which acts in the Euro Area as the international clearing agency (Lavoie 2015; Caseratto, 2015). He recognizes the main cause of the European sovereign debt crisis in the long-run absence of a credible lender of last resort in the Euro Area, which explains the speculative attacks against the securities issued by the governments of the Euro Area periphery countries. Therefore, he and Frenkel (2012) see true causes of the crisis on the side of investors, in the set up and self-imposed constraints of the ECB and in the imperfect institutional design of the Euro Area.

Sinn and Wollmershäuser (2012) emphasize that the root of the current European sovereign debt crisis lies in the external imbalances between its core and periphery countries and they claim that these imbalances occur as a reaction on optimistic expectations about income convergence generated in the Euro Area and as a reaction on an investment boom in the Euro Area periphery, which was accompanied by ballooning current account deficits financed by private capital inflows (Bonatti and Fracasso, 2013). According to Bonatti and Fracasso (2013) and Chen et al. (2013) the situation turned sour only when Greece was fingered and when ECB and other international organizations decided to embark on the fiscal consolidation.

Grahl (2011) therefore recommends the Euro Area to create an adjustment mechanism to smooth out the imbalances arising between the surplus and deficit members. Sklias et al. (2014) criticizes the absence of European mechanism for fiscal transfers. Eichengreen (1991) has the same opinion and proposes a system of budgetary transfers in the form of injections of liquidity between the individual countries of the Euro Area, a creation of suitable system of redistributing policies and central fiscal authority (Dibooglu a Horváth, 1997). Varoufakis

(2012) assumes that this necessary type of “recycling” of budget surpluses can have either the form of standard money transfers between countries or the form of transnational investments in production in countries and regions with a deficit (Sklias et al., 2014; Chen et al., 2013). Also Jager and Hafner (2013) point out that in the case of asymmetric shock, a transfer payments system is a valuable feature in a currency union that helps to effectively re-establish economic equilibrium.

In general, the current European sovereign debt crisis sparked a debate about creation of a fiscal union in Europe. Mac Dougall et al. (1977) and De Grauwe (2009) state that public finance in existing economic union plays a major role in eliminating short term fluctuations and cyclical fluctuations. They say that there is no such mechanism in the Euro Area and that this is an important reason why in present circumstances monetary union in Europe is impracticable (Bargain et al., 2013). Many economists similarly warn that the Euro Area is too heterogeneous and thus far from being an optimum currency area. Therefore, the Euro Area will be fragile and vulnerable to economic shocks unless complemented by more fiscal and political integration. Schuknecht et al. (2011) emphasize the importance of fiscal discipline and proposing an independent fiscal council for the Euro Area with the aim of improving governance and compliance.

Fuest and Peichl (2012) suggest some possible elements of a European fiscal union, namely: fiscal rules for the Euro Area member states, a crisis resolution mechanism, a joint guarantee for government debt, a mechanism of fiscal transfers between Euro Area countries, and an extended European budget and European taxes. Bargain et al. (2013) studied effects of a European tax and transfer system and of a fiscal equalization mechanism on the income distribution and automatic stabilizers in the Euro Area. He finds that replacing one third of the national tax-benefit systems with a new European system would lead to significant redistributive effects both within and across Euro Area countries. Introducing a fiscal equalization mechanism would redistribute revenues from high to low income countries, but according his opinion the stabilization properties of this mechanism are ambiguous. He also argues that strengthening of fiscal discipline alone is not sufficient.

The main argument in favor of deeper fiscal integration in Europe is also that it might improve macroeconomic stability in the Euro Area, increase the transparency and improve democratic control of EU policies. However, fiscal integration raises various concerns and the political enforceability of such integration is disputable. Although some economists argue that the unprecedented divorce between the main monetary and fiscal authorities offers advantages in limiting political influence on monetary policy, the current European sovereign debt crisis has renewed doubts about the wisdom of this approach (Goodhart, 1998, Beetsma and Bovenberg, 1998; Beetsma and Giuliodori, 2010).

The European sovereign debt crisis is therefore a balance of payments crisis, which arose and became persistent due to the presence of large external imbalances of members of the Euro Area in relation to their main partners in the Euro Area. It is also necessary to draw attention to the unique position of Germany in the Euro Area as a leading export nation and therefore not only to propose the requirement of an effective system of fiscal transfers in the Euro Area, but also the need to set certain limits on its internal trade that would prevent the emergence and development of a "fatal addiction" among its members similar to that between China and the USA. An increasing number of economists considers German neomercantilist policies as one of the main causes of the current European sovereign debt crisis (Sinn, 2007; Bonatti and Fracasso, 2013; Kaindl, 2013; Caseratto, 2015).

And because the growth strategy of German economy included an "agreement with trade unions for real wage restraint, reduction of labor protection to allow for reduced wages at the low end of a segmented labor market" (Constant and Massey, 2003), and de facto large export subsidies through tax incentives linked to exports, Germany is seen as the main beneficiary of the euro as well as the main reason of the problems of the Euro Area. Germany was criticized regarding to its entry the Eurozone at an uncompetitive exchange rate and regarding to its wage moderation that was equal to a real devaluation against other members in the Euro Area (Young and Semmler, 2011). Also Jager and Hafner (2013) confirmed that competitiveness of Germany has increased since the introduction of the euro (Jager and Hafner, 2013; Baimbridge et al., 2012).

Therefore, Germany now needs to reconsider its position and its steps because "the only way for other Euro Area countries to lower fiscal deficits without their economies collapsing is through a huge net export expansion, based upon both improved productivity and crucially buoyant external demand" (Baimbridge et al., 2012).

The amount of newly created euros and for some Euro Area countries the interest rate which was maintained too low by the ECB, have radically reduced the cost of loans for private sector entities in the peripheral Euro Area countries. In these peripheral countries a formation of bubbles started appearing (i.e. the real mortgage markets in Spain and Ireland or the public sector in Greece) (Stein, 2011; Baimbridge et al., 2012; Soares et al., 2014). Thanks to the support from the government, the euro-illusion of homogeneous Europe, despite its negative consequences, was still growing. There has been a deepening economic recession and moral hazard on the part of ECB and Euro Area governments, which under the temptation of the low cost borrowing and the newly established guarantee of rescue in case of difficulties, decided to "gamble for redemption" from the problems associated with external influences and their irresponsible deficit management (Stein, 2011).

It can be said that that Euro and the membership in the Euro Area are generally increasing the risk of endogenously caused, self-fulfilling crisis, both when talking about crises caused by self-fulfilling panic in the financial markets, as well as in those of the crisis which are caused by reckless behavior of "Panglossian" borrowers (Cohen and Villemot, 2014). Therefore, considering that the basic determinant of the self-fulfilling crisis is the starting level of public debt of an individual country, it is necessary to reassess the adequacy of existing rules of fiscal discipline in the Euro Area.

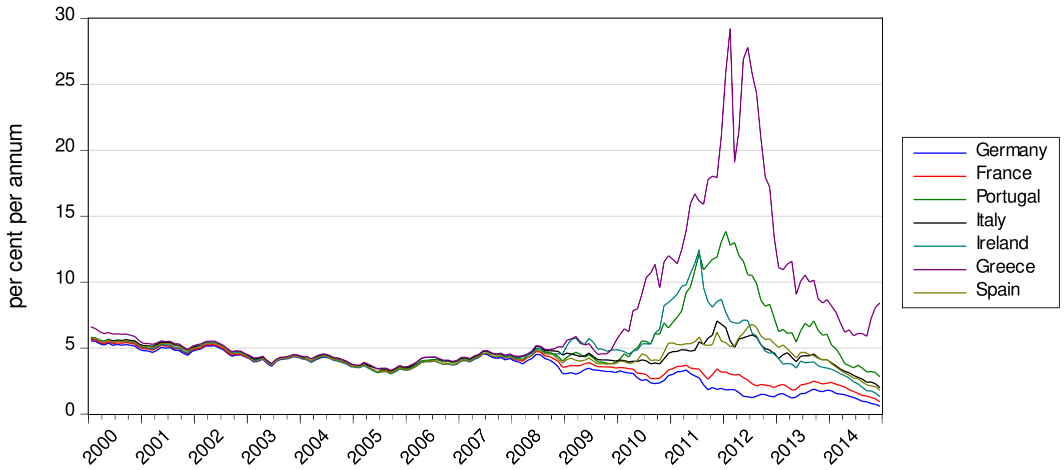
The Euro-Illusion and Economic Myths of Euro Area

The third relevant group of the systematic causes behind the current European Sovereign Debt Crisis, considering a clarification of the main aspects of the European integration, is represented by a group of sources related to the euro-illusion and economical myths of the Euro Area. "The euro has been promoted on the basis of spreading of myths and illusions which fail to respect economic principles, which postulated a prerequisite for a common market, competition and economic integration in Europe that are the one and only (the administratively established - fiat) currency and harmonized conditions" (Gonda, 2012). The general preconditions for a trouble-free and efficient functioning of the market, however, are unrestricted competition supported by diversity and the absence of core barriers to the free exchange (Arghyrou and Kontonikas, 2012).

At the same time, the arguments that strict compliance of the Maastricht criteria and the fiscal rules in their current form, without a working and automatically acting sanctioning mechanism, will preserve trouble-free functioning of the monetary union with heterogeneous members, which the Euro Area undoubtedly is, are very optimistic. The formerly listed rules are, in fact, mainly administrative measures. For many countries, the above mentioned compliance can prove to be inappropriate and even harmful. They are often perceived as a strong stranglehold of their economic growth, as a factor which deepens the disparity between economies and as a reason for their deterioration. Also De Grauwe (1995) states that the criteria are not based on arguments of economic theory but they result from political economy of monetary union in Europe. For example, in 1994, only Luxembourg satisfied these conditions and many of current Euro Area member states do not satisfy some of these conditions now. As a result, there is a great likelihood that these convergence requirements will have the effect of keeping the monetary union small. Already De Grauwe (1995) warns that the Maastricht criteria will be ineffective. Moreover, they have no root in the OCA theory. The relevance of the criteria consists, according his opinion, only in two elements. One has to do with the hegemonic position of Germany in the Euro Area, the other with the possible inflation bias of the monetary union caused by inflation development in Germany in the time introducing of the euro.

Marelli and Signorelli (2010) have highlighted the complexities between nominal convergence and real convergence of the Euro Area countries. The OCA theory also indicates the existence of functional chain between these forms of economic convergence and emphasizes the task that real convergence plays in creating an effective monetary union, which would be able to yield pure growing benefits out of its existence. On the other hand, many authors are pointing out that the benefits of a nominal convergence manifest themselves rather macroeconomically unstable economies at later stages. They argue that balancing the disparities in the structural conditions of the Euro Area member countries, the growth of their economic openness and the effects of fortifying the integration of international trade within the Euro Area require many years, if not decades. De Grauwe and Yueimei (2013) point out the possible short-term negative effect on the economic growth of the Euro Area member countries when enforcing adherence to the criteria of nominal convergence. Efforts to maintain the criteria of nominal convergence and fiscal discipline rules often lead to the enforcement of restrictive economic policies, and thus to introducing measures that slow down economic efficiency and performance and support economic divergence among member countries.

Figure 4 Long-term Government Bond Yields in the Euro Area (10 years maturity)



Source: Compiled by author based on data taken from IMF - International Financial Statistics (November 2015).

Opinions on the criteria of nominal convergence and the rules of fiscal discipline pushed in the Euro Area are generally quite divergent. Buiter (2004) underestimates the role of an inflation criterion, criteria of progress in long-term interest rates and criteria of the exchange rate control, and only highlights the criteria for fiscal sustainability. On the other hand, De Grauwe and Schnabi (2005) who emphasize the conflict between nominal and real convergence, emphasize just the requirement for stability of exchange rates.

A single currency also means one central bank for all Euro Area countries, with one interest rate regardless of the economic level and national competitiveness of the country. A system of unspoken guarantee was formed, promising the weaker members to be rescued by the stronger, and a dangerous illusion of prosperity in Euro Area was created (Gibson et al., 2012). While before entering the Euro Area countries paid a premium corresponding to the state of their economies for the money borrowed on the financial markets, the introduction of euro has reconciled the development and the level of interest rates on government loans. Thus, as shown in Figure 4, since the idea of a common currency was adopted, interest rates of the peripheral economies have stabilized and moved to the level of interest rates the core countries (i.e. Germany and France) (Gajewski, 2014).

Euro Economic and Euro-Political Factors

The fourth and last relevant group of the causes behind the current European Sovereign Debt Crisis is represented by a group of sources associated with the euro-political factors. The European Sovereign Debt Crisis has highlighted the fact that having a single currency and a “one-size-fits-all” monetary policy prolongs and deepens the economic cycles and supports the growth of debt in the Euro Area member countries. At the same time it confirmed, that a single monetary policy conducted in the Euro Area wasn’t equally desirable for all of its members. It was only apparently convenient for the core countries, while being too expansive and harmful for the peripheral countries (Lothian, 2014; Panico, 2010; Crowley and Lee, 2009). Initially the ECB adopted a low interest rate policy in 2002-2003. The policy stimulated financial speculation. However, after 2005 it changed strategy so that interest rates climbed until the autumn 2008 crash. Its goal was to curb “external inflation” despite an already tight monetary environment (Baimbridge et al., 2012).

Huge capital inflows had an identically negative impact on the debt in the Euro Area, as reported by all stressed countries during the period leading to the crisis. These capital inflows reflected the belief of the investors to the “Euro Illusion”. These large capital inflows were accompanied by a substantial reduction in long-term bonds, a large increase in the growth rate of money and credit supply, the relatively sharp increase in price levels and a deterioration of competitiveness. All these factors demotivated governments of the Euro Area members to implement reforms to comply with the budgetary constraints to which they are committed (Dellas and Tavlas, 2012; Lothian, 2014).

5. Conclusion

The Euro is essentially a political project with an unprecedented character. Namely the adoption of a common fiat money, common monetary authority and common monetary policy by a large number of independent and heterogeneous countries (insufficient progress in cyclical and structural convergence), but still without any better fiscal integration or coordination, attracts great attention worldwide, particularly with regard to its long-term prospects (Hall, 2012; Baimbridge et al., 2012). It is questionable, what is the optimum number of countries participating in the common European currency so that the Euro Area can be considered as the optimum currency area and what are the necessary integration forms for effective functioning of this currency area. Especially the political integration issue is an important subject of a further discussion. This admits also Bordo (2004), which states that monetary union without political union proved to be short-lived (Bordo 2004). The prevalence of the one-money-one-country pattern is namely a striking regularity, something like a general natural law, which clashes with the implications of the Optimum Currency Area Theory (Cesarano, 2013). Consistent with this opinion is also the current Eurozone crisis considered as a result of a large failure of political will, because the proximate cause of declining confidence in the bond markets lay in increases in public or private sector debt that might have been avoided if governments had taken steps to limit it. Additionally, some economists claim that the crisis might have been prevented by more assertive structural reforms focused on competition in markets for goods and production factors. They also stress the importance of coordination of strategies for preserving a sustainability of economic growth in the Euro Area and the fact that degree of financial integration is unequal in several countries using the euro (Cesarano, 2013; Ferreira et al., 2016). Eichengreen et al (2014) also emphasizes the crucial roles of the real exchange rate, of the external environment, i.e. of external shocks, and of the debt restructuring.

Thus, by taking the role of financial market agents and rating agencies into account, the current Euro Area crisis is mainly the crisis of confidence. Moreover, the euro turned out to be a heavy burden for some periphery countries when the monetary union was hit by an asymmetric shock, i.e. by the financial crisis of 2007-2008 (Jager and Hafner, 2013). Also governing institutions of the Euro Area, the ECB and the European Commission, are generally seen as no subject to democratic accountability, let alone control (Baimbridge et al., 2012). Therefore, the solutions of the crisis have to be systemic and consistent. However, the results of previous actions indicate a lack of efficiency, do not solve its nature, but even worsen it, and move it into the future. They also have created a precedent of certain eligibility for salvation for all entities that fall into similar problems with the fulfilment of their debt obligations in the future, irrespective of the causes of these problems (Detlef, 2012). Forms of assistance to indebted countries and austerity measures underlying this aid depend namely on the sentiment in the financial market without a sufficient economic base (De Grauwe and Yueimei, 2013).

Considering that during the current crisis the Euro Area members cannot adjust interest rates or exchange rates to stabilize their economies, they have to find an another solution. One of the possible solutions is moral suasion and to castigating debtor countries for their lack of responsibility and for their profligacy. However, the effect of this solution is disputable, it has only short duration and it is not rational (Chick and Pettifor, 2011). More generally it indicates that implementation of austerity policies across the Euro Area has been asymmetric. Hence, if the euro is to prove permanent, it requires a firmly based equilibrating mechanism.

Relying on the OCA theory, according to which the euro area is clearly a sub-optimal currency area, and on views of Keynes, one can consider a working mechanism of fiscal transfers as an appropriate adjustment tool for smoothening out the imbalances between surplus and deficit Euro Area member countries (Sklias et al., 2014). However, implementation of such mechanism in the Euro Area requires establishment of a fiscal union and, despite the fact that centralization and regulation are one of the main problems of the Euro Area, a further strengthening of the political integration. A common European tax system, which would be complementary to existing national tax systems and a common European budget, is necessary (Baimbridge et al., 2012).

One of the possible ways of solving the current European debt crisis is to create some sort of the United States of Europe, i.e. a European (federal) state; similar to what Winston Churchill declares in his discourse in 1946. However, the basis for correct functioning of this state should be a suitable compromise between government interventionism and leases faire approach of government to the economy of the country. Keynes insists on the unavoidability of the government affecting the economy because of the uncertainty that is formed when relying on the free hand of the market. However, experience shows that excessive centralization and excessive government intervention in the economy only lead to the growth of costs and inefficiency. When handling this compromise, it is necessary to consider that alongside the government, the market is another factor capable of manipulating economic agents and influencing their decisions (Sklias et al., 2014).

When creating an adequate system of fiscal transfers in the Euro Area, again according to views of Keynes, it is necessary to ensure an expansionary effect of this mechanism in the years of economic recession and crisis. However it should be based on the rationalization of government expenditures. The fiscal transfers in the Euro Area on the supranational level would be able to mitigate the volatility of investments of the Euro Area in the turbulent years (Kuhn, 2014).

Considering fiscal centralization, it's appropriate to propose a common European tax system, which would be complementary to national tax systems. Major European investment projects should be founded. They would be realized in the peripheral Euro Area countries and would lead to more efficient use of resources in the Euro Area and would be an essential mechanism for preserving converging development of the Euro Area member countries. It is also important to implement sanctions for trade within the Euro Area, especially for countries with large surpluses on their current account, such as Germany. The funds that would flow from them could be part of a system of fiscal transfers in the Euro Area and could be invested in the development of deficient regions (Cesarano, 2013).

Establishment of a European super-state is obviously a last resort and not a very realistic solution. "It ignores constraints imposed by current political reality. It also intensifies long-held fears about the diminution of national sovereignty involved in closer integration, whereby such an attack upon the independence of nation-states camouflages the fact that the single currency project was inadequately conceived, ignoring many of the tenants of OCA theory in favor of a preference for a political "fix"" (Baimbridge et al., 2012). Thus, this strategy is at least politically impassable and would cause massive waves of nationalism and resistance against the idea that the disciplined countries would have to pay for the mistakes and irresponsibility of the less disciplined countries. Likewise, British Prime Minister David Cameron commented on the idea of closer political integration: "For us, the European Union is a means to an end - prosperity, stability, the anchor of freedom and democracy both within Europe and beyond her shores - not an end in itself" (Kuhn, 2014).

Of course, there are several other alternatives how to solve the Euro Area crisis, such as the managed or unmanaged breakdown of the Euro Area. For example Baimbridge et al. (2012), in this context suggests that “Germany could leave the single currency, taking Austria, Finland and the Netherlands (if they so desire) with it to form a German-mark area. Exiting from a position of strength would generate less panic, reducing the threat of bank runs and contagion. Many legal and technical challenges would remain, but the reputation of the Bundesbank would permit time to erect the required institutions and controls. The remaining euro countries would secure immediate gains from the devaluation of the slimmed-down currency, following a debt restructuring aimed at controlling private and public sector debt whilst promoting the demand required for economic growth. The demise of the currently constituted Euro Area would impose fewer costs than the status quo or alternative scenarios” (Brancaccio, 2012).

Controlled collapse of the Euro Area, however, it is unlikely alternative because in such a case, the European leaders would have to admit their failure and the failure of the euro project. However, this solution would be possible and real if the political prominent members of the Euro Area would be opened to compromises. Voluntary withdrawal of individual countries from the Euro Area would create a precedent and a wave of mass exodus from the Euro Area countries (Gonda, 2014). In such a case the proposal of a multi-speed monetary union could be the solution, in which the new members, or markedly underdeveloped countries of Euro Area would be inserted into a different regime of monetary policy. This measure would allow them to reduce the gap with other, more efficient and developed members of the union and sufficiently adapt to the conditions of a single currency. However, a crucial problem of this solution is the absence of sufficient data to indicate where this process of disintegration or fragmentation of the Euro Area might end (McNelis, 2013). Although Klaus (2004) is convinced that such a way from the problems of the Euro Area is real and he states: “My own experience with the termination of the Czechoslovak monetary union in February 1993 suggests that it can be done without serious costs, smoothly and efficiently” (Klaus, 2004).

“Current account imbalances among Euro Area members and the resulting accumulation of external private and public credit and debt appear to be further causes of instability. The gap between unit labor costs seems to be one of the determinants of trade imbalances. More specifically, Germany, despite its current account surplus, has adopted a policy of relative wage deflation in recent years that has increased this gap” (Brancaccio, 2012). According to him the possible paths are adjustment of effective demand and of unit labor costs in the Euro Area, i.e. introduction of an "European wage standard". It "may prompt countries with surpluses to generate higher growth in nominal wages, prices, and wage shares, thus helping to restore the balance in trade and safeguard European unity. This means that any asymmetric shocks would be absorbed through the flexibility of wages" (Brancaccio, 2012). Additionally, the adoption of adequate expansionary economic policies by countries with surpluses, and of the EU as a whole is necessary.

However, changes in the Euro Area regardless of the implementation of any concepts of solving its problems should necessarily include appropriate reforms and structural policies. These should be focused on employment and the labor market, to promote flexibility in wages and prices, to minimize bureaucracy and regulatory burden on businesses and the elimination of patents that are a significant drawback to progress and innovation in the Euro Area. Despite the shortcomings of the Euro Area and the euro projects, it is necessary to make an effort to sustain a common currency. Only the united Europe is competitive enough to its competitors on world markets, e.g. China and the USA. However, the question about the optimum design of the common currency union consisting of the European nations remains unanswered.

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