Economic 461 | Maymester 2014
The crisis and European Economic and Monetary Integration | Prof. Bruno Dallago
M-F 9AM-12:15PM | GA 06F

A guide to readings

Background reading: Baldwin, Richard and Charles Wyplosz (2012), *The Economics of European Integration*, 4th ed., New York: McGraw Hill

The book provides students with an accessible presentation of the facts, theories and controversies driving rapid change in the heart of Europe. The authors combine essential elements of European history, institutions, law, politics and policies with clear and accessible explanations of the economic principles of European integration. The result is an expert analysis of the contemporary status of integration within the European Union.

Note: Background reading is a reference text for those who do not have a deep knowledge of the European integration. The background reading is not part of the exam. All other readings are required for the exam.

1. The long-run perspective and the context:

Issues:

- Introduction to the European Union and the crisis
- The long-term view: the United States and the European Union
- Globalization, financialization, deregulation, and the new economy
- The roaring Nineties
- The European Union: internal convergence and divergence, inequalities and vulnerability
- Europe: A declining continent or a continent in transformation crisis?

Discussion/reflection questions

- What is exceptional or particular in the European integration compared to other cases (e.g. NAFTA)
- What is your view of the leading motives for the European integration and how do they interact with economic structures and situation?
- Why is the context so important for the European Union?

Required reading:

Faini Riccardo (2004), 'Europe: A Continent in decline?' (http://www.dagliano.unimi.it/media/98.pdf)

It was a common perception, on both sides of the Atlantic, during the 1990s that the European economy performed poorly when compared to that of the United States. While the latter's GDP grew at an average annual rate of 3.2 percent, the European Union's managed only an annual average increase of 2.1 percent. Moreover, the world's export share of the large Continental economies sharply declined, while the United States was able to achieve a slight increase in its share of total world trade. More importantly still, labor productivity growth in Europe remained higher than in the United States until the mid-1990s, after which time, however, productivity growth in the United States was more than twice as fast as that of the European Union. It is likely, therefore, that the 1990s witnessed a break in the long-established postwar trends that saw Western Europe and Japan catching up with the United States after losing ground for over a century prior to 1950.

Additional readings:

Ash, Ken (2013), The Implications of Global Value Chains for Trade Policy and Trade Agreement (http://www.unitn.it/files/download/31972/ash_tiva_polici_trento_nov_2013_k_ash.pdf)

Global value chains (GVCs) have become a dominant feature of world trade, encompassing developing, emerging, and developed economies. The whole process of producing goods, from raw materials to finished products, is increasingly carried out wherever the necessary skills and materials are available at competitive cost and quality. The growing fragmentation of production across borders highlights the need for countries to have an open, predictable and transparent trade and investment regime as tariffs, non-tariff barriers and other restrictive measures impact not only on foreign suppliers, but also on domestic producers. It also highlights the importance of an ambitious complementary policy agenda to leverage engagement in GVCs into more inclusive growth and employment. Finally, more interconnected economies characterized by GVCs can have implications for multilateral, plurilateral and regional trade agreements. The OECD is currently undertaking comprehensive statistical and analytical work that aims to shed light on the scale, nature and consequences of international production sharing. This note explores just one aspect - the implications of GVCs for trade policy and trade agreements.

Becker, Joachim and Johannes Jager (2011), From an Economic Crisis to a Crisis of European Integration (http://www.iippe.org/wiki/images/b/b7/CONF_2011_Joachim_Becker.pdf)

The crisis in the periphery of the EU is frequently addressed as crises of excess government debt (neo-classical theory) or of current account imbalances (Keynesian approach). In the paper we adopt a critical regulationist perspective in order to analyse the political economy of economic crisis and responses to it in Europe. A modified regulation approach allows analysing the transformations of structural forms at different scales. In addition, we adapt the regulation approach in order to classify the regimes of accumulation in the periphery and the core of the European Union. This allows analysing the asymmetric interaction of different regimes of accumulation and the resulting division of labour. It is found that the interaction of neo-mercantilist and financialized regimes of accumulation had postponed stagnating tendencies due to over-accumulation. We argue that this type of interaction and therefore the respective regimes of accumulation have reached their limits and are therefore in a structural crisis. Until yet, responses to the crisis intended to maintain the respective regimes of accumulation. This has led to a radicalisation of neo-liberalism.

Crafts, Nicholas (2006), 'The World Economy in the 1990s: a long-run perspective', in Paul Rhode and Gianni Toniolo, *The Global Economy in the 1990s. A long-run perspective*, Cambridge: Cambridge University Press, 2006 pp. 21-42 (http://eprints.lse.ac.uk/22334/1/WP87.pdf)

Nicholas Crafts finds that for the industrial countries as a whole there was no resurgence in total factor productivity (TFP) growth. He concludes that, despite the excitement of the 'new economy' in the United States and the international take-up of new electronic age technologies, there was no return to the TFP growth of the (1950–70) Golden Age. Crafts does find that, from other vantage points, the 1990s appear rich in novelties. The most notable potential breakthrough, both from a historical perspective and for its implications for the future of the international economy, is the rise of China to the rank of a world economic power. Between 1990 and 2000 the Chinese economy more than doubled its size in real terms, its share in the world economy growing from 7.8 to 12.5 percent (from 2.7 to 7.0 percent in manufacturing production). Growth acceleration in India was also outstanding by historical standards. As these two countries together accounted in the year 2000 for about 38 percent of the world's population, it may be argued that their recent growth performance brought about probably the biggest single improvement in human welfare anywhere, at any time.

The rapid growth of China and India brought about the second important change in the 1990s, already under way in the previous decade: the end, perhaps the reversal, of the increase in worldwide income inequality that characterized modern economic growth since it began in the early nineteenth century. If "divergence big time" was a key feature of the last century, then the 1990s highlight a true structural break in the economic history of the world. Crafts argues that welfare indicators such as the Human Development Index (HDI), which, in addition to income, takes into account education and mortality, have converged worldwide since the 1950s.

The whole African continent, and in particular its sub-Saharan part, did not share in the world's output surge of the 1990s. The continent's per capita GDP remained stagnant throughout the decade in real terms, declining from 28 to 24 percent of the world average between 1990 and 2000. At the end of the twentieth century Africa's poverty remained the world's most intractable development issue, underlying the failure of policies thus far undertaken and consigning to the twenty-first century what will probably turn out to be its most relevant economic challenge.

Two economic failures were specific to the 1990s: Japan and Russia. The two experiences differ greatly. Japan's performance was disappointing mostly in the light of its previous outstanding growth. Between 1990 and 2000 Japanese per capita GDP grew on average only by 0.8 percent per year, as against almost 6 percent over the previous four decades.

The case of the Russian Federation was one of the most serious economic failures in the 1990s, particularly in the light of the performance of the formerly centrally planned Eastern European economies and of Russia's claim to being a political and military superpower. In 2000 the per capita GDP of Russia was only two-thirds of that of Soviet Russia in 1990. Moreover, welfare indicators such as life expectancy had also dramatically declined and income distribution became vastly unequal.

Frieden, Jeffry, Michael Pettis, Dani Rodrik, and Ernesto Zedillo (2012), *After the Fall: The Future of Global Cooperation*, Geneva Reports on the World Economy 14, ICMB International Center For Monetary and Banking Studies, Geneva and Centre for Economic Policy Research, London (http://www.sss.ias.edu/files/pdfs/Rodrik/Research/After-the%20Fall-Future-Global-Cooperation.pdf)

The report looks at international cooperation focusing on identifying the issues that are most likely to benefit from cooperation, and on which the international community should focus its efforts. The authors' argument is very clear: international cooperation is difficult at the best of times, and these are not the best of times. Governments in the developed countries, beset by all manner of economic and financial difficulties, lack the political capital to spend on international cooperation; the demands of their domestic constituencies are too pressing. Governments in the large emerging economies may be under less domestic political pressure and so more inclined to cooperate, but they have very different incentives from their developed country counterparts. Cooperative agreements may therefore be difficult in general, and impossible in some areas. Since improving international cooperation will be very difficult for the foreseeable future, governments should concentrate their efforts on that issues where the gains are likely to be larger and the difficulties smaller. More precisely, progress is likely to be more difficult in trade policy and financial regulation, and the gains are likely to be smaller; governments should spend their political capital on other issues instead. They should focus on improving macroeconomic policy coordination as a means of preventing a resurgence of the global imbalances that helped trigger the crisis. The only way progress can be achieved is by focusing on a one key issue.

Jacoby, Wade and Sophie Meunier (2010), 'Europe and the Management of Globalization', *Journal of European Public Policy*, Vol. 17, N° 3, pp. 299–317 (http://www.princeton.edu/~smeunier/Jacoby%20Meunier%20JEPP%20pdf.pdf)

European policy-makers often speak of their efforts to 'manage globalization'. The Authors argue that the advocacy of managed globalization is more than a rhetorical device and indeed has been a primary driver of major European Union (EU) policies over the past 25 years. They sketch the outlines of the concept of managed globalization, raise broad questions about its extent, and describe five major mechanisms through which it has been pursued: (1) expanding policy scope; (2) exercising regulatory influence; (3) empowering international institutions; (4) enlarging the territorial sphere of EU influence; and (5) redistributing the costs of globalization. These mechanisms are neither entirely novel, nor are they necessarily effective, but they provide the contours of an approach to globalization that is neither ad hoc deregulation nor old-style economic protectionism.

Levine, Ross (2005), 'Finance and Growth: Theory and Evidence', in: Philippe Aghion and Steven N. Durlauf (eds.), *Handbook of Economic Growth, Volume 1A*, Elsevier, pp. 865-934 (also in http://thannaletchimy.webs.com/Topic%201.pdf)

This paper reviews, appraises, and critiques theoretical and empirical research on the connections between the operation of the financial system and economic growth. While subject to ample qualifications and countervailing views, the preponderance of evidence suggests that both financial intermediaries and markets matter for growth and that reverse causality alone is not driving this relationship. Furthermore, theory and evidence imply that better developed financial systems ease external financing constraints facing firms, which illuminates one mechanism through which financial development influences economic growth. The paper highlights many areas needing additional research.

Renda, Andrea (2013), 'Globalization, the New Geography of Power, and EU Policy Response', *Transworld*, Working Paper 10, march (http://www.iai.it/pdf/Transworld/TW_WP_10.pdf)

The globalization of the economy of the past two decades has created more challenges than opportunities for the EU. Already at the beginning of this century, the EU started feeling a heavy pressure from emerging economies, which led to a reshuffling of global GDP shares, the polarization of EU job markets and a gradual loss of competitiveness in several industry sectors. The economic downturn since 2008 has just exacerbated this process. Overall, this paper portraits a rather gloomy outlook for Europe's future role in the global economy: the EU suffers from major weaknesses at home, not least due to lack of political and economic integration and the prevalence of parochial instances in the trade negotiations. Current policy responses in the domain of trade policy, innovation and industrial policy do not seem likely to restore and ensure the EU's leading role in the global economy.

Stockhammer, Engelbert (2012), 'Rising Inequality as a Root Cause of the Present Crisis', Political Economy Research Institute, University of Massachusetts at Amherst, *Working Papers Series 282* (http://www.peri.umass.edu/fileadmin/pdf/working_papers/working_papers_251-300/WP282.pdf)

The paper argues that the economic imbalances that caused the present crisis should be thought of as the outcome of the interaction of the effects of financial deregulation with the macroeconomic effects of rising inequality. In this sense rising inequality should be regarded as a root cause of the present crisis. We identify four channels by which it has contributed to the crisis. First, rising inequality creates a downward pressure on aggregate demand since it is poorer income groups that have high marginal propensities to consume. Second, international financial deregulation has allowed countries to run larger current account deficits and for longer time periods. Thus, in reaction to potentially stagnant demand two growth models have emerged: a debt-led model and an export-led model. Third, (in the debt-led growth models) higher inequality has led to higher household debt as working class families have tried to keep up with social consumption norms despite stagnating or falling real wages. Fourth, rising inequality has increased the propensity to speculate as richer households tend hold riskier financial assets than other groups. The rise of hedge funds and of subprime derivatives in particular has been linked to rise of the superrich.