

# The Euro in Trouble

Source: <http://www.bbc.co.uk/news/business>



## The Euro was created

- to reduce trading costs
- to boom tourism
- to smooth the economy

The trouble started with governments spending more than they earn thus creating budget deficit.

By the mid-2010s many governments increased significantly their debts compared to their GDP.

And of course, lenders want their money back sooner or later, so if they don't see a promising debt service, interest rates will soar and borrowing becomes unaffordable. This could be the moment for governments to start to ask for emergency loans.

But these loans have to be paid back... The trouble is that the loans of one country affect financial markets all over the Eurozone. Somebody has to finance the loan. But is it a solution to exclude a country from the Eurozone? The slide-show suggests the opposite...

Click on the image above and watch the video and find the Hungarian equivalent of the English terms.

- |                      |                   |
|----------------------|-------------------|
| 1. crumble V         | összeomlik        |
| 2. rioting N         | adósság           |
| 3. boost V           | lázasítás         |
| 4. smooth V          | fertőzés          |
| 5. debt N            | hiányköltségvetés |
| 6. soar V            | megugrik          |
| 7. bail-out N        | megmentés         |
| 8. emergency loan N  | felélénkítő       |
| 9. contagion N       | kisimít           |
| 10. budget deficit N | vészkölcsön       |

Look at some of the slides and explain the story with your own words:

1999: Launch of the Euro  
*"Inspiration for the € symbol came from the Greek epsilon..."*  
*...crossed by two parallel lines*  
*to 'certify' the stability of the euro."*  
 European Commission

...the idea was

**Reduce trading costs**



...the idea was

**Boost tourism**



...the idea was

**Smooth the economy**



Most governments  
~~spend more than they earn.~~  
 spend more than they earn.



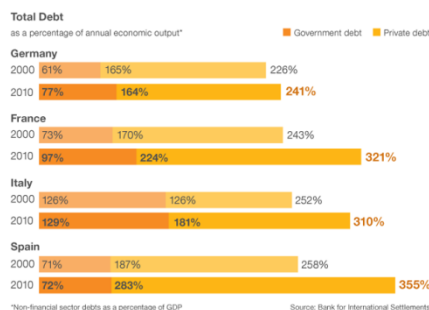
**€340bn**  
 total Greek debt  
**€31,000**  
 debt per person

**€25,915**  
 Average Greek salary 2008  
 Source: Eurostat



# The Euro in Trouble Version 2

Others analysts have a different opinion. Read version 2 to find out. What is the main difference between the two opinions?



There was a big build-up of debts in Spain and Italy before 2008, but it had nothing to do with governments. Instead it was the private sector - companies and mortgage borrowers - who were taking out loans. Interest rates had fallen to unprecedented lows in southern European countries when they joined the euro. And that encouraged a debt-fuelled boom.

## ...bad news for southern Europe

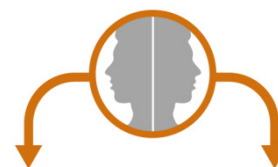
But debts are only part of the problem in Italy and Spain. During the boom years, wages rose and rose in the south (and in France). But German unions agreed to hold their wages steady. So Italian and Spanish workers now face a huge competitive price disadvantage. Indeed, this loss of competitiveness is the main reason why southern Europeans have been finding it so much harder to export than Germany.

## ...and a nasty dilemma

So to recap, government borrowing - which has ballooned since the 2008 global financial crisis - had very little to do with creating the current eurozone crisis in the first place, especially in Spain (Greece's government is the big exception here). So even if governments don't break the borrowing rules this time, that won't necessarily stop a similar crisis from happening all over again.

Spain and Italy are now facing nasty recessions, because no-one wants to spend. Companies and mortgage borrowers are too busy repaying their debts to spend more. Exports are uncompetitive. And now governments - whose borrowing has exploded since the 2008 financial crisis savaged their economies - have agreed to drastically cut their spending back as well.

But...



## cut spending...

...and you are pretty sure to deepen the recession. That probably means even more unemployment (already over 20% in Spain), which may push wages down to more competitive levels. Even so, lower wages will just make people's debts even harder to repay, meaning they are likely to cut their own spending even more, or stop repaying their debts. And lower wages may not even lead to a quick rise in exports, if all of your European export markets are in recession too. In any case, you can probably expect more strikes and protests, and more nervousness in financial markets about whether you really will stay in the euro.

## don't cut spending...

...and you risk a financial collapse. The amount you borrow each year has exploded since 2008 due to economic stagnation and high unemployment. But your economy looks to be chronically uncompetitive within the euro. So markets are liable to lose confidence in you - they may fear your economy is simply too weak to support your ballooning debt load. Meanwhile, other European governments may not have enough money to bail you out, and the European Central Bank says its mandate doesn't allow it to. And if they won't lend to you, why would anyone else?