

# The future of the European Economic and Monetary Union: European monetary and fiscal policies

Reinhard Neck<sup>1</sup>

Published online: 8 April 2016  
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NOeG 2015, the 2015 Annual Meeting of the Austrian Economic Association, took place in Klagenfurt, June 5–6, 2015. It was organized by the Department of Economics, Alpen-Adria-University Klagenfurt. The main theme of the conference was “The Future of the European Economic and Monetary Union—European Monetary and Fiscal Policies”. 55 papers dealing with macroeconomic policies in the European Union, especially the Euro Area, as well as other fields of economics were presented and discussed. Among the highlights were invited plenary papers by Mike Wickens (University of York), Seppo Honkapohja (Bank of Finland) and Ansgar Belke (University of Duisburg-Essen); and a plenary discussion on “The Future of the Euro” with Ansgar Belke, Peter Gauper (Raiffeisen Landesbank Kärnten), Thomas Gehrig (University of Vienna), Ewald Nowotny (Oesterreichische Nationalbank) and Willi Semmler (New School for Social Research, New York) as invited speakers. The present special issue of *Empirica—Journal of European Economics* contains the invited papers and a selection of papers from the conference devoted to the main topic of the conference. They were selected from a larger number of submissions following the usual refereeing process of the journal.

At the time of the conference, economic policy makers in the Euro Area were fully occupied with the “Greek tragedy” of exploding sovereign debt amidst a deep recession with record unemployment and negative growth. Several contributions to the conference and to this issue deal with that crisis, which not only affected Greece but the entire Euro Area. Although in the meantime the Greek crisis was mitigated, it cannot be regarded as having been solved. The crisis has several aspects,

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✉ Reinhard Neck  
reinhard.neck@aau.at

<sup>1</sup> Department of Economics, Alpen-Adria-University Klagenfurt, Universitätsstrasse 65-67, 9020 Klagenfurt, Austria

including heterogeneity among Euro Area countries in terms of public finances and of competitiveness. Michael Wickens shows that the debt crisis was largely the result of the “one size fits all” monetary policy, which led to inadequate price signals in financial markets. He also makes proposals for better governance in the Euro Area and for obtaining more reliable credit ratings in Europe. One effect of the crisis was the lowering of interest rates to near zero values in order to avoid monetary policy failures that have been made during the Great Depression. An additional impulse from monetary policy should, according to the central banks (including the ECB), come from quantitative easing, that is, large asset purchases by the central banks. Seppo Honkapohja presents a thorough theoretical analysis of the problems such a policy presents to central banks and gives a brief survey of empirical work on this topic. Alexander Haider and Willi Semmler deal with the problem of debt deflation and the possibility of a secular stagnation in the Euro Area, which is currently on top of the agenda of the European Central Bank. They show that especially the Southern periphery of the Euro Area is threatened by such an adverse development. Milan Damjanovic and Igor Masten propose an alternative measure of the monetary policy stance in times of near-zero interest rates, the so-called shadow short rate, which is derived from the yield curve. They show that shocks identified by this rate lead to similar macroeconomic responses as shocks identified by the standard policy rate and allow for meaningful interpretations of the effects of monetary policy measures in recent years.

In addition to monetary policy, fiscal policy has to be analyzed to arrive at recommendations for the European Economic and Monetary Union. One solution to the trade-off between low growth and high unemployment on the one hand and high government debt on the other is a change in the tax structure, consisting in reducing taxes on labour and production and increasing taxes on “unproductive” economic activities. The paper by Andreas Eder considers the inheritance tax as a possibility of generating revenues for the government without negative incentive effects. Instead, he shows that high untaxed inheritances even provide incentives for early retirement and thus may contribute to difficulties for the pension system. From a macroeconomic point of view, the paper by Reinhard Neck and Dmitri Blueschke investigates the interaction of monetary and fiscal policies in a simplified economic model, emphasizing strategic behavior of policy makers in a dynamic game context. They show that a cooperative solution (a fiscal and monetary union or pact) in most but not all cases turns out to be superior to the results of noncooperative behavior by different policy makers.

Trade policy issues are the subjects of the next two papers. Dominik Kronen and Ansgar Belke study the exports of Greece depending on the real exchange rate. Looking at sectoral exports, they show that there is a hysteresis phenomenon in the real exchange effect, meaning that within some “band of inaction” exports do not react. Mohd Hussein Kunroo, Irfan Ahmad Sofi and Naushad Ali Azad investigate the effects of the adoption of the euro on trade in the countries of the European Union, using a panel gravity approach. They conclude that over the decade since the introduction of the euro, intra-Euro Area trade has significantly increased and the Euro Area is on a path of convergence.

The final paper by Jing Zeng deals with the notoriously difficult problem of forecasting macroeconomic aggregates, which is exacerbated in the case of Euro Area aggregates due to the heterogeneity of the countries involved. Zeng points toward the importance of the weights used for aggregating country-specific forecasts and recommends using flexible combinations of weights for forecasting some variables. Including too many countries may introduce country-specific noise; hence combining only forecasts for the three largest European countries improves the forecast performance.

It remains to thank the sponsors of the conference and the resulting publication: Oesterreichische Nationalbank, Raiffeisen Landesbank Kärnten, Verein zur Förderung der Wirtschaftswissenschaften an der Alpen-Adria-Universität Klagenfurt, Forschungsrat der Alpen-Adria-Universität Klagenfurt aus Mitteln der Privatstiftung Kärntner Sparkasse, Fakultät für Wirtschaftswissenschaften der Alpen-Adria-Universität Klagenfurt, and Austrian Economic Association.