THE IMPACT OF THE CONVERGENCE CRITERIA ON THE STATES FROM THE EURO AREA

Assoc. Prof. Nicu Marcu Ph. D
University of Craiova
Faculty of Economics and Business Administration
Craiova, Romania

Abstract: A single currency can be imagined in countries with convergent economies. Only the States that respect the four convergence criteria can take part in euro. These convergence criteria are: without excessive public deficits, which means less than 3% from GDP for the annual public deficit and less than 60% from GDP for public debt; a reasonable inflation that must not exceed with more than 1,5% the three better national performances of the European Union during the precedent year; the respect of the fluctuation margins of the European Monetary System throughout the national currency for at least two years; the long term interest rates must not exceed with more than 2% on average the three countries with the lowest interest rates from the European Union. Having in mind these convergence criteria and the economic crisis we must be very careful.

JEL classification: G00, G01

Key words: economic crisis; convergence criteria; European Union; Maastricht Treaty; euro zone

1. INTRODUCTION

The budgetary system has some advantages that allow the reconsideration of the budgetary deficits. Wyplosz (1990) shows that the existence of a deficit can not be seen as a sign of indiscipline. For this, the author cites Diamond, Lucas, Stockley, Stiglitz and Weiss who developed arguments pro deficits.

Diamond (1956) established the capital stock efficiency criterion and showed that an economy can maintain a capital stock under the optimum level, even if it doesn't work ideally. Every supplementary accumulation of capital needs a sacrifice from the current generations, even if the benefit comes for the future generations. Surely the future generations will have to indemnify the current generations, but there is no market to allow this transfer between generations. Diamond showed that a budgetary deficit can allow reaching an optimal situation.

Lucas and Stockey (1983) come with another opinion. The authors remark that the governments succeed and because of the fact that they are not alike, a government reverses the fiscal orientations of the previous. This behavior creates an incertitude that encourages the private sector to create precaution measures so as to grow the distortions associated to the fiscal system in general. Lucas and Stockey show that a government can issue a debt and actives structure so as to determine the successors not to doubt the

initial choices. We are speaking here about an argument in favor of the public debt, even it is permanent.

Another argument is the case of the credit rationalization. Regarding this subject, the authors Stiglitz and Weiss (1981) proved that the banks with no perfect information on the loans are often determined to refuse a credit towards the solvable agents. Within these conditions, the government can ease the negative effects by taking a loan (i.e. the emission of a public debt) to finance the collective goods and services production that will be purchased by the private sector.

2. Objectives

The effects of the budgetary deficit on the activity depend on:

- the way of deficit financing (throughout the creation of currency and loan);
- the deficit cause (the diminishing of the incomes or the growth of the expenses);
- the expences composition (consumption, investment, debt);
- the fiscal structure (repartition between direct and indirect taxes);
- the level of opening towards the foreign countries (penetration degree);
- the nature of the saving behaviours;
- the anticipations of the economic agents.

It is advisable to take into consideration all these elements before judging the budgetary deficit of a country and its effects in time.

Beginning with the year 2008, the crisis hit all the European countries and caused the altering of the loan conditions for various States from the euro area, leading to a growing level of debt.

3. Methodology

The Maastricht treaty imposes strict rules on the national budgetary politics. These rules introduce some barriers regarding the public debt and the budgetary deficit of the member States of the Monetary Economic Union and represent criteria that have to be obeyed as part of it.

Scarifying the necessary flexibility for the decentralized budgetary politics responds to a very powerful preoccupation not to be exposed to the risk of the Monetary Economic Union destabilization throughout unsustainable national budgetary politics.

Thus, the Maastricht Treaty has some dispositions which target the fact that the public debt is not favored by the access to a large capital market the result of the creation of the monetary union.

4. Analysis

The Treaty excludes that the Central European Bank finances the debt of a member state or any other form of financial solidarity (the article 107 from the Treaty). From this perspective, two criteria can be used to make an appreciation on the member states budgetary politics:

- the ratio between the public deficit and GDP is not allowed to exceed 3%.
- the ratio between the public debt and GDP has to remain inferior to the percentage of 60%.

These rules will be appreciated and will serve, on one hand, as a precondition to enter in the Union and as a modality for the European Union to work. They focus on

the fact that the national budgetary policies will not risk the Union's monetary solvability on a short term.

The articles 2 and 3a reveal the meeting of the conditions for a durable and non inflationist growth, passing throughout a coordination of the economic policies, an attachment towards the public finances and the wealthy monetary conditions.

The articles 102a and 103a dispose that the coordination is assigned to the Council and the supervision of the economic and financial situations of every country is assigned to the Commission.

The article 104c allows the formulation of some instigation for the countries that fail to establish their finances. This article stipulates:

- The member States have to avoid the excessive public deficits;
- The Commission supervises the evolution of the budgetary situation and the amount of the public debt from the member states so as to diminish the errors.

The Commission examines if the budgetary discipline was respected based on two criteria:

a. The ratio between the public deficit or the effective public deficit and the GDP exceeds a value of reference if:
- the ratio was not diminished substantially and constantly and reaches a level close to the reference value;
- or the exceeding of the reference value is exceptional and temporary and the ratio stays close to the reference value;

b. The ratio between the public debt and GDP exceeds a reference value if at least this ratio does not sufficiently diminish and approaches the reference value in a satisfying rhythm.

We have to note the expression "at least" that attenuate the rules, letting the alternative to the States to continue a structural adjustment or to react to a temporary shock throughout an exceptional public deficit.

4.1 Critical

It is very probable that the ratio between debt and deficit evolves in an opposite way. Nothing proves that a country that meets a criterion goes straight towards meeting the other.

Contrary to the deficit reduction, the diminishing of the public debt implies a budgetary surplus. This fact can be seen as an incitement not to respect the criterion on the debt. If the deciders go for this temptation, the markets will have a rapid reaction and will not lose the opportunity to assure the State's solvability. Thus, the interest's rates will grow and the deficit will be higher, aggravating the debt problem. If the deciders will not look forward to respect the ratio of the debt, the market should be preoccupied to make them work.

5. CONCLUSIONS

It is possible that the debt criteria and the deficit are not the only possible incoherent terms of the monetary union. It is possible that the countries with a weak level of debt, with no prices diminishing or a reduction of their fiscal system will not abbey the inflation criterion. It is possible that they reach an inflation rate superior to that of the economies engaged into a restructure.

In conclusion, there are a high number of unsure situations that can lead to some conflicts between some convergence criteria established in the Maastricht Treaty. The problem is that, currently, nobody knows which criterion should predominate.

REFERENCES

1. Cristea, M. — Romanian Electronic System Of Interbank Payments In The Background Of Creating The Single Euro Payments Area. The Young Economists Journal, no 1/2007
2. Diamond, P. — National debt in a neo-classical growth model. American Economic Review, 1956
3. Echkenazi, J. — Guide de l'Union européenne, Paris: Nathan, 2007
4. Lucas, R Stokey N. — Optimal monetary and fiscal policy in an economy without capital. Journal of monetary economics, no 12/1983
5. Meghisan, G-M Meghisan, F. — Convergence strategies and telecommunications. International Conference Business Excellence, Transylvania University of Brasov, Romania, 15th-16th October 2010
6. Stiglitz, J. Weiss, A. — Credit rationing in markets with imperfect information. American Economic Review, 1981
7. Wyplosz, C. — Les implications bugetaires de l'Union monétaire. OFCE Journal, no 33/1990