THE EFFECTS OF THE ECONOMIC CRISIS ON THE PUBLIC DEBT OF THE MEMBER STATES OF EUROPEAN UNION[1]

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Abstract

This paper propose to analyze the causes and effects of the economic crisis on public debt of Member States of the European Union and the measures undertaken by specialized authorities of the countries affected by the sovereign debt crisis. Much of the blame for the debt crisis can be attributed to irresponsible fiscal policies practiced by some EU Member States, and another part due to reckless bank lending practices. Fiscal discipline is one of the key elements of macroeconomic stability and this is especially relevant in a monetary union and the euro area, composed of sovereign states retain their tax liability policies. In the euro area, monetary policies and exchange rates are no longer able to cope with country-specific imbalances.

Keywords: crisis, public debt, gross domestic product, euro-zone.

JEL Classification H, H6, H63

1.Introduction

Global economic activity has been slowing down during the last months, as a result of transitional factors, but also as a result of the tensions on financial markets. Regional differences still persist in relation to cycling position of the different savings.

In the advanced economies economic recovery remains weak, while it is found that moderate growth in emerging economies.

In the member countries of the European Union, the debt-to-GDP ratio increased from 80.0% at end-2010 to 82.5% in late 2011 and in the euro area from 85.3% to 87.2%. A total of 14 member states reported a debt level of 60% of GDP in 2011. In late 2011, the lowest share of government debt to GDP were recorded in Estonia (6.0%), Bulgaria (16.3%) and Luxembourg (18.2%).In 2011, the 21 member

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states, the share of public debt in GDP compared to 2010 and decreased for 6 member states: Germany, Estonia, Latvia, Luxembourg, Hungary and Sweden. The most significant increases in debt ratios between 2010 and 2011 were registered in Greece (20.4%, Ireland (15.7%), Portugal (14.4%) and Cyprus (10.2%).

2. State of the art

Public debt represents all internal and external obligations of the state at a time.[Stănescu Cristina ,Nedelescu Mihai, 2012]

The public debt means the state has a duty to third parties, such as individuals, businesses, banks, companies in the country or abroad, who bought bonds issued by the state to cover the financial needs of the state.

In 2011, the risks to euro area financial stability increased considerably in light of worsening sovereign debt crisis and increasing its negative effects on the banking sector. [Raport anual al Bancii Centrale Europene, 2012]

Uncontrolled growth of public debt is the main reason that investors punished European countries while keeping a climate of confidence in international financial markets

The budget is an important lever for the EU to deliver existing policy goals, to bring about change and to maximize the long-term impact of EU action.

Due to the difficult situation of the Greek economy, Greek authoritis were suggesting that leaving from the European Union and stop using the euro as the nation's currency. Still,as bad as things are for Greece, they're not alone in their struggles.

Another country with major problem's of public debt is the US, federal government's debt burden ($15.5 trillion) is larger than the country's entire economy, measured in terms of gross domestic product (GDP). The GDP is simply the total market value of all goods and services a country produces in a year.

The nation's debt to GDP ratio now exceeds 100%. It means that all of the goods and services produced in the United States in one year still wouldn't be enough to pay off our nation's debt.

Public debt rose from 64% of GDP in 2007 to 101.7% in 2012, amid massive public spending for reviving the economy and social expenditures of the U.S. administration. They rose from 35% of GDP before the crisis to over 40% and the deficit from 3% to 8%. These are numbers which would have worried any European state and would have led to a sustained increase in financing costs. [www.finanteazi.ro/2012]

The gross domestic product (GDP) is one the primary indicators used to gauge the health of a country's economy. It represents the total dollar value of all goods and services produced over a specific time period you can think of it as the size of the economy. Usually, GDP is expressed as a comparison to the previous quarter or year. For example, if the year-to-year GDP is up 3%, this is thought to mean that the economy has grown by 3% over the last year.[www.investopedia.com]

In the year 2012 it is estimated that debt level using the government methodology will be 33.9 % of the GDP, and, during the period 2013-2015 the estimated amount of government debt is below 33.5 % of the GDP was below the level required by the Maastricht Treaty of 60% of the GDP, and is an advantage for Romania, in view of the new rules relating to the level of public debt and budget deficit introduced by new rules of economic governess at European level, in which the concept of prudent budgetary policy becomes central.[Raport privind administrarea datoriei publice guvernamentale,2011]

At the end of the year 2010, the Romanian government debt level in accordance with the methodology ESA 95 has reached the 31,02 % of the GDP. Even if this indicator fits comfortably within the limit of 60% of the gross domestic product provided by the Maastricht Treaty, its rate of growth remains as technocrats. This is an additional reason for the adoption of a conduct proactive by continuing fiscal consolidation measures.

At the end of the year 2010 Romania ranks 4 between EU states with the lowest level of indebtedness that 31,0 % of GDP compared with Estonia (6.7 %), Bulgaria (16.3 %) and Luxembourg (19,1 %) . EU Member States with the highest level of indebtedness are: Greece (145%), Italy (118%),Belgium (96 %), Ireland (94) and Portugal (93%).

3. Causes of the global economic crisis and debt default of the Member States of the European Union

1. Most of come to crisis public debt can be traced to irresponsible fiscal policies practiced by certain Member States of the EU, and another part on bank loans imprudent practice, which has generated a real estate market.

2. Shares of large-scale rescue of the banking sector in certain Member States, financed with taxpayers' money, and frailty later world financial system have represented also important factors which have contributed to crisis. In the future there should be an effective reform of the banking sector worldwide, such as to prevent recurrence of such behaviors.

3. Public debt crisis - caused by the crises financial and tax – jeopardizes the existence of economic and monetary union (EMU) and require answers financial, economic and political effectiveness. This has highlighted in deficiencies of the Stability and Growth Pact as a mechanism of guarantee of fiscal responsibility in the Member States.

4. Fiscal discipline is one of key elements of macroeconomic stability and this is all the more relevant in a monetary union as well as euro area, made up of sovereign states that retain liability for their fiscal policies. In the euro area, national policies monetary and exchange rates are no longer able to make imbalances front

especifice each countries.[Comitetul Economic si Social European,2010]. Apparent failure in relation to the compliance with tax rules governing the EU is above current global financial crisis, it could be argued that the risks inability to pay for the monetary union is a second phase of the crisis. After more than a decade of increase in the volume of credit easy which led in the formation of bubbles in real estate and constructions, followed by economic implosions in some member states, the latter have been caught in spiral of debts. The Governments of Greece, Spain and Portugal have not had to resort to measures to save, financed by tax payers, their bank systems during financial crisis, but their difficulties related to the debt threatens to destabilize the banks in the entire EU. This illustrates that the measures to rescue the banks, financed by taxpayers, have not been the main cause of the increase in public debt.

6. In the banking crisis, it has been said often that some banks were "too big to be allowed to go bankrupt", and now they speak of member states, which is faced with government debt on the rise, as being "too large to be allowed to enter in defaulting". Even though at a conceptual level the government interventions to save the banks on the basis of the well known-principle “too big to fail” or “too many to fail”, was nothing more than another form of representing moral chance, in reality there are some situations in which the intervention of the government was mandatory. [Teodora Barbu, Georgeta Vintilă, Dan Armeanu, Mihai Nedelescu,2010] As tax payers have accepted with weight need to rescue the banks who have violated rules, are now prompted by international markets of the bonds an adjustment, which may be even higher, in the public finances in some member states. In the banking sector there was some inefficiency in meeting market order but the main purpose of any bank is that of insuring the best response to the customer’s demand, therefore achieving customer satisfaction which leads to the increase of bank profit. [Preda Oana, Avram Emanuela, Furdui Iulia] The uncertainty created by the inability to pay the public debt also began to undermine itself the euro of causing fears that the problem could be extended to a number of member states in the euro area.

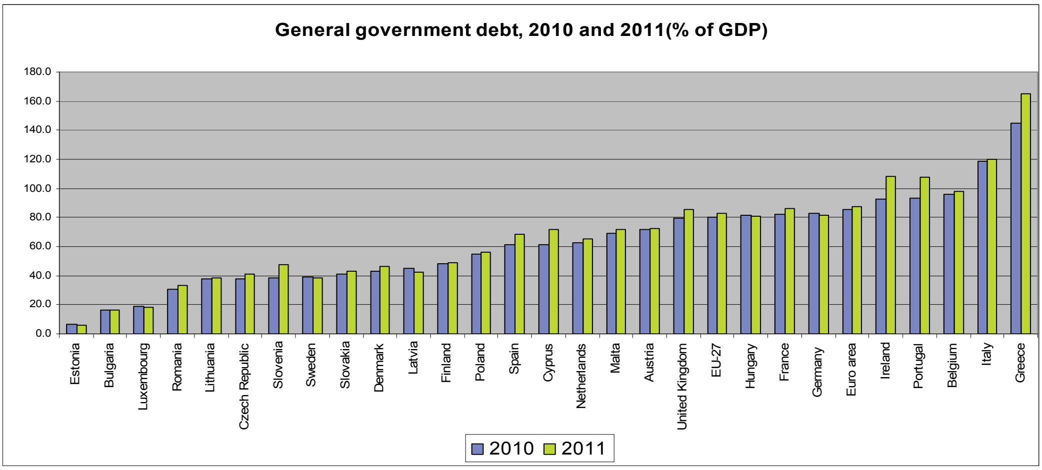
7. Public debt crisis is a crisis of confidence in the EU, in general, and in the euro area in particular. This requires a political solution, as well as financial. You could say with a certain be reasonably the Stability and Growth Pact has failed and now that Europe must create a new framework that fiscal and monetary able to stand up to more efficient economic results of serious negative or even of failure of a Member State.The main short-term challenge for the states that have an increased public debt is to restore the investor’s and consumer’s confidence [Preda Oana, Furdui Iulia, 2009]

Table no. 1 General government debt 2010 and 2011(% of GDP)

General government debt 2010 and 2011(% of GDP)	2010	2011
EU-27	80.0	82.5
Euro area	85.3	87.2
Greece	145.0	165.3
Italy	118.6	120.1
Ireland	92.5	106.9
Portugal	93.3	107.8
Belgium	96.0	98.0
France	82.3	85.8
United Kingdom	79.6	85.7
Germany	83.0	81.2
Hungary	81.4	80.6
Austria	71.9	72.2
Malta	69.4	72.0
Cyprus	61.5	71.6
Spain	61.2	68.5
Netherlands	62.9	65.2
Poland	54.8	56.3
Finland	48.4	48.6
Slovenia	38.8	47.6
Denmark	42.9	46.5
Slovakia	41.1	43.3
Latvia	44.7	42.6
Czech Republic	38.1	41.2
Lithuania	38.0	38.5
Sweden	39.4	38.4
Romania	30.5	33.3
Luxembourg	19.1	18.2
Bulgaria	16.3	16.3

Source Eurostat

Fig. no. 1 General Government debt to GDP 2010, 2011



Source: Eurostat, processing author

Most EU countries have a public debt above the maximum level of 60% required by one of the five quantitative criteria of Maastricht. The debt sustainability is not only the important but also the interest on the debt that you can redeem them, which can be achieved by replacing maturing liabilities with new payment obligations. This rate depends on the insurance market investor perceptions aimed against the risk of default.

1. Greece - Debt equals 165.3% of GDP [www.eurostat.com]

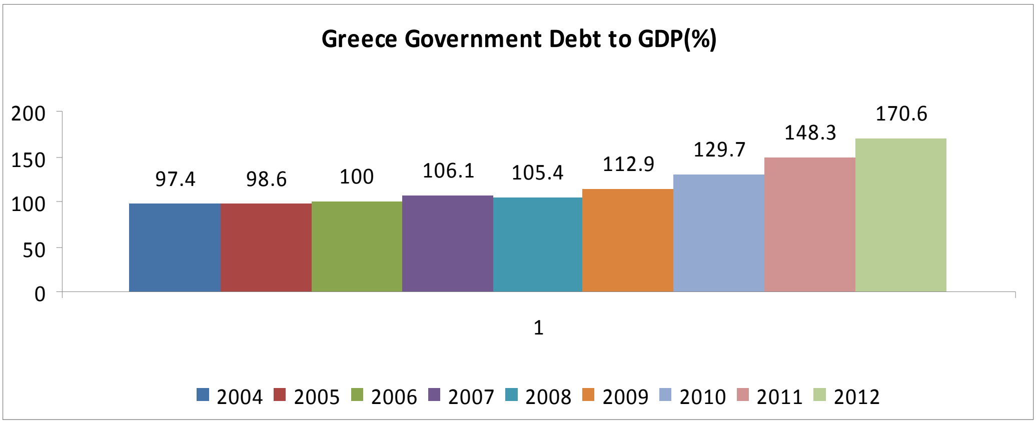
Anyone who has been paying attention to the euro-zone crisis is aware of Greece's dire financial situation. Greece's expensive social entitlement programs (including healthcare and pension systems), the 2008 financial crisis and an economy that has been shrinking for the past four years have resulted in plummeting tax revenues and sky-high government deficits.

Greece's budget deficit peaked in 2009, amounting to a massive 15% of the country's GDP. Since then, Greece's government has taken action, but despite passing politically toxic and unpopular austerity measures draconian cuts in the federal budget, for example government budget shortfalls amounted to a still elevated 9% of GDP in 2011.

To help them cover those kinds of budget shortfalls and give the country more time to shore up its debt, the International Monetary Found and the European Union granted Greece a second $169 billion bailout if the country promised more spending cuts and increased taxes. Greece can expect a painfully slow economic recovery - expect the federal debt here to get worse before it gets much better.

Greece was the first in the country with the highest degree of indebtedness in conditions which public debt has grown in the first quarter of 2011 by over 20%.Greece's total public debt is about 350 billion euros. Public debt has grown last year from 115% to 144% of GDP, reaching now at 170.6% of GDP.

Fig. no. 2 Greece Government debt to GDP



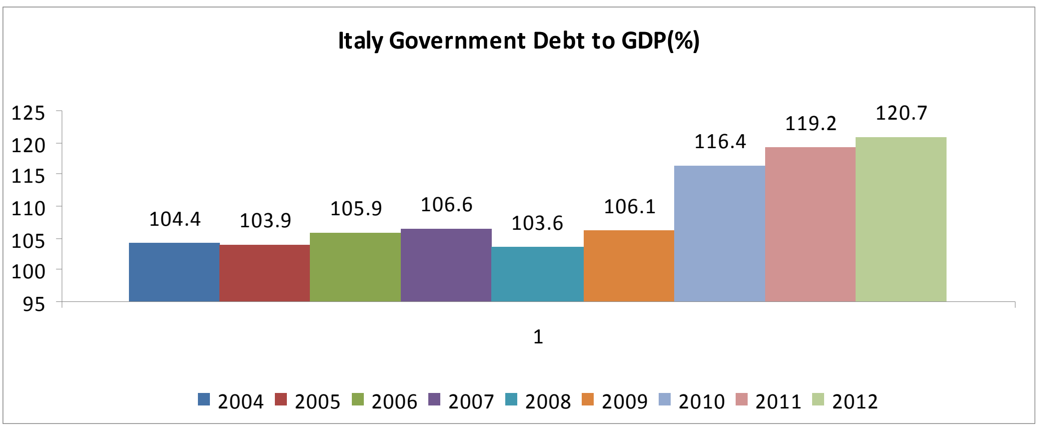
Source: Eurostat

2. Italy - Debt equals 120.1% of GDP [www.investinganswers.com]

Italy's sizable economy (the third largest in the European Union) may not have been threatened by a real estate bust like many others, but that hasn't stopped it from racking up serious public debt. Italy's inability to solve its debt and deficit problems stems from its shrinking economy. To this day, Italy's GDP is still 5% below its 2007 pre-crisis levels, and growth has been virtually stagnant for the past three years 0.4% in 2011, 1.3% in 2010 and 5.2% in 2009. Adding to its long-term challenges, Italy's low fertility rate and strict immigration policies will cause headwinds against future economic growth, meaning its public debt will likely stay around for a while.

Italy's public debt is affected by a low economic growth. In 2010, its GDP stepped up at a slower pace of 1.3%, after two years of recession. In 2011, Italy adopted a set of austerity measures in order to reduce the loan costs.

Fig. no. 3 Italy Government debt to GDP



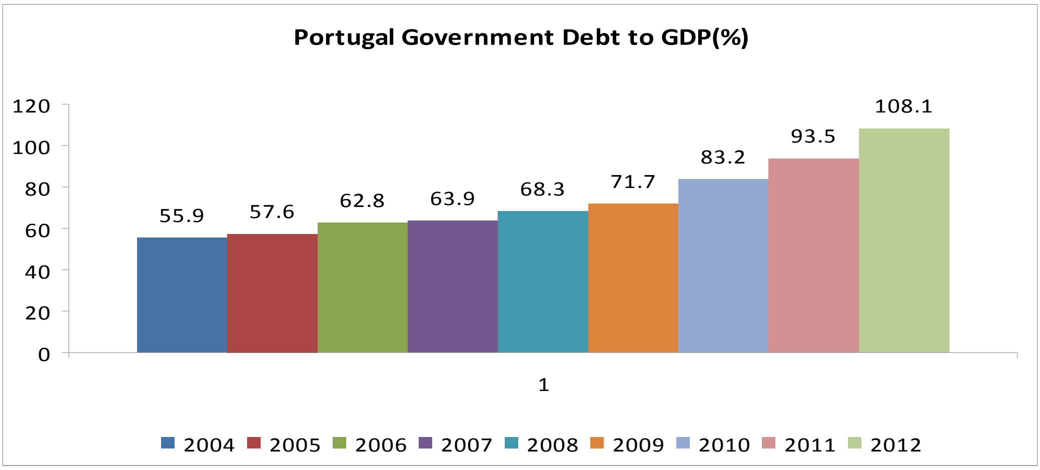
3. Portugal -Debt equals 107.8% of GDP

Weak or even negative economic growth in the past three years has kept Portugal from climbing out of its debt hole. Adding to the problem, Portugal's lack of a competitive labor force may keep the country's economy from growing much at all in the future. While the government is planning to boost exports and improve its citizen's skills to improve economic growth, you can expect Portugal's tax revenues to reduce and its public debt levels high, until those improvements actually come to fruition.

Portugal, with a public debt of 257 billion dollars, ranks second among European Union countries, with the highest degree of highest degree of debt.

In 2011, the country received one financial aid from the European Union and International Monetary Found .As a result of these receiving aid from the EU and IMF, the Portuguese Government has set reducing the budget deficit from 9.8% of GDP in 2010 to 4.5% of GDP in 2012, as in 2013 to reach the asked the EU 3%.

Fig.no. 4 Portugal Government debt to GDP



Source: Eurostat

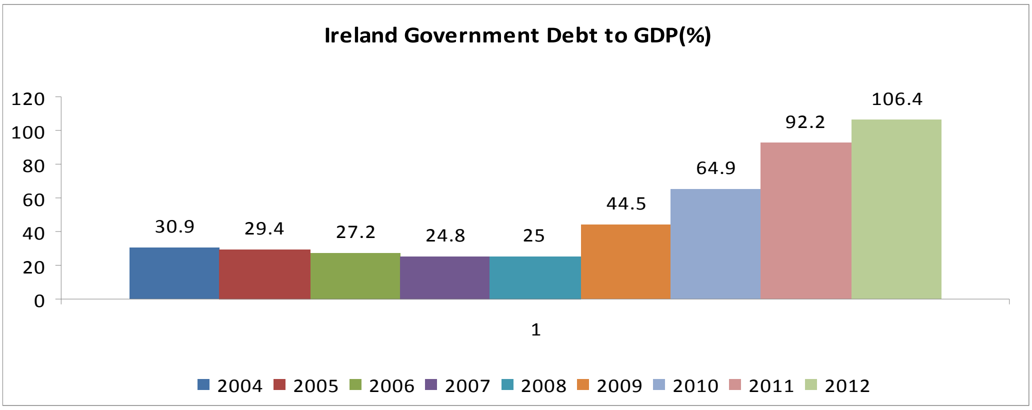
4. Ireland - Debt equals 106.95% of GDP

Ireland hasn't had much luck in curbing its debt problem in recent years. The 2008 financial crisis brought on a devastating housing market along with a series of large bank collapses. Despite making severe cuts in federal spending, the government's obligation to fund its flailing banking sector in 2010 gave Ireland the largest federal budget deficit in the world that year amounting to a whopping 32.4% of GDP. The bailout and the resulting budget deficit was so large, Ireland had to take out a $112 billion loan package from the European Union and International Monetary Found just to avoid defaulting altogether on its sovereign debt.

In 2011, Ireland faced a reduced-but-still-high budget deficit worth 10.1% of its GDP. As the country slowly heals, Ireland's debt continues to be watched closely by the European Union to prevent more complications in the euro-zone debt crisis.

Ireland, which was considered the healthiest economy in the European Union, in early 2000, recorded the lowest unemployment rate of all developed countries came to classes during present on the 4th position among the most indebted EU countries. Since 2001, Ireland's public debt has grown by more than 500%.

Fig.no. 5 Ireland Government debt to GDP



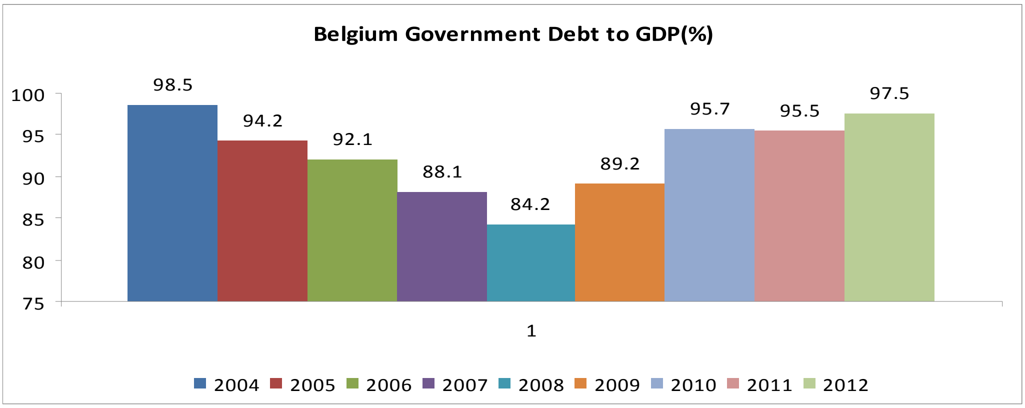
Source: Eurostat

5. Belgium -Debt equals 98% of GDP

The 2008 financial crisis wasn't cheap for Belgium. Like in the United States, Belgium's government was forced to provide its own expensive financial bailout, injecting capital into three of the country's major troubled banks [Hudspeth Christian,2012] Things have been looking up in the country over the past year, however. Unemployment fell from 8.3% to 7.7% in 2011. Also, GDP grew 2.0%, and the federal deficit decreased from 6% in 2009 to 4.2% of GDP in 2011.Nonetheless, with a debt-to-GDP ratio nearing 100%, many investors believe Belgium may be vulnerable in the short term to growing debt problems in the European Union. Belgium also faces two other major problems an increasingly aging population and rising social program costs that will cause headwinds when it comes to chipping away at its national debt.

Belgium's public debt in 1993 reached about 135% of GDP, but was subsequently reduced to 84% of GDP by 2007.In just four years, the ratio increased to almost 95% of Gross Domestic Product. In 2012, the country was forced to reduce costs by $ 1.3 billion to respond new fiscal rules imposed by the European Union, aimed at preventing a new debt crisis in the euro area.

Fig.no. 6 Belgium Government debt to GDP

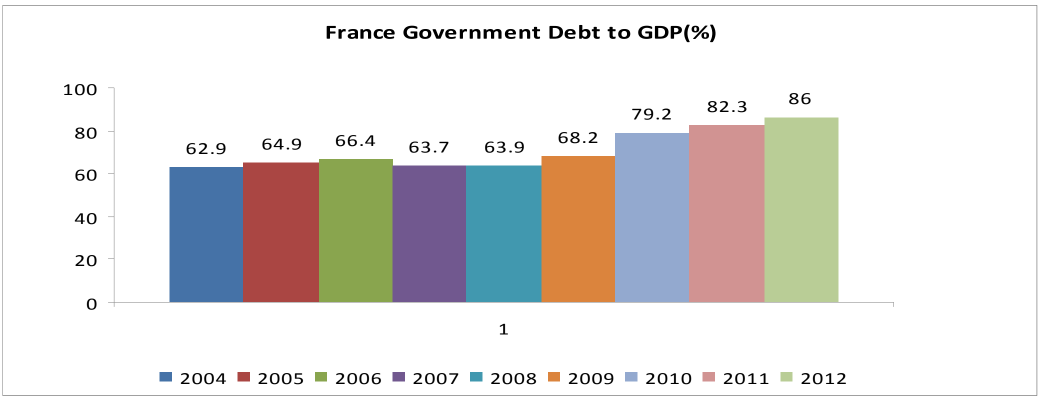


Source: Eurostat

6. France -Debt equals 85.8% of GDP

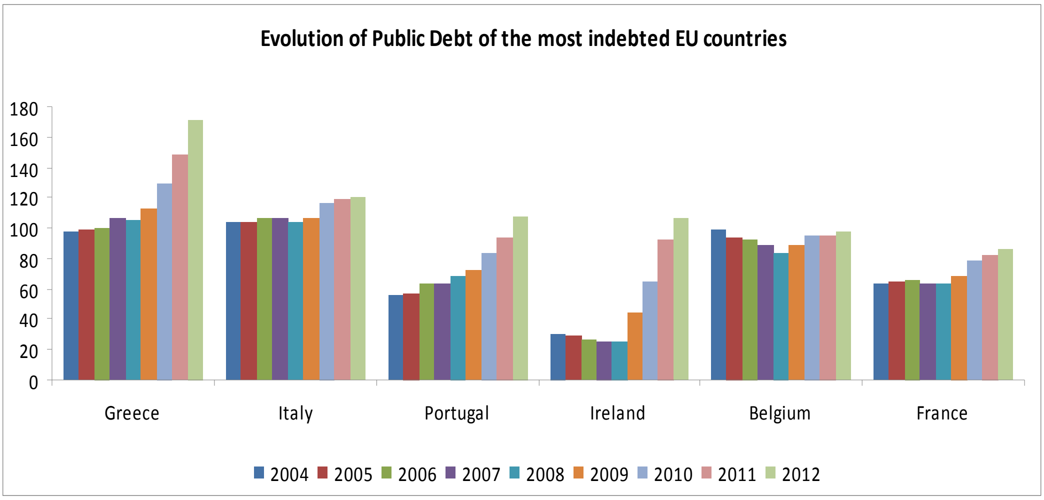
A damaging combination of high unemployment (9.1% in 2011), lower than expected economic growth, depressed tax revenues and continuously heavy social spending has led to sharp increases in France's public debt., these factors have caused France's gross-national-debt-to-GDP ratio to skyrocket from 68% in 2008 to 86% in 2011[www.cia.gov] As economic headwinds persist, don't expect France's debt problems to go away anytime soon.

Fig.no. 7 France Government debt to GDP



Source: Eurostat

Fig.no. 8 Evolution of Public Debt of the most indebted EU Countries



5.Conclusions

It becomes clear that debt crisis could have been avoided if there had been a better governess in the Member States and in the EU and it is absolutely necessary that governess weakness in the past may not be repeated. To this end, be taken a series of measures to strengthen budgetary supervision in accordance with the Stability and Growth Pact. These measures effects :

- mutual monitoring the projects of the budget of the Member States;
- early application of the penalties in relation to the compliance with thresholds debt/equity ratio of 3% of GDP, and 60% of public duty;
- triggered excessive deficit procedure applicable if debt reduction does not take place early enough;
- greater independence for national statistical offices to their national governments.

Senior Officials of the European Union have been of the opinion that the attitude rating agencies was not as expected. German Chancellor has proposed creation of a new European agencies independent rating which can compete with the three major existing agents. It has been suggested also that Eurostat to obtain competence to public ratings of public finances of the member states. If he had already have these skills, the Eurostat could warn earlier that there is a crisis of the debt in Greece.

The Commission has been criticized for lack of vigilance and proactive to ensure the quality of the data on public finance national. This aspect refers to the matter wider monitoring, and the compliance examination which is located at the base of failure mechanisms of the Stability and Growth Pact. Any solution in the longer term must address these aspects effectively.

While banks in Greece, Spain and Portugal have not benefited from the measures of saving financed with taxpayers' money, the extent of such measures in the other parts of the EU and the USA has contributed for the exercise of a unprecedented pressures on the markets of the bonds by the state and accelerated into a crisis. It is necessary to implement effective measures to reform of the banking sector worldwide, such as to prevent recurrence of such financial instability, economic and social.

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