The effectiveness of the EU economic governance framework

Stefan Marian DUMITRU*

Abstract

The purpose of this paper is to evaluate the effectiveness of the European Union's (EU) economic governance framework as a key component and driver of the EU - Economic and Monetary Union (EMU). Considerable measures to strengthen the EMU have been undertaken in recent years. In spite of this, its effectiveness in tackling challenges that might appear especially in times of crisis, is still called into question. The creation or reformation of institutions seems to be the most efficient manner in which the Eurozone can advance policies and mechanisms meant to stimulate economic growth. We have found that the major obstacles to more efficiency are two components: 1. the political dimension of the EU – or better said political interference of MS's to protect their own interests; 2. weak EU leadership and vision – this, together with political interests, dilutes significantly the building of institutions, creation and enforcement of policies. Ultimately the question of improving effectiveness of EU economic governance lies in the EU's ability to build a stronger foundation for its institutions. As a modern political and economic entity, subjugated to the MS's, the EU must maintain a balance between state powers and institutional powers, a legal and democratically accountable system of governance, the enforcement and respect of law, whilst also protecting economic growth and the right for a better future.

Keywords: EU, Economic Governance, Effectiveness, EMU

Introduction

After 8 years of economic crisis, the EU and EMU seem to have found some measure of a fragile stability. Policy changes undertaken between 2010 and 2012 have brought urgent revisions to the EMU. It has been transformed from a system of coordinated economic policies to a system of economic governance. The outdated architecture of economic policy coordination was based on the willing cooperation of Member States. This was done under the rational that the advantages of cooperation would outweigh the disadvantages. Economic governance changes the paradigm by institutionalizing the cooperation of economic policies. It is a much better and well welcomed improvement from the voluntary system utilised before. Even so, these efforts have not resulted in a more competitive market that can sustain growth, efforts must be multiplied to break from the lack of strong and sustainable growth.

* Stefan Marian DUMITRU is doctoral student at the Bucharest University of Economic Studies, Romania, e-mail: stefan.dumitru91@gmail.com.

At fault is that time and time again the political discourse of leaders has not been met with the necessary impetus and clear objectives. The economic crisis has shown that the EMU requires new institutions with clear powers to implement the necessary reforms destined for the market. Under an unclear path and with numerous gaps exposed, the effectiveness of the EMU has produced a debate on what the further steps should be. On one side, we have community method, which argues that more resources and sovereignty must be given to the community. On the other we have the intergovernmentalist method which argues that MS's must remain in control as the true benefactors of the policies. The community method, while preferred by institutions and academia, is a highly unlikely option in a time in which there is growing anti-EU sentiment which encourages MS's to favour direct control.

Notwithstanding obvious political barriers, the long-term effectiveness of EU economic governance remains to be seen. The complexity, and need for pooling sovereignty for policies is often the friction point the sprouts other divergences and slows the reaction time of the EU.

The first part of this paper will be an overview of EU economic governance and some recent developments that can be said to have improved its effectiveness. The second, third and fourth parts address the effectiveness of the key elements that make up the system. The paper will use a mix of EU documents, studies and an extensive range of academic literature. Based on what is observed, we will evaluate and criticize the positive and negative features of EU economic governance, and how these affect its effectiveness.

1. EU Economic Governance

EU Economic Governance has been built on a pre-existing framework of the EMU. The most valuable contribution that it has brought to the system is the European Semester. Continuous supervision and monitoring from the Commission coupled with institutionalized cooperation between Member States, has created a much greater coordination of policies and a stronger check and balance system. Indeed, this has created a much more restraining system, but it is a necessary quasi-evil due to the penchant of Member States to follow their own interests to the detriment of the EU. We must understand that most shortcomings of the framework are due to its fragility at the hands of MS's political interests, and not pure ineffectiveness on its part.

EU economic governance is a new framework, born out of the reforms undertaken in the 2010-2012 period to the EMU. Naturally it is prone to missteps and has had errors in design that might have been overlooked, but it has continuously improved since its inception. Institutional reforms have been most effective in tackling misgivings that have appeared.

Going back in time, to the signing of the Maastricht Treaty, economic governance was not even a concept. Instead, economic coordination was the mechanism envisioned to support the EMU. It could only be effective if MS's consented to endeavouring in it. The design lacked power dynamics, policy processes and proper enforcement. MS's sensed this deficiency, and proceeded to abuse the system which they had created. In time, new evolutions have redefined and streamlined the system, especially since the economic crisis: 1. by relying less on the Commission as leader of the framework; 2. more observance of imbalances between MS's by putting more pressure to respect the country specific recommendations and Maastricht criteria; stronger fiscal observance and punishment of deviations. Important changes relate to the power dynamic: 1. an increased role of the Council of Ministers, specifically ECO-FIN and Council Presidency as decision makers and 2. the European Parliament taking on the position of mediator. In an amusing twist of events, the better inclusion of multiple institutions in the process of economic governance has actually given it more legitimacy and credibility as a coordinated and European effort. In the following sections, we shall see how these developments came to be.

Under the sovereign debt crisis, the misgivings and errors of the framework have been brought to light. With this, substantial undertakings have been implemented to make the system more credible and encourage growth and stability. Of the numerous measures adopted (too many to discuss in such a short essay) the one with the most impact targets the Stability and Growth Pact (SGP) thought the Six Pack and Two Pack (European Commission, 1998). In the following three parts, we shall analyse the EMU, ESFS/EMA and ECB as integral components and influencers of the ultimate effectiveness of EU economic governance.

2. The European Monetary Union

2.1. The framework of the EMU

The European Monetary Union is an indispensable tool which has not only regional but global ramifications. Its miss comings inherently affect the effectiveness of the EU Economic Governance. Two major deficiencies have been observed: 1. Its incomplete nature of the EMU; 2. The financial markets incentive scheme which would assure MS's respected the Maastricht criteria.

First, the incomplete nature of the EMU can only be resolved by pushing forward with the Eurozone completion. It is ultimately a question of possibility (from an economic point of view) and willingness (from a political point of view) of MS's (Chinn, 2012). Second, the poorly constructed framework of the 90's was a major flaw of the system. The principle idea revolved around the financial markets incentive system. Under this, financial markets would punish countries that disregard the Maastricht criteria. In reality it actually contributed to the creation and deepening of the sovereign debt crisis.

The concept was a double tiered one. First, it was expected that MS's would adhere to these regulations as they would to their own policies, primarily due to the adverse reactions that breaking them would entail. Second, financial markets would act as a check and balance system by punishing states that did not adhere to the discipline imposed by treaty. In theory financiers, would expose bad credit practices and thus push the government in taking action to avoid proliferation of such behaviours, otherwise risk having higher costs in obtaining credit (Afxentiou, 2000). In all actuality, the process turned out to be in reverse, financial market did not send any signals of bad behaviour, and thus no cause for worry was observed. Governments did not feel any pressure from markets to employ self-discipline. Thus, these initial design aspects of the EMU were flawed and ineffective from the beginning. By basing itself on an incentive system and rational behaviour of markets, it did not discourage MS's from breaking the Maastricht criteria, which happened quite soon after the switch to Euro. It created gold rush for cheap cash.

The EMU was born out of the necessity for more efficiency of the Single Market (European Commission 1986). Having dozens of currencies would act as a bottleneck to EU trade. This was validated by the Delores Report – One Market, One Money of 90 (European Commission, 1990). It brought into focus the need for the establishment of a single currency for the European project as a measure of liberating intra EU trade from the costs of running multiple currencies. As Dyson and Featherstone (1999) detail, there was a strong belief that a single currency could be manageable with the implementation of convergence criteria. The wide spread agreement of academia was that the mobility of capital was becoming more and more crucial to businesses and financial markets, as technology made it easier to implement and more efficient to administer, it would make business cheaper (Dyson and Featherstone 1999).

Thus, it was only logical for the EMU to be established under certain strict criteria that would maintain stability of the new currency by keeping MS's financial behaviour in check. It was set it place through Articles 104 and 109 of the TFEU of the Maastricht criteria (European Commission, 2007). Under the Maastricht criteria, MS's both in and outside (to avoid negative influence from their actions) the Eurozone, must maintain a debt of maximum 60% of GDP, with a maximum 3% deficit per year. Strict limitations were imposed on becoming a euro member. A non-euro MS must hold a stable inflation and interstate rate for two years, before being invited to join. But as we have previously stated, MS's after joining the Eurozone, were quick to sway from the criteria.

In anticipation of this, the SGP entered into force in 1998 as an agreement between MS's, as a measure of prevention to protect and maintain stable public finances (European Commission, 1998).

Without a doubt this was a sound decision, a control mechanism would naturally be needed. Even though in concept a good measure, political interests went beyond the SGP as we shall see further on

Under Article 126 of the Treaty (European Commission, 2007), the SGP was provided with several tools to enforce its powers: 1.a preventive and corrective arm, 2. The Excessive Deficit Procedure (EDP). The EDP is a potent tool observance and guidance tool. It relates to the dissuasive dimension of the SGP, as it can culminate with sanctions for repeat offenders which run high deficits and do not remedy bad practices. As Machiavelli said, “it is better to be feared than to be loved” (Machiavelli, 1556). The EDP was meant to be feared, and rightfully so, as dissuasive measures are always necessary, if no punishments exist, then legislation is just writing on paper.

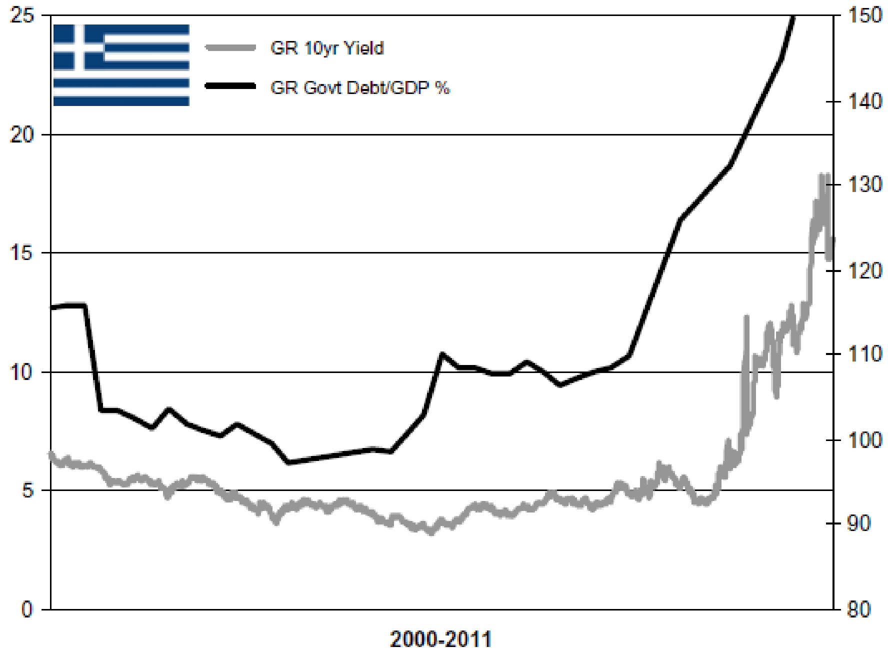
Thusly we have seen that the initial design aspects of the EMU were flawed and ineffective from the beginning. By basing itself on an incentive system and rational behaviour of markets. It led to MS’s in not respecting the Maastricht criteria immediately after few years of its implementation, running high debts and deficits, or even cooking the books as we have seen in the case of Greece (Allen Little, 2016), to enter the euro. Naturally, by ignoring the very rules MS’s helped to create, the system would become weaker and problematic.

2.2. The problems of the EMU

The problems of the EMU stem from a poor design and lack of vision on part of the creators. While this is mainly due to the incomplete nature of the policy, MS’s are equal contributors to the confounding of the spectrum as their short-term interests are valued for the fast results. This section of the paper will set under the microscope the EMU’s most visible problems and expose their implications.

Firstly, economic governance through the influence of market discipline is a very hopeful concept. Not only do markets seem uninterested in the Maastricht criteria, they mostly disregarded them. This is based on the fact that MS’s retained individual entities as creditors. With such individuality, as Schimmelfennig and Sedelmeier (2004) point out, MS’s preferred to retain high credit ratings and as such, without negative singles from the market, the lack of a bail-out clause would be no deterrent. All MS’s had ratings that would ensure good returns, and as risk was only seen at country level, not EU level, there was no cause for concern as long as ratings were unaffected. Naturally this created a false impression of the future for MS’s, actually encouraging them to spend more and take more loans. The rest would have been easy to observe. Of course, had the markets punished and not encouraged states to continue on taking credit. When the smoke vanished with the announcement by the Greek government in 2009 that its deficit would be 12% - double of what was anticipated. Such a spike, as we can see in Figure 1 naturally caused markets to panic. Ushering in the full destructive nature of the global economic crisis and inaugurating the sovereign debt crisis.

Figure 1. Greek debt and bond yield



Source: Bloomberg, 2012

Secondly, the euro area has an inbuilt ineffective fiscal governance. The SGP was prevented from exercising its power of prevention. Only when the Six and Two Pack were inaugurated, did the prevention mechanism of the EMU start to truly work.

MS's are susceptible to willingly disregard the Maastricht criteria if not properly enforced (Channel 4, 2015). Not only this, but shot term economic gains impulse them to block the prevention of their actions through the SGP. The Commission faced procedural hurdles that States actively tried to set. The most common of which being that of diluting decisions of the Commission through their Commissioners. A second barrier can be observed in with the case of Ireland vs. The Commission (2001). In this, ECOFIN used its powers to block Commission actions through the procedural steps (Hodson, 2011). In 2001, the Council blocked a Recommendation for Ireland, pushed by the Commission, due to the fact that Ireland was experiencing growing economic imbalances (Hodson, 2011). As there were no signs of diminishment of said imbalance, three years later, the SGP threatened with sanctions. The response was shocking, ECOFIN amended the powers of the SGP so that it would include a differentiation of medium term economic targets, and not only short or long term (European Commission, 2005). Thus, its mandate against Ireland was nullified. This reform presented as giving flexibility to the SGP was, in the words of Schuknecht (2011) a means by which MS's gained more control, thus making it even more haphazardly to monitor unruly states (Hagen and Schuknecht, 2011).

Thirdly, the EMU has difficulty in confronting numerous adverse situations at the same time (financial instability, higher debt, austerity). Compounded to this, there exists a clause that prohibits the European Central Bank from bailing out any country actually risking default due to deficit, thus adding to the destabilization of the system. The scene is 2010/2011, financial markets continue to panic more and more. Without an institution that would save the countries from defaulting, panic and uncertainty was flourishing (de Grauwe, 2012). This spiral in which the ECB was finding itself created more and more pressure (from academia, politicians, financiers, etc.) to provide liquidity to stabilize the markets. But it did not succumb to these pressures. The system found new flexibility not by renouncing the core tenants of monetary financial prohibition, but by reinventing and redesigning the existing systems, as we will see in the final section of this part. We observe further below, how it has become general knowledge and an expected feature of the EU to evolve under pressure.

2.3. The European Monetary Union adapting to the economic crisis

The decision to diligently respect the core tenants around which the ECB and EMU were built upon was central in shaping the evolution of the EMU in recent years. As Salinas, (2007) observes, the strategy chosen was to focus on the aspects that hindered institutions from becoming efficient. Essentially tackling poor frameworks and loopholes that permitted the hindrance of institutions. Leading to several positive outcomes.

First, the market is more transparent. Specifically, the ability of speculators to disregard risks and manipulate them to their advantage has been diminished by making economic conditions of MS's more transparent. National statistic authorities must report under the Six Pack legislation specific information on the finances and economy (European Council, 2011a). Added to this, the SGP can now use the Macroeconomic Imbalances Procedure (MIP) to showcase vulnerable aspects of the private sector. This information is analysed directly by the Commission and recommendations were given (European Parliament, 2011). The Two – Pack goes even further by gaining the ability for the Commission to warrant special surveillance of states which are under threat of financial duress (European Commission, 2011). Stress tests in the banking sector by the EBA (European Banking Authority) expose the vulnerabilities and threats of the banking sector and report directly to the ECB. Unsurprisingly numerous banks have either failed or had poor performance in the beginning, with some improvements seen recently (European Banking Authority, 2016).

Second, the SGP is more potent in prevention, correction and enforcement. Its reaction time is much faster. This is because the Council now takes decisions on applying financial sanctions by revers qualified majority voting. MS's representatives have less control, and thus are must push for better application of recommendations.

Third, the adoption of the policy "keep all houses in order" shifts the attention to more vulnerable countries. All crises have a spill over effect, thus no country is immune to the decisions and actions of other countries. An intra-euro financial assistance framework has been built to motivate and make national governments more responsible to not only monitor their own economic practices but also that of neighbours and another MS's. This has led to a stronger focus in Eurogroup discussion on more vulnerable countries (European Central Bank, 2014).

Last but not least, countries can now use a mechanism by which they give liquidity to financially struggling counterparts. As we shall see later, the EFSF/ESM has been established as an intergovernmental institution which can provide capital in need. It can do so under several mechanisms: loans, programs, market purchases, secondary market purchases, bank recapitalizations. The no bail out clause was not scrapped but a system acting similarly was set in place by MS's, led by themselves. The ECB continues to cover the private sector by buying poor quality bonds. These measures have subsequently reinforced the position of the EMU and strengthened the notion for markets that they would not be allowed to fail. Arguably in the long run this could prove to be a decision that can come and bit back the EU. With such an assurance, there is always the potential risk that companies and markets would abuse the system, knowing that they could not fail.

3. The EFSF/ESM

The ESFS diminished the manoeuvrability of MS's in taking individual actions against the crisis. From a coordination point of view, it imposes a much better system that impulses MS's in acting together.

The European Financial Stability Facility (EFSF) was created due to the economic shocks which accompanied the Greek debt crisis in 2010 (European Council, 2010). Its goal was that of convincing markets that the crisis had been contained through the commitment of EU leaders. As a result of poor planning, it became evident after coming into operation that the initial capital of 750 billion (of which only 440 billion was raised) euro guaranteed by MS's is insufficient. In the following parts, we will see how and why the ESFS evolved into the European Stability Mechanism (ESM) in 2012, arguably a form it should have been given from the beginning.

The hasty creation of the ESFS is one of the major reason for the diluted condition of the institution, and lead to its ultimate need for reformation. This naturally brings up the question of the reliability of the whole institution, one born out of panic from the Greek Crisis. To understand how the EFSF evolved into the ESM and subsequently how this is a reflection of the efficiency of EU Economic Governance, this section of the essay will analyse: the compromises between MS's that rushed the creation of the ESFS; the initial form of the EFSF and lastly the transformation of the institution into the ESM.

3.1. Rushed creation of the European Financial Stability Facility

Fear of contagion and spread of the sovereign debt crisis led to the hasty creation of the ESFS. The European Monetary Union was never intended to manage a sovereign debt crisis for EU MS's, never mind one in several countries. The outbreak of the crisis in Greece in 2008 with the fiscal revisions not only worsened the environment but spread it to other Southern states. As Gianviti (2010) observed at the time, if it spread, the absence of rules to manage such a situation would become ever more pressing, leading states to scramble a solution to curb market fear. And they did in the form of the EFSF.

The European banking sector is highly interlinked. As such, a Greek default would have had the potential to bring down the whole Eurozone. French and German banks had borrowed close to one trillion euro to the Southern Countries and Ireland (Clarke, 2016). A massive exposure on their part in a rush for riches. Naturally there was a high interest in managing the situation so that the contagion would not dissipate to the French and German banks. With the primary banking markets of the EU compromised, the contagion would disperse easily to the rest of the EU and beyond. Thus, it was not only in the interest of French, German and other states implicated, but of all MS's, to remedy the situation. We can thus observe that European Economic Governance does not only spring from the desire to protect and regulate the euro and single market, but also the interdependence of MS's economies.

3.2. How the Greek Bail-out was managed

Time was the main catalyst that lead to poor decisions, or lack of it. While initially reluctant to intervene, the possibility of contagion backed Eurozone leader into a corner to solve the problem. The reason, lack of a better option: either intervene and save the house or fail and let it burn. As the

ECB had no mandate to intervene and would not break the rules, a different kind of solution was found. In March 2010, the European Council declared that Germany (27.92%) and France (20.97%) would bypass the limitations of the ECB and finance loans directly to the Greeks, together with the IMF. Only a direct intervention from MS's in a move of 'solidarity" managed to appease the markets (European Council, 2011b). As we shall see further below, it would evolve into a Troika as the money and conditions were managed by the ECB, Commission and IMF, creating significant tensions and political exchanges.

The fact that the markets pushed the Eurozone leaders and IMF into a corner is a sign of weakness and poor credibility of EU Economic Governance. Initially a 45-billion-euro package was offered by the Eurogroup to Greece as bilateral loans (European Commission, 2010). The reaction was that of cornering the Eurogroup even more as a wave of scepticism towards Greece's ability to avoid default hit even with the promised help. One month later in May 2010 with the ECB and Finance Ministers agreed that Greece would be offered a 3 year 110-billion-euro support package to prevent Greek default (European Commission, 2010). But yet again, the market reaction was not one of faith in the measure (E. Moore, 2010). Thus, it was recognized that a new mechanism or institution was needed to preside and tackle the spread of the contagion of the Greek crisis to other euro countries, for a short term. This led to a debate on the best possible solution, of which the options were not few:

1. **European Monetary Fund (EMF)**. Was one of the first ideas proposed, initially by academia, but later on by others. It would be a European stability mechanism which would fund countries in need of aid, similar to the IMF, with a budget of 5-700 billion euro. Micossi (2008) interprets its failure due to the significant similarities it shared with eh IMF, and the potential for it to evolve into a rival.
2. **A Commission led organization.** Proposed by the Commission, it would be a fund that would use bonds backed by guarantees provided by MS's. Such a proposition had little chance of giving the Commission access to their own funds without the backlash of citizens.
3. **A European Debt Agency**. Proposed by the Prime Minister of Belgium at that time - Yves Leterme (2010). The European Debt Agency would have managed euro debt from a central point. Such a proposal would have created a common interest rate for all MS's based on the pooled rating of all Eurozone states. This proposition had even less chance to pass as high rating states would have never agreed to see their ratings and thus costs be affected. Not only this, but as Laterme states, it would have also required a change in the treaties as it affected the fundamental functioning of EMU.

4. **An intergovernmental Special Purpose Vehicle (SPV).** Which would come to be known under the name of EFSF won the debate. After months, the SPV or EFSF was chosen as it would allow the raising of money through issuing of bonds supported by MS's. Renaud - Basso (2011) identify the principal motive for accepting the SPV as the ability of MS's to have direct control of the institution, and avoid another EU controlled or independent institution.

Markets did not consider enough the measures decided upon by Eurozone leaders with regards to Greece and containing the crisis. Thus, the EFSF emerged under pressure and panic of a potential default, not only of Greece but also of Spain, Portugal and possibly leading to a domino effect in the rest of the states.

3.3. Creation of the EFSF

The decision to utilise an intergovernmental SPV as the tool to tackle the crisis was not a surprise, not because of the intergovernmental aspect but because of the way it was managed. In the original statement, it promised 750 billion euro (guaranteed by the euro countries and IMF) as bail-out. Tsoukalis (2010) states that it would only be natural that the leading contributor to the institutions, Germany would have the highest influence on the rules of the EFSF. This proved to be a significant flaw. German sentiments were very negative towards the idea of using German money to bail-out Greeks, thus pushing for stronger more difficult reforms. A flaw that would create significant political tensions between the countries, a referendum on the Greek side and almost a default of the Greek economy.

France also plaid a role in the process as the second biggest economy of the euro. But it is often overlooked because its interests aligned with the Germany's. Why? It shared a similar exposure as Germany towards southern banks. But initially, as Ludlow (2010) declares, the more favourable option for the French was for the ECB and Commission to take action directly. This measure would have likely been blocked by UK. The reason behind this being that it did not desire to provide further funds to EU mechanisms as the Eurozone problem was seen as one of euro countries (even if UK banks were also very much exposed). As Renaud - Basso (2011) argues, a community mechanism would have been much more difficult to pass, and control by MS's, the clear reason why the intergovernmental method was preferred. In an increasingly anti-EU Europe, more powers to the EU can spell a recipe for disaster.

3.4. Implementing the EFSF

The short comings of the ESFS can be attributed to mostly political interests interfering with the framework of the institution. The EFSF is by no means a simple institution which has the mandate to protect EU financial stability. The concept of using capital markets to raise liquidity and fund loans sounds simple but it is deceptive.

As we have stated before, the EFSF biggest contributor was Germany, and subsequently German efforts to influence the institution prevailed. Set up in Luxembourg, the ESFS is a combination between an institution and a corporation and thus not under the control of either the Council or Commission. MS's are in all actuality shareholders that preside the company and are observed by the ECB and Commission (Gianviti, 2010). This showcases the ingenuity demonstrated by EU economic governance through MS's. It has created an entity that could be outside of any control of direct EU institutions, but be able to exert direct influence through its actions on them.

The EFSF was initially accepted with positive reviews, but these would not stick. Even with this mechanism set in place, markets reacted again with worries that Greek default could still happen. This time it was a reverse of the previous situation. Bowley observed that the massive amounts promised were interpreted would be difficult or impossible to reach. A correct assessment (Bowley, 2012). Thus, the potential of the EFSF was negated by the markets. Added to this, its interest rates were not only the same as the ones of offered by markets, but also added charges to discourage other countries (a direct link to the ECB no bail out policy) from arriving in the same debacle. The German legal and political system is the main culprit in this case, as the German constitution would be unlikely to accept more ambitious plans. In a sad twist of fate, it resulted in the political conflict between Germany and Greece, which felt exasperated and cornered (Pisani, 2011).

The 2011 bail out of Ireland was successful, but it resulted in higher costs for borrowing for the southern Latin states. The reason? Markets did not trust in what was built. More panic ensued at the thought of having to bail out Portugal, Italy and Spain. The motivation as Atkins observes is simple: the EFSF did not have the funds all four southern states defaulting (Atkins, 2010). In the view of Atkins, Germany is once again the culprit as it wanted to retain AAA rating for the EFSF. Compounded to this, it was discovered that in fact, only half of the over 750-billion-euro lending capacity promised was actually available. Naturally another scramble to find a solution began ultimately leading to the transformation of the EFSF into the permanent ESM.

The fault for the failings of the EFSF came from the mix between economic necessities and political agendas pushed by MS's. Thus, we observe one of the major inefficiencies of EU Economic

Governance, the continuous mix of national interests to the detriment of supranational and economic needs, one which we will see time and time again.

3.5. From the EFSF to the ESM

What lead to the metamorphosis of the EFSF? An amalgam of factors: continued threat of Greek default, fear of contagion, a rush to create the institution and political interests in economic matters; All of these and others let to the necessity of transforming the EFSF from a temporary institution to a permanent one. This last section will examine the ESM in a similar fashion to the EFSF.

From the very beginning the inadequacies of the EFSF were recognised by the political spectrum, markets and academia. Debates on how to change and adapt it began and they were cantered mostly on the temporal permanence of the institution and decrease of interest rates. The problem lied in German reluctance to expand the EFSF. But they were in favour of Treaty change for a more permanent institution. In unconventional fashion as Peel (2010) presents, the ECB took a more direct approach in expressing its support of EFSF by acquisitioning bonds, supporting lower interest rates and a bigger fund. Naturally, the countries that would benefit from the EFSF very outspoken towards the pushes of evolving the institution. Not only this, but this period was marked by an increased activity of the Commission which was also in support of such actions (Peel, 2010).

Ultimately, with the reluctance of France and Germany, the pressure from MS's, institutions and other parts of society prevailed. A formal increase in powers of the EFSF, transformed it into the ESM by 2013. It increasing the lending capacity and lowered interests rates it offered as well as making the institution permanent (European Council, 2011c). In atypical fashion the ESM was not hijacked by political interests and within a few months, new powers such as capitalizing banks, intervention in secondary markets and others were given (European Council, 2011d). In time, the ESM became more organized and structured.

The ultimate form of the intergovernmental institution known as ESM is that of a mechanism set up to avoid breaking the rules for the EMU set through the TFEU. It is a compromise solution, one to salvage both the credibility of institutions but also the Eurozone itself. Is it a model of the efficiency of EU economic governance? Yes and no. No because it exposes the fundamental flaws of the EMU system, which were inherently built in and ignored for decades, leading to an unprepared and weak system that could threaten the whole European project. But it is also a model of efficiency, not in the traditional sense of the word of a mechanism running as intended, but of an entity which experiences events, makes multiple faults and finally learns and adapts. The EU does thrive in adverse conditions, and the evolution of the EMU and ESM is a testament to this and how efficient it is in doing so.

4. The European Central Bank

The European Central Bank (ECB) is one of the most efficient institutions of the EU and EMU. It is one that sticks religiously to its powers but also maximises them for full utility. The best example of this being its refusal to finance MS's deficits. This would ensure that any thoughts by MS's that the ECB would finance their deficits would not occur.

As stated in Article 2 of the ECB Statute, the mandate of the ECB is that of "maintaining price stability within the Eurozone, implement monetary policy of the Eurozone, conduct foreign exchanges, care for the foreign reserves of the European System of Central Banks and operate the financial market infrastructure. Most importantly it is the sole issuer of euro banknotes (MS's can issue coins at certain ECB authorised amounts)" (European Central Bank, 1997).

Subsequently, within the system of the EMU, the ECB isn't only an agency responsible with monetary policy, but also the principal actor that defends its interests and construction. A role that has proven crucial in the crisis. As the EMU is still incomplete (the target for its completion being 2025), the sovereign debt crisis has brought it, quite realistically to the brink of collapse. The ECB thus sees itself as the natural protector of the EMU, and principal driver. In the context of the economic crisis it has the highest authority in stepping in to avoid significant incidents. Leading to the ECB to take an active role in building up institutions that cover the gaps left by the incomplete EMU (such as the ESM). It will take all necessary precautions to protect the EMU. In 2012 the ECB fearing MS's not respecting agreements, threatened to impose harsh conditions on them. Under the threat of sanctions, governments were coerced in becoming ready to activate the ESM when needed (European Central Bank, 2016).

In the view of the ECB, MS's should be the principle economic contributors to the achievement of the EMU and Union objectives, stemming from its mandate given through the TFEU (European Commission, 2007). With the advent of the economic crisis the ECB took a much greater role in protecting the EMU and as such sees it as a special and strategic mandate (Mario Draghi – ECB, 2012).

With this in mind, it seems the ECB is strategically pushing for reforms in Eurozone countries (most visibly in Spain and Italy as well as Troika countries) through conditionality. This more than once has put it in close partnership with Germany, much to the dislike of states such as Greece. This leads to the observation that the ECB acts very strategically with respect to other institutions but mostly the MS's.

Under the authority of achieving its mandate of price stability with the Eurozone, in January 2015, the ECB mandated an asset purchase programme, also known as Quantitative Easing program. This would be done by purchasing risky private sector sovereign bonds as well as bonds from euro central governments, agencies and institution on the secondary market to ensure the avoidance of a deflationary path and stability of EU prices. It is a program that has been well welcomed by the markets and has maintained an upper inflationary trend for the EU, even if at a low level (0.6% expected for 2016) (Trading Economics, 2016). In 2016 the ECB mandated a continuation of the program. The study of the full effects and implications of the Quantitative Easing program could not be fully undertaken in this paper due to limitations of space, but it is an area which I will reserve for future research. What is clear is that the ECB is an efficient institution that has managed to bypass political interests better than most. It has a clear objective of its goals and how to achieve them, and utilizes its powers to their fullest extent. Quite frankly it would not be incorrect to say that the ECB is a model to be followed for good economic governance.

Conclusions

This paper has proceeded to demonstrate, by analysing at multiple levels and branches the EU framework of economic governance that it can and sometimes is indeed effective. The major obstacles to more efficiency are two components: 1. the political dimension of the EU – or better said political interference of MS's to protect their own interests; 2. weak EU leadership and vision – this, together with political interests, dilutes significantly the building of institutions, creation and enforcement of policies. Ultimately the question of improving effectiveness of EU economic governance lies in the EU's ability to build a stronger foundation for its institutions. Stronger leaders, which are better prepared are needed, but as MS's are the ultimate decedents in this aspect, only a change in their attitude will change this. If not, it is highly likely that we will see a perpetuation of the trends we have seen time and time again in the EU. Crises seem to be indeed, in a weird fashion, the means by which the EU can evolve efficiently. Not out of desire, but out of need.

The economic and sovereign debt crisis has been an impulse not only for the European Union, but also for its economic governance, institutions and leaders to adapt and change. The result is a more intergovernmental approach with regards to managing debt problems between states. The Stability and Growth Pact has been upgraded and can now penalize MS's much easier for deviations from the agreed economic reforms or imbalances then it could before. Such reforms have been pushed in exchange for the debt relief offered to states such as Greece, Italy and Spain, and naturally they have been met with significant backlash. The result is a continued push for more Europe, but meanwhile inside, anti-European and far-right parties are becoming more and more popular due to the continued austerity. With and incomplete banking union and fiscal union, there remain sufficient points of tension for conflict and instability between states in the future.

The ECB remains a staunch support of the incomplete EMU, it is a driving force that has strengthened the frame of economic governance of the Eurozone. By aiding in the creation of debt relief institutions, by pushing reforms through conditionality, it has led to more resilient and respected institutions. With the EMU imposing regulations and conditionality, and by institutionalizing cooperation under the European Semester, the EU's national government have now an extra impetus to keep their policies in check but also work with other states so that there are lesser overlapping effects.

The ECB is an actor that plays in a very strategic manner due to the circumstances in which it is. It derives its independence from the EMU, which is incomplete. Thus, it tries to legitimate its role and actions not only by guarding the EMU from the effects of the crisis, but also by maintaining a stable environment within the Eurozone. Under the mantra of "doing whatever it takes to preserve the euro, the ECB has gone to all the necessary steps to ensure its objectives and sustainability of the EMU: economic debates, conditionality of MS's, institution building, etc. It is an efficient ad integral part of the EU Economic Governance, ensuring that steadily yet surely the EMU remains viable and working for its completion. It is not without its imperfections, but it is an institution that functions efficiently and sticks to the mandate it has been given.

The EFSF is a classic example of EU institution building, a process in which economics become tangled up with political interests and create an amalgam institution. Then for it to be reanalysed and reformed into a more and more efficient tool through subsequent amendments. Such a process is a strong testament to one of the most inefficient elements of EU economic governance, and to EU governance in essence. It is time consuming and wasteful as MS's fight for power. This usually leads to a deepening of adverse conditions until the mechanism becomes more efficient. We cannot fully disregard national interests, they are part of the reason for which the EMU was built, as a better mechanism of economic exchange, and the resilience and flexibility of the system in such tough condition is a testament to its flexibility.

In this paper, we have observed a clear progress in the efficiency and legitimacy of European economic governance, led by the effects of the economic crisis. It is true that adverse economic conditions, debt crisis, political tensions have all been influenced by the incomplete system. But they are a testament to the inadequacies of EU governance, and we do not expect them to disappear overnight, or ever completely. The EU is a melting pot of 28 different yet similar states, of which 19 share a single currency. EU economic governance cannot be regarded as inefficient under the existing adverse conditions, but praised for its continued resilience and flexibility to adapt even on the brink of potential collapse. As a modern political and economic entity, subjugated to the MS's, the EU must maintain a balance between state powers and institutional powers, a legal and democratically accountable system of governance, the enforcement and respect of law, whilst also protecting economic growth and the right for a better future. The profound interconnectivity between the EU and Member States is the strongest element of EU economic governance, it ensures that in time the system must, and can become more and more efficient.

References

Afxentiou, P. C. (2000), Convergence, the Maastricht criteria and their benefits, *Brown Journal of World Affairs*, 7(1), pp. 245-254.

Atkins, R. (2010) Five potential weapons for the Eurozone, *The Financial Times* retrieved from http://www.ft.com/intl/cms/s/0/d6e13bae-fd83-11df-a049-00144feab49a.html.

Bloomberg, (2012), *Greece Government Debt*, retrieved from: https://www.bloomberg.com /quote/GGGB10YR:IND

Bowley, G. (2012), Fearing Return to a Recession, *The Economist*, retrieved from: www.economist.com/blogs/freeexchange/2012/02/european-stability-mechanism.

Channel 4, (2015), *State have broken borrowing rules*, retrieved from: https://www.channel4.com/news/france-and-germany-have-broken-borrowing-rules MS's cooperation in rule breaking.

Chinn, M.D. (2012), The Eurozone in crisis, *Harvard Journal*, Massachusetts, retrieved from: http://dash.harvard.edu/handle/1/10212562

Clarke, T. (2015), How Much Money does Greece owe?, *Money Morning*, retrieved from: http://moneymorning.com/2015/03/25/how-much-does-greece-owe-4-charts-that-put-greek-debt-in-perspective/.

de Grauwe, P. (2011), The Governance of a Fragile Eurozone, *Center for European Policy Studies*, retrieved from: http://aei.pitt.edu/31741/1/WD_346_De_Grauwe_on_ Eurozone_Governance-1.pdf

Draghi, M. (2012), President of the European Central Bank at Hungarian National Bank Conference.

Dyson, K. and Featherstone, K. (1999), The road to Maastricht, *The Oxford Scholarship*, retrieved from: http://www.oxfordscholarship.com/view/10.1093/019829638X. 001.0001/acprof-9780198296386

European Banking Authority (2016), *Stress Test Results*, https://www.eba.europa.eu/-/eba-publishes-2016-eu-wide-stress-test-results

European Central Bank (1997), *Statute of the ECB*, retrieved from: https://www.ecb.europa.eu/ecb/legal/1341/1343/html/index.en.html

European Central Bank (2014), *Report on Banking structures*, retrieved from: https://www.ecb.europa.eu/pub/pdf/other/bankingstructuresreport201410.en.pdf

European Central Bank (2016), *Guidelines on Monetary & Fiscal Policy*, retrieved from: https://www.ecb.europa.eu/ecb/legal/pdf/celex_32016o00045_en_txt.pdf

European Commission (1986), *The Single European Act*, retrieved from: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=URISERV%3Axy0027

European Commission (1990), One market one money, Bruxelles, retrieved from: http://ec.europa.eu/economy_finance/publications/pages/publication7454_en.pdf

European Commission (1998), *Stability and Growth Pact*, Bruxelles, retrieved from: http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1412156825485&uri=URISERV:l25021

European Commission (2007), *Treaty on the Functioning of the European Union*, Lisbon, retrieved from: eur-lex.europa.eu/legal-content/EN/TXT/?...celex%3A12012E%2FTXT

European Commission (2010), *Economic Adjustment Programme for Greece*, retrieved from: http://ec.europa.eu/economy_finance/publications/occasional_paper/2010/pdf/ocp61_en.pdf

European Commission (2016), *Specifications on the implementation of the Stability and Growth Pact*, retrieved from: http://ec.europa.eu/economy_finance/economic_ governance/sgp/pdf/coc/code _of_conduct_en.pdf

European Council (2010), Regulation No 407/2010 of 11 of the European Council of 11 May 2010, on establishing a European Financial Stabilisation Mechanism.

European Council (2011a), *Conclusions of the European Council*, Brussels, retrieved from: https://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/119175.pdf

European Council (2011b), *Statement by the euro area heads of state or government*, retrieved from: http://consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/126658.pdf

European Council (2011c), *The Stability of the eurozone*, retrieved from: https://www.consilium.europa.eu/media/21347/qcao11001enc.pdf

European Council, (2011d), *Council Directive 2011/85/, on requirements for budgetary framework of the MS's*.

European Parliament (2011), Regulation EU 1176/2011 of the European Parliament and of the European Council of November 23 2011 on the prevention and correction of macroeconomic imbalances.

Gianviti, F. (2010), *European mechanism for sovereign debt crisis resolution*.

Hagen, J. (2011), The impact of the financial crisis, *European Journal of Political Affairs*, Vol. 27, Issue 1, pp. 36-43.

Hodson, D. (2011), *Governing the Euro Area in Good Times and Bad*, OUP: Oxford.

Le Monde, (2010) *Pour une agence européenne de la dette, par Yves Leterme*, retrieved from: http://www.lemonde.fr/idees/article/2010/03/05/pour-une-agence-europeenne-de-la-dette-par-yves-leterme_1314894_3232.html

Little, A. (2013), *Magic made Greek debt disappear*, BBC, retrieved from: http://www.bbc.com/news/world-europe-16834815

Ludlow, P. (2010), In *the last resort, the euro crisis and the European Council*, *EuroComment*, retrieved from: http://www.eurocomment.be/?p=182#more-182

Machiavelli, N. (1532), *The Prince*, Boston: Dante University Press.

Moore, E. (2010), Markets set to react sharply to escalation in Greek debt crisis, *Financial Times*, retrieved from: https://www.ft.com/content/45ae1932-1da3-11e5-aa5a-398b2169cf79

Pisani, B. (2011) *Why EFSF auction was so weak*, CNBC.com, retrieved from: https://www.cnbc.com/id/45195376

Renaud-Basso, O. (2011), Interview by Ledina Gocaj, European Council, Bruxelles, January 25.

Salina, M. (2007), Spatial heterogeneity and interregional spillovers in the European Union: Do cohesion policies encourage convergence across regions, *European Economic Review*, Vol 52, Issue 3.

Schimmelfennig, F. and Sedelmeier, U. (2004), Governance by conditionality: EU rule transfer to the candidate countries of Central and Eastern Europe, *Journal of European Public Policy*, Vol. 11, Issue 4, pp. 661-679.

Trading Economics (2016), Euro Area Inflation Rate, *Trading Economics*, retrieved from: http://www.tradingeconomics.com/euro-area/inflation-cpi