Financial Integration and Banking Regulation in Europe in Contemporary Capitalism

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ABSTRACT

This paper discusses the completeness of the European Union framework according to a bibliographic review of Keynesian theory and financial domination approach in response to the Optimal Currency Area debate in Europe. The hypothesis is that the monetary union in Europe is irreversible. The current stage of bank regulation and financial prudential supervision is analysed through a comparison between the official purposes of the European Commission for the monetary union, as well as its actions in dealing with the recent crisis, and alternate ideas for resolving both current critical scenarios and the Union's failures. In order to illustrate this framework, the European Central Bank's financial integration indicators are presented as a background. The European Banking Union emerges as one of the main points of possible reforms after recent facts and negotiation issues, despite its preliminary stage. The main conclusion is that dynamic tools must be applied aiming to overcome the rigidity of the Maastricht Treaty without breaking it, pointing to a federalisation of the European Union as a reasonable fate, if one has in mind the pressure over members for abandoning the agreement.

1. Introduction

The European Union (EU) is a historical effort of economic co-

A preliminary version of this paper has been presented at the International Conference of the Brazilian Keynesian Association in August 2015. For comments and suggestions, I thank my advisor Simone Silva de Deos and my professors José Carlos de Souza Braga and Giuliano Contento de Oliveira, as well as my colleague Paulo José Whitaker Wolf. Any errors and/or omissions are the responsibility of the author alone.

ordination, perhaps one of the largest ever undertaken. Known as an important centre to generate employment and income, for cultural traditions, technological capacity and productive dynamism, over the period from 1970 until now, the EU presented a low level of activity compared to the Americas and Asia, although the union itself has been argued to be a form of ideal organisation that would overcome friction and allocate factors in a maximising way.

The impact of the international credit crisis and its consequences for EU countries, particularly in the Eurozone[1] since 2009, raise questions about the sustainability of the current arrangement as a path to sustained economic growth. The long process of European integration, whose summit was the establishment of the euro in 1999, is recognised as a worldwide paradigm.

The model of monetary and financial integration of the EU had not yet been through such turmoil. The crisis started in the Southern Europe countries, initially Greece in May 2010 and Ireland late that year, which were followed by Portugal in May 2011. Then major economies such as Spain, Italy and even France were affected in July 2012. Recession and threats to public budget equilibria in some of those countries called attention to the effectiveness of monetary, financial and banking policies of the European Central Bank (ECB)[2], and thus the European integration structuring purposes. During

[1] The EU is composed of 28 members, of which 19 have already adopted the euro as the single currency: Belgium, Germany, Estonia, Ireland, Greece, Spain, France, Italy, Cyprus, Luxembourg, Malta, Netherlands, Austria, Portugal, Slovenia, Slovakia, Finland, Lithuania and Latvia, thus forming the so-called "Eurozone". There are 7 countries, Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania and Sweden, that do not currently use the euro and two, Denmark and the UK, which are EU members, but chose not to use the euro when the Maastricht Treaty had been signed. Despite the latter two, the remaining countries that do not yet meet the conditions for adopting the single currency (many of the new Member States and Sweden) will replace their national currencies with the euro when they do. The euro has been adopted as the official currency in 4 other countries which are not part of the EU: the Principality of Monaco, the Republic of San Marino, the Vatican City State and lately also the Principality of Andorra.

[2] The ECB works with the central banks of all member countries to form the European System of Central Banks (Eurosystem).

2015, debt negotiation in Greece resulted in political debate of austerity versus activism of public sector after the Syriza group attempted to review demands of the ECB, the European Commission (EC)[3] and the International Monetary Fund (IMF) concerning their aid granted for rollover liabilities and to recover the economy.

The debate on the efficiency and relevance of the EU has been held mostly from the perspective of models of economic integration. In the 1960s, interpretations, such as the "optimum currency area", supposedly the most efficient integration arrangement for an economic area, consolidated that debate. However, in a Keynesian perspective, one can discuss the EU as a case of integration of different countries under the coordinating efforts of a leader, Germany, which is responsible for the arrangement of monetary policies and the framework of the ECB. Thus, at first, one can review both the effectiveness and efficiency of the optimal currency area model in Europe and its orthodox background, which includes austere rules of macroeconomic policy and financial liberalisation, by presenting the Keynesian interpretation. The latter criticises the need to impose such rules for different economies, since a possible effect could be inequality. The main point is the relevance of the European Monetary Union (EMU) and the role of the euro as an effective integration tool of development.

On the other hand, while the EU framework was under construction, financial dynamics produced a general consequence of the dynamics of capitalism since the 1970s. It is an interpretation that reveals the worldwide dominance of financial logic over economic priorities since the end of the Bretton Woods agreement, a process which liberalised financial markets where money plays a central role. Concerning the euro, it has established itself as a reference point

[3] The EC is an organ of debate and legislation set up to represent the EU interests as a whole. It may ensure the correct application of European law by the EU through initiatives by the European Parliament and the Council of the EU. The term "Commission" refers both to the EC's national members (Commissioners) as the institution itself in the broadest sense.

for wealth in Europe nowadays, so discussions of the relevance and effectiveness of the "optimum currency area" can go further, to the essence of financial logic, once the European project faces deep indebtedness and instability.

The discussion on the future of the euro includes a growing challenge of changing its fundamentals, for instance 1) reviewing European banking systems; 2) the degree of financial integration between countries and their institutions; and 3) banking regulation and supervision, so that financial integration, currently at an advanced stage in Europe, may proceed.

In order to discuss those points, this paper is organised as follows. The first section presents a theoretical debate between the "optimum currency area" view and the Keynesian interpretation, putting together the implications of austerity proposals as common rules for entry and performance in the EU. The second section emphasises the role of money and finance in the dynamics of European integration, in order to evaluate its limits and possibilities, notably the viability of the current arrangement under Minsky's paradigm of financial instability and the finance-led view. In the third section, we present empirical evidence concerning financial integration progresses and gaps in the EU. Then, in the fourth section we present a critical review of the European Banking Union proposal, with the background of the regulatory arrangement of financial and banking sectors. Finally, we present the conclusions.

2. Brief discussion on economic integration

In the orthodox view of monetary integration, central objectives (McKinnon, 2004) are the liberalisation of markets and stability of price levels, so that regional policies follow a uniform standard. Effects commonly expected of economic integration, according to this interpretation, would be increased trade and controlled inflation, under a common monetary policy.

In the 1960s, Mundell (1961) questioned the mechanisms of fluc-

tuation in exchange rates and discussed the possibility of creating the so-called "optimum currency area". Mundell's model led to the conclusion that an "optimum currency area" is established (or could be) when the mobility of factors of production, as a way to equalise different economic areas, replaces the need for exchange-rate fluctuations. Orthodox views indicates "real economic convergence" as a consequence of regional integration of members of the area, reflecting the best possible allocation of factors of production.

The evolution of the EU reflects a historical economic integration process since its foundation, in the Treaty of Rome (1957), when Member States have focused on the creation of the common market. With time, the need for monetary cooperation became higher. The "snake in the tunnel", in 1972, a well-known reaction to the Bretton Woods standard extinction, was a first step towards the creation of the European Monetary System (EMS), in 1979, which in turn laid the foundations for a new era of monetary co-operation. Years later, the Single European Act (1986), the so called "pan-European", was essential to facilitate movement of people and capital within the member countries. The goal of the EMU and the single currency has only been consolidated in the Maastricht Treaty (1992), when it established the rules for the introduction of the euro, the objectives of EMU and responsibilities of each member country as well as the conditions to be met for adopting the euro. These are the "convergence criteria" or "Maastricht criteria", namely price stability, with low inflation, stable exchange rates and sound public finances.

The purpose of the ECB since its creation lies in orthodox paradigms of austerity and the rules of the Maastricht agreement among EU members. Its main objective is to maintain price stability and to protect the value of the currency[4]. Recommendations to all Eurozo-

[4] In the first three years since its establishment on 1 January 1999, the euro was an invisible currency, only used for accounting purposes – for example, in electronic payments. The notes and coins came into circulation on 1 January 2002, replacing national banknotes and coins (for example, the Belgian franc and the German mark), at irrevocable conversion rates. Available in the official virtual page of the ECB: http://www.ecb.europa.eu.

ne's members in surplus or fiscal balance are on the basis of this programme, according to the Stability and Growth Pact of July 1997, as well as the monetary policy of the ECB itself, which is based on inflation targets. Parameters under which the ECB operates refer to the Delors Commission (1988-1992) and the Maastricht Treaty, resulting from negotiations lead by Germany and France, which decreed that the euro would be the common currency and the ECB would operate according to the structure of the German Central Bank (Bundesbank). In general, countries are recommended to achieve a high level of savings as a prime condition to make investments.

The Keynesian view, on the other side, is quite critical about the effects of market-driven integration and considers state intervention essential. For instance, unequal sectors or countries should receive unequal treatment; that is, each one according to its needs. General policies, or even the absence of specific ones, tend to perpetuate and further worsen existing inequalities between member countries (Amado, Mollo, 2004, p. 144). If there is significant difference of income among countries, the degree of uncertainty and liquidity preference becomes higher in the "periphery" than in the "centre", where there are more favourable conditions for financing. This can affect investment, and hence increase regional disparities, with a possible concentration of the banking system (*ibid.*, p. 137).

Orthodox proposals for regional development make inconsistent assumptions. Following the theory of "loanable funds", banks are financial intermediaries and allocate money through loans. When it is assumed that investment must "wait savings" the process becomes slow. This has a negative impact on disadvantaged areas, which depend on external capital flows, with impacts on new decisions and hence on the economy (Chick, Dow, 1988, p. 224). In Keynes, investment is the key variable and credit the instrument which enables the advancement of the banking sector, which finances production.

In addition, the orthodox interpretation ignores both information asymmetry and imperfect capital mobility. It is then difficult for it to study the EU establishment in terms of its financial dominance and macroeconomic instability. The focus should be on consolidating

long-term financing (Deos, Mendonça, Wegner; 2010). Another proposal is liquidity-management by the state, promoting countercyclical policies and articulating institutions in order to supply the market and guarantee investments, reducing macroeconomic instability.

The Keynesian interpretation of financial integration in the EU discusses Maastricht's arrangements in terms of their increasingly restrictive implications for member countries' performance.

"[…] The European 'single currency' was born with an original sin. From the beginning it embodied the tendency for permanent recessionary drift, differences in relative competitiveness among member nations, a wage squeeze, mounting social inequality, the dismantling of trade unions and continuous industrial restructuring". (Bellofiore, 2013, p. 504)

In this way, there would be a bias in the core of EU's dynamics, because there would be a "monetarist" and "anti-Keynesian" philosophy (Guttmann, Plihon, 2011, p. 13) guiding the ECB's policies, defending its own independence, targeting inflation as its main objective and balancing the public-sector finances of member countries (avoiding as much as possible rescue operations). That structure led to an overvaluation of the euro in financial markets (*ibid.*).

During the 2000s liquidity cycle, the Eurozone achieved results in a "neo-mercantilist" model (Bellofiore, 2013, p. 503) in which Germany, followed by the Netherlands and Denmark, led the process of accumulation, with strong emphasis through the export dynamics of high value-added goods, whose main destination was the set of "peripheral" member countries. These, in turn, with a negative trade balance, could not devalue the exchange rate, so the adjustment should be recessive. Despite the exogenous origin of the European crisis, it is dangerously integrated by structural characteristics of this "neo-mercantilist" model, which favoured Germany and was carried forward by the ECB.

These two groups of countries developed in different ways after the consolidation of the EMU. On one hand, the "core" group achieved low inflation, a productive dynamics driven by exports, trade surpluses and low public deficits. On the other hand, the "peripheral"

group, Greece, Ireland, Portugal, Spain and Italy, faced pressure from inflation, high public deficits etc. In this division of countries, France's position would be uncertain (Guttmann, Plihon, 2011, p. 15).

Imbalances among member countries come from divergence of labour productivity costs (Plihon, 2014). Despite what is guaranteed by the EC, labour mobility is not simple (Guttmann, Plihon, 2011, p. 15) and tax transfers from the "core" countries to the "peripherals" are insufficient to offset structural differences. Thus, development of the Eurozone has been partial and incipient because balanced public-finance requirements made it difficult for the new member countries and they are now very dependent.

The policy of recommending a high level of savings assumes that the Eurozone faces an adjustment problem to an "optimal currency area". According to the orthodox interpretation, deliberate actions by the public sector in order to increase resource-allocation efficiency may deteriorate long-term efficiency. This is a Walrasian interpretation (Minsky, 1985), for which the relative price level and allocation of resources are determined from aggregate supply, and currency and financial institutions have a neutral effect on trade between agents.

A complete theory must take into account the instability of economic structures and institutions. Keynes' theory combines the idea of creating resources, human and material, with the role of money and investment. Therefore it integrates both real and financial markets, from the point of view of effective demand, in opposition to orthodoxy dichotomy.

3. The Eurozone under financial dominance

In the neoclassical rational expectations approach (Sargent, 1987), agents make decisions based on all available and processed information, and any instability of the system is exogenous. But the behaviour of a portfolio manager is determined by investments, which, in turn, respond to his profit expectations. According to Keynes

(1983), risk and uncertainty affect economic activity once preference for liquid assets affects production decisions. The financial circuit connects both short and long-term expectations. Current contracts are based on debt and they also generate payment needs as part of the investment process. Current expectations reflect current profits, which pay current debts and determine future profit that will honour future debts. Minsky (1985) stated that, when institutions achieve good results, new debt structures are formed due to favourable expectations. However, this movement amplifies systemic instability because risk perception is prejudiced. A sustained period of financial stability may induce agents to adopt unsustainable debt structures, which, in turn, are systemically destabilising (*ibid.*).

The "financial dominance" interpretation indicates that financial assets are the criterion *par excellence* to calculate production and the allocation of wealth (Braga, 2000). Through history, as capitalism became finance-led, governments took larger and more interventionist policies, in order to stabilise the level of profit and to refinance debt structures, as long as deeper crises occurred. Big government is more efficient in earning stability (Minsky, 1986).

Throughout the 1960s, the USA dollar suffered a growing political challenge to its hegemony, especially by European countries such as France, while financial businesses expanded beyond the prudential controls of the Bretton Woods agreement (Belluzzo, 2009, p.286). Europe developed a defensive strategy in the face of dilemmas and constraints, after the USA abandoned the regime of Bretton Woods in 1971, with a growing consensus to create a strong single currency.

As a response, most of the European Economic Community (EEC) countries decided in 1972 to maintain stable exchange rates by preventing fluctuations of more than 2.25%, the so called European "snake in the tunnel". In March 1979, such a structure was substituted by the EMS. It was an arrangement established under the Jenkins European Commission (1977-1981), linking European currencies and defining the European Currency Unit (ECU) as a way to keep foreign-exchange rates within agreed bands. No currency was

designated as the anchor; nevertheless, the Deutsche Mark and the Bundesbank structured the EMS because of their relative strength and Germany's low-inflation policies. The EMS effort revealed the crucial role that convergence of economic policies played for the EU architects. Exchange-rate realignments, primarily unilateral decisions, became collective decisions, so the EMS was strengthened (Padoa-Schioppa, 1985).

In the early 1980s, the USA resumed its hegemony through a high interest-rate policy and international agreements with direct effects on its trading-partner economies (Tavares, Melin, 1997). Later, when the USA achieved a competitive devaluation of the dollar in the Plaza Agreement (1985), European currencies and also the Japanese Yen became overvalued, once they raised interest rates above USA's level. Periodic adjustments within the EMS raised the values of strong European currencies and lowered those of weaker ones, but after 1986 changes in national interest rates were used to keep the currencies within a narrow range. In the early 1990s the EMS was stressed by the differing economic policies and conditions of its members, especially the newly reunified Germany and the United Kingdom (which joined the EMS only in 1990).

During those years, speculative attacks on the French Franc, the Italian Lira and the British Pound Sterling led to a crisis of the EMS in September 1992, officially extinguished in 1998 as well as the ECU. Such an event can be seen as the root of the expansion of speculative operations in Europe, with a growing number of derivatives related to risk securitisation and financial arbitrage (Tavares, Melin, 1997, p.63). After that, the idea of an "optimal currency area" gained force, as well as the growth of dissatisfaction with Germany's leadership of the EMS. Key factors behind the drive to the EMU, such as the Delors Report (1989) ultimately led to the euro in further discussions and negotiations in the Maastricht Treaty (1992). However, critics point out that the euro happened to become subordinated to the dollar's financial dominance in global markets since then. Those fundamentals, before the establishment of the common currency in 1999, implied a low dynamism of exports of the Eurozone; nonetheless, its domestic trade grew (Tavares, Melin, 1997).

In the 2000s, finance-led accumulation standard had the most profound effects, showing the interpenetration, by the way of securitisation, of the banking system with the capital market and the USA dollar, as the latter reassured the whole process. Actually, reference to the dollar grows as reference to the USA public debt does the same (Tavares, Melin, 1997), indicating the ability of that country to establish a finance-led accumulation standard under its guarantee, and to expand it to the rest of world.

The collapse of deregulated financial operations since 2007 reached a great range of agents, namely important institutions such as Leman Brothers and a high number of states (Braga, 2009). Minsky (2011) explained how big banking apparatus was responsible for ensuring systemic solvency through Central Banks. According to Plihon (2014), in policy makers' mainstream theoretical view, the role of these institutions is to pursue inflation targets in order to maintain monetary stability, disregarding banking and financial stability policies[5]. However, governments around the world are conscious that Central Banks are lenders of last resort to the banking sector. In fact, they were also liquidity providers for all financial institutions, so this avoided worse impacts for the financial system as a whole.

The European system of payments plays an important role in the deepening of the recent crisis effects because the TARGET 2[6] operates with the effect that almost any asset, even those of highly dubious quality, can serve as collateral to be offered by commercial banks throughout the EU to their respective Central Banks in order to match daily open-market operations (Pessôa, 2012). Once the

[5] That is the "principle of separation" (Plihon, 2014), a kind of prevention against moral hazard. Notwithstanding, it is gradually being abolished (*ibid.*), once Ben Bernanke, USA's Federal Reserve chairman, acted differently from his predecessor Alan Greenspan and also Trichet and Draghi, ECB presidents, to ensure systemic liquidity. Such evidence indicates how limited the role of government in Europe was, something Draghi now seems to reconsider.

[6] TARGET 2 is the second generation of TARGET, the interbank payment system for the real-time processing of cross-border transfers throughout the EU, an electronic platform centred on the ECB's headquarters in Frankfurt. It is owned and operated by the Eurosystem.

ECB's monetary policy committee validated those kinds of operation, imbalances among members of the Eurozone were covered by reserve transfers between Central Banks, i.e. "core" EU countries accumulate large volumes of credit against the TARGET 2, as a reflection of their transactions with the "peripheral" ones, which in turn accumulate debts.

The subprime crisis of American mortgages contaminated insurance companies and banks worldwide, once GDP dynamics incorporated individual consumption through the securitisation of all kinds of receivable cash flows (Belluzzo, 2013, p. 142). Meanwhile, in Europe, treasury bonds of "peripheral" governments were, for German and French banks throughout the 2000s, something similar to the American subprime loans (Serfati, 2014a), that is, an easy and profitable path for financial operations, which then became "toxic" (Bellofiore, 2013, p. 505). The outbreak of the debt crisis in Eurozone countries with a high fiscal deficit in the years 2010-2012 reflected measures taken to bail out private banks and to support aggregate demand in a context of deep recession (Freitas, 2011, p. 35). However, the reversal of policies, that is, reduction of tax incentives, and successive austerity plans, adopted in response to pressure from international investors, contributed to further weakness of the Eurozone (*ibid.*). Plihon (2014) points out that there could be in the Eurozone a new type of "twin crises", a vicious circle between banking crises and sovereign debt, because governments' actions to rescue banks put public sector operations under pressure.

The crisis of public sectors in some countries of the Eurozone could be a second stage in the global financial crisis, in which Europe suffered most severely the consequences of the American crisis. Greece, Ireland and Portugal were hit in a first phase and then Spain, Italy and France so as well. Since then, the "core" countries of the Eurozone are "exporting unemployment" to the "peripheral" ones because there is not, in the Eurozone, an independent variable of adjustment (Plihon, 2014). This is a fact that contradicts the euro's purposes, namely to be an alternative to the USA dollar and to ensure an "optimal currency area". Since the financial credit crisis hit

Greece, Ireland, Portugal and Spain, public-debt levels have led to financial stress and these countries have been rescued through financial aids. That is, the EMU has been established but mechanisms for the management of instability have not. It showed up both the fragility and incompleteness of EU arrangement (Oliveira, 2012, p. 558).

3.1 The EU in a dilemma

For different reasons, the possibility that "distressed" countries exit the Eurozone is each day more likely. Some views state that it would be better to implement in Europe a multiple currency system, so that Europe would be a "multispeed zone", each country having a particular parity of its own currency to the euro (Mazier, Petit, 2013, p. 527). There are also views that propose turning the euro into a standard reference currency like the "bancor", original proposal of John Maynard Keynes during the negotiations of Bretton Woods in 1944, or even some other kind of alternative. However, both the absence of an international currency and the currency trade itself have already generated losses costly enough, as Amato and Fantacci (2012) point out. This crisis opens a window, as they say, so that efforts should be made in order to establish a new standard immediately, revoking financial logic worldwide.

Padoa-Schioppa (2010) claims that not "bancor" itself, but one of its "heirs", the IMF-issued Special Drawing Rights (SDRs), might fulfil the task. The EMU framework has already used the ECU through the 1980s, when it worked successfully. Now the SDRs could be triggered, in stages, so that currencies achieve stability at regional levels (e.g. the EU) and then globally, by the means of managing the creation and allocation of the common currency, in order to replace any current demand for reserves (*ibid.*). In such a framework, the author himself warns that coordination efforts involving existing institutions like the EU, the IMF, the BIS, the G7 and the G20 must undoubtedly be greater.

More incisive interpretations are recommending disruption. The

resolution of the financial stress of "peripheral" countries in the Eurozone would only be reached through the abolition of the euro as the single currency and a return to national currencies. Among them, Huerta González (2014) points out that the EMU creates a vicious circle, because the rules for adapting to the monetary standard conflict with the management possibilities of economic policy for each member country. Germany would have had the greatest benefits from the dynamics of the euro, prejudicing the strategic sectors of debtor countries. The euro standard establishes German omnipotence parallel to their claims in World War II. And because Germans repeatedly reprove sovereign intervention measures by the ECB, especially regarding QE measures (the expansion of liquidity through purchase of public assets of financially "distressed" countries), the current framework of the EU would inhibit any exit that is dangerous for monetary stability, the key role of the ECB.

However, the exit of any country from the euro or even the EU would be not only politically inconvenient, but also costly, because of the EU's current critical position. The EU faces a dilemma (Kregel, 2015) about which path to choose: aiming for currency stability or sustainable growth. Germany advocates austerity rules as a political strategy for cohesion; however, this implies a recessive impact for the distressed countries like Greece, and the economy would tend to stagnate (*ibid.*, p. 7). The alternative scenario of breaking the rules, i.e. allowing Greece to accelerate public spending, disregarding that disobedience of Maastricht criteria would set a precedent for other cases, moreover it would be an affront to stable countries.

Public and private-sector equilibria are required according to growth and financial stability criteria. To restore growth in countries with sovereign debt crises, a fiscal surplus must not result in private debt. The solution is to achieve a balanced international current account. However, the problem of "external adjustment" refers to relative salary-reduction policies or exchange rate devaluation (Kregel, 2015, p. 5), not to mention submission to the moods of global capital markets. Still, the achievement of a stable and feasible export surplus would demand a rate of foreign loans growing faster than the inte-

rest rate of commitments (*ibid.*, p. 7) which results in a Ponzi profile. Europe would be caught in such a politically unsustainable context, causing a prolonged period of "destabilising stagnation".

The problem is how to permit "distressed" countries to take counter-cyclical action without breaking the rules during a crisis. But, in a general view, it concerns the alternatives to both the threat of stagnation and instability. The "socialisation of investment", suggested by Keynes, is a possible answer. It reduces an economy's inherent inefficiencies in a way wide enough to avoid a collapse of profits, the cause of great depressions. Public-spending multiplier capacity is not infinite, thus fiscal deficit should focus on high-risk projects known to be expensive (Minsky; 1985). In order to achieve a coordinated expansion of spending and investment in Europe, starting from public-sector stimuli, Bellofiore (2013, p. 510) proposes that the so-called eurobonds, debt securities to be launched under the custody of the ECB, come to constitute the financial tools of a new policy, which would be the only way out of a deep and systemic debt crisis (Minsky, 2011, p. 88).

This is more reasonable than accepting any country's exit from the euro. There is a considerable degree of interaction, beyond the boundaries of national systems, between the operations of European banks, as a result of EMU terms and proposals. In one dimension, even if a country exits the euro it would still be deeply attached to the operations that banks perform. In another, supposing that a debtor country disrupts the exchange rate of the euro and re-establishes its national currency, there would be either an adjustment based on a devaluation of real wages, due to the recessionary impact, or a default of sovereign debt (in the case of a country's solvency crisis). In both cases a deflationary spiral of financial assets would worsen, "distressed" countries could transmit financial instability to balanced ones at an unpredictable rate, with a potential of contagion to all European banking systems (Toporowski, 2013, pp. 580-581), including important countries not using the euro[7].

[7] Particularly the United Kingdom should be mentioned here, once its relevant financial centre, the City of London, is highly connected to transactions in euros.

In addition to systemic liquidity support measures, Toporowski (*idem*, pp. 582-583) believes there is a more effective solution than the deflation of assets and its consequences. Levels of primary fiscal deficit and government investment should be maintained, the latter especially, in order to achieve a GDP growth at a faster rate than sovereign debt. This adjustment option should be taken in a dynamic approach, i.e. ensuring that financial commitments are carried sustainably in the long run, according to either Maastricht Treaty criteria or Fiscal and Stability Pact ones (*ibid.*, p. 583).

4. Progress on monetary and financial integration in the Eurozone

The European case is emblematic for the discussion of economic integration because the main issue lies with the financial dimension. Each member country has adapted the Maastricht criteria, and they still are, facing the rigid unified system of ECB standards, which symbolises both the "common rule" for entering the EU and the "insurance" of sound performance. However, national banking structures operate freely, actually responding to a liberalised and globalised financial system. There are evident biases, ineffectiveness, inefficiency, financial fragility – in sum instability and an incomplete framework, which results from the lack of proper regulation.

If Eurozone is an "optimal currency area", one of the main points should be its ability to bypass critical shocks through factor mobility without exchange-rate adjustments. GDP is highly concentrated in four members, namely Germany (29%), France (21%), Italy (16%) and Spain (10%), according to Eurostat data. However, there is divergence between growth paths. Until 2007, member countries achieved satisfactory results, while the international liquidity cycle favoured economic growth. But the region's growth was not significant; that might be an effect of ECB's rigid policies (Arestis, Sawyer, 2012, pp. 2-8). Countries of the Eurozone showed lower GDP growth through the period 2003-2014, in contrast to the EU as a whole, cu-

riously because Eastern European countries had higher rates before the financial crisis. Nonetheless, GDPs' movement reversals have also been strong.

A failure of the European project would have been the insufficient discussion precisely about the impacts of countries with structural differences (Arestis, Sawyer, 2012, p. 14). The hypothesis of "real economic convergence" is not clear in labour productivity movements, once few changes took place eleven years after the launch of the euro. It is also relevant to say Eurozone and EU labour productivity levels are lower than the ones in important European economies outside the EU and in the rest of the world.

Differences of inflation rates (Table 1) are also significant. Despite of ECB's monetary policy target, price levels are not homogeneous within countries. They are even more volatile where public debt levels are high (Table 2).

It is also important to point out that European integration led some of the so called "peripheral" countries to a considerable increase in their rates of domestic credit, namely Spain, Ireland, Portugal and Italy as it can be seen in their high standard deviation levels after the adoption of the euro (Table 3). Cyprus called the attention for its high level and then for a banking run threat in March 2013. EU countries as a whole have lower levels of domestic credit than the USA.

With the credit crunch, the ECB reduced interest rates as well as major economies also did, but later than the USA (Graph 1), which in turn had already taken a counter-cyclical monetary policy since 2007. The ECB came to work in the rescue of sovereign debt crisis countries in mid-2008, despite of its austerity program, and thereafter provided liquidity, financing public expenditure in these countries on the secondary market.

In fact, such measures took a reactive character and ineffective from the standpoint of combating financial speculative spiral (Bellofiore, 2013, p. 507).

According to the ECB Financial Report analysis of European integration in financial markets (ECB, 2015), there have been identified

TABLE 1

Harmonised indices of consumer prices (Annual average rate of change 2005 = 100) - Selected countries (2003-2014)

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Mean	St. Dev.
Latvia	2,9	6,2	6,9	6,6	10,1	15,3	3,3	-1,2	4,2	2,3	0,0	0,7	4,8	3,5
Estonia	1,4	3,0	4,1	4,4	6,7	10,6	0,2	2,7	5,1	4,2	3,2	0,5	3,8	2,0
Slovakia	8,4	7,5	2,8	4,3	1,9	3,9	0,9	0,7	4,1	3,7	1,5	-0,1	3,3	2,0
Lithuania	-1,1	1,2	2,7	3,8	5,8	11,1	4,2	1,2	4,1	3,2	1,2	0,2	3,1	2,2
Slovenia	5,7	3,7	2,5	2,5	3,8	5,5	0,9	2,1	2,1	2,8	1,9	0,4	2,8	1,2
Luxembourg	2,5	3,2	3,8	3,0	2,7	4,1	0,0	2,8	3,7	2,9	1,7	0,7	2,6	0,9
Spain	3,1	3,1	3,4	3,6	2,8	4,1	-0,2	2,0	3,1	2,4	1,5	-0,2	2,4	1,1
Greece	3,4	3,0	3,5	3,3	3,0	4,2	1,3	4,7	3,1	1,0	-0,9	-1,4	2,4	1,6
Malta	1,9	2,7	2,5	2,6	0,7	4,7	1,8	2,0	2,5	3,2	1,0	0,8	2,2	0,8
Cyprus	4,0	1,9	2,0	2,2	2,2	4,4	0,2	2,6	3,5	3,1	0,4	-0,3	2,2	1,1
Italy	2,8	2,3	2,2	2,2	2,0	3,5	0,8	1,6	2,9	3,3	1,3	0,2	2,1	0,8
Belgium	1,5	1,9	2,5	2,3	1,8	4,5	0,0	2,3	3,4	2,6	1,2	0,5	2,0	0,9
Austria	1,3	2,0	2,1	1,7	2,2	3,2	0,4	1,7	3,6	2,6	2,1	1,5	2,0	0,6
Portugal	3,3	2,5	2,1	3,0	2,4	2,7	-0,9	1,4	3,6	2,8	0,4	-0,2	1,9	1,2
Euro area (19 countries)	2,1	2,2	2,2	2,2	2,2	3,3	0,3	1,6	2,7	2,5	1,3	0,4	1,9	0,7
Finland	1,3	0,1	0,8	1,3	1,6	3,9	1,6	1,7	3,3	3,2	2,2	1,2	1,9	0,9
France	2,2	2,3	1,9	1,9	1,6	3,2	0,1	1,7	2,3	2,2	1,0	0,6	1,8	0,6
Netherlands	2,2	1,4	1,5	1,7	1,6	2,2	1,0	0,9	2,5	2,8	2,6	0,3	1,7	0,6
Germany	1,0	1,8	1,9	1,8	2,3	2,8	0,2	1,2	2,5	2,1	1,6	0,8	1,7	0,6
Ireland	4,0	2,3	2,2	2,7	2,9	3,1	-1,7	-1,6	1,2	1,9	0,5	0,3	1,5	1,5
Romania	15,3	11,9	9,1	6,6	4,9	7,9	5,6	6,1	5,8	3,4	3,2	1,4	6,8	2,9
Hungary	4,7	6,8	3,5	4,0	7,9	6,0	4,0	4,7	3,9	5,7	1,7	0,0	4,4	1,6
Bulgaria	2,3	6,1	6,0	7,4	7,6	12,0	2,5	3,0	3,4	2,4	0,4	-1,6	4,3	2,9
Croatia	2,4	2,1	3,0	3,3	2,7	5,8	2,2	1,1	2,2	3,4	2,3	0,2	2,6	0,9
United Kingdom	1,4	1,3	2,1	2,3	2,3	3,6	2,2	3,3	4,5	2,8	2,6	1,5	2,5	0,7
Poland	0,7	3,6	2,2	1,3	2,6	4,2	4,0	2,7	3,9	3,7	0,8	0,1	2,5	1,2
Czech Republic	-0,1	2,6	1,6	2,1	3,0	6,3	0,6	1,2	2,1	3,5	1,4	0,4	2,1	1,2
Denmark	2,0	0,9	1,7	1,9	1,7	3,6	1,1	2,2	2,7	2,4	0,5	0,3	1,8	0,7
Sweden	2,3	1,0	0,8	1,5	1,7	3,3	1,9	1,9	1,4	0,9	0,4	0,2	1,4	0,7
Turkey	25,3	10,1	8,1	9,3	8,8	10,4	6,3	8,6	6,5	9,0	7,5	8,9	9,9	2,7
Iceland	1,4	2,3	1,4	4,6	3,6	12,8	16,3	7,5	4,2	6,0	4,1	1,0	5,4	3,5
United States	2,3	2,7	3,7	3,2	2,6	4,4	-0,8	2,4	3,8	2,1	1,3	1,3	2,4	1,0
European Union (28 countries)	2,1	2,3	2,3	2,3	2,4	3,7	1,0	2,1	3,1	2,6	1,5	0,6	2,2	0,6
Norway	2,0	0,6	1,5	2,5	0,7	3,4	2,3	2,3	1,2	0,4	2,0	1,9	1,7	0,7
Switzerland	-	-	-	1,0	0,8	2,3	-0,7	0,6	0,1	-0,7	0,1	0,0	0,3	0,7

Source: Eurostat.

TABLE 2
Gross public debt (% of GDP) - Selected EU and Eurozone countries (2000-2014)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	Mean	St. Dev.
Eurozone	69,3	68,2	68,0	69,2	69,8	70,4	68,7	66,4	70,3	80,1	85,9	88,3	92,9	95,1	96,0	95,2	78,4	10,6
Greece	103,5	103,7	101,7	97,5	98,9	101,2	107,5	107,2	112,9	129,7	148,3	170,3	157,2	175,1	177,7	177,2	129,4	28,8
Italy	108,5	108,3	105,4	104,1	103,8	105,7	106,2	103,3	106,1	116,5	119,4	120,7	127,0	132,6	134,3	134,5	114,8	10,2
Belgium	107,8	106,5	103,4	98,4	94,0	91,9	87,9	84,0	89,2	96,6	96,6	99,2	101,1	101,6	101,7	100,3	97,5	5,3
Portugal	50,7	53,8	56,8	59,4	61,9	67,7	69,4	68,4	71,7	83,7	94,0	108,2	124,1	129,0	130,8	131,8	85,1	25,9
France	57,3	56,9	59,0	63,2	65,1	66,8	63,9	64,2	68,3	79,2	82,8	86,2	90,6	93,4	95,9	96,9	74,4	13,1
Germany	60,2	59,1	60,6	64,3	66,4	68,6	68,0	65,1	66,9	74,6	82,7	80,1	81,0	78,3	76,3	72,3	70,3	6,7
Austria	66,1	66,7	66,1	65,2	64,9	64,2	62,2	60,2	64,1	69,4	72,4	73,0	74,5	74,6	81,2	80,7	69,1	5,3
Ireland	37,0	34,5	31,8	31,0	29,4	27,2	24,6	24,9	44,2	64,4	91,2	104,1	117,4	123,7	121,9	121,1	64,3	36,7
Spain	59,4	55,6	52,6	48,8	46,3	43,2	39,7	36,3	40,2	54,0	61,7	70,5	86,0	93,9	98,3	101,4	61,7	17,7
Netherlands	53,7	50,7	50,5	51,9	52,5	51,8	47,3	45,3	58,4	60,7	63,4	65,7	71,2	73,4	74,7	74,9	59,1	8,8
Finland	43,8	42,5	41,5	44,5	44,4	41,7	39,7	35,2	34,0	43,6	48,8	49,4	53,7	57,0	59,9	60,7	46,3	6,5
Slovakia	50,3	48,9	43,4	42,4	41,5	34,2	30,5	29,6	27,9	35,6	41,0	43,6	52,7	55,4	55,2	56,2	43,0	7,7
Slovenia	26,3	26,5	27,8	27,2	27,3	26,7	26,4	23,1	22,0	35,2	38,7	47,1	54,4	71,7	77,2	80,9	39,9	16,5
Luxembourg	6,2	6,3	6,3	6,2	6,4	6,1	6,7	6,7	14,4	15,5	19,5	18,7	21,7	23,1	24,4	26,3	13,4	7,1
Estonia	5,1	4,8	5,7	5,6	5,0	4,6	4,4	3,7	4,5	7,1	6,7	6,1	9,8	10,0	9,9	9,7	6,4	1,8
Hungary	56,0	52,4	55,6	58,3	59,5	61,6	65,6	66,7	73,0	79,5	81,9	81,8	79,7	78,8	79,7	79,5	69,4	9,9
UK	40,5	37,3	37,1	38,7	40,3	41,7	42,7	43,7	51,9	67,1	78,4	84,3	89,1	90,6	91,5	93,1	60,5	21,3
Poland	36,8	37,6	42,2	47,1	45,7	47,1	47,7	45,0	47,1	50,9	54,9	56,2	55,6	57,1	50,2	51,7	48,3	4,8
Sweden	53,9	54,7	52,5	51,6	50,4	50,5	45,3	40,2	38,8	42,5	39,5	38,7	38,3	40,5	42,0	41,7	45,1	5,4
Denmark	52,4	49,6	49,5	47,2	45,1	37,8	32,1	27,1	33,4	40,7	42,8	46,4	45,4	44,5	45,8	48,6	43,0	5,5
Czech Republic	17,8	23,9	27,1	28,6	29,0	28,4	28,3	27,9	28,7	34,5	38,4	41,4	46,1	46,0	47,8	49,8	34,0	8,3

Source: Eurostat and OECD.

TABLE 3

Change in domestic credit* provided by the financial sector (% of GDP) - EU and other selected countries (2000-2013)

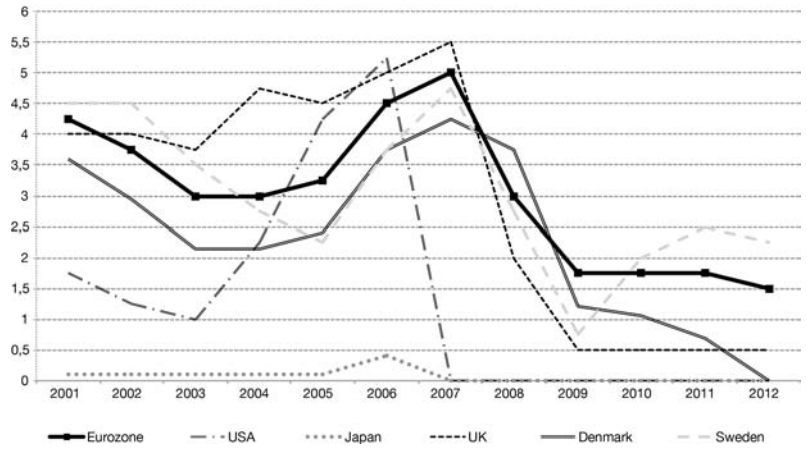
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	Mean	St. Dev.
Cyprus	234,73	239,57	191,61	191,13	187,91	191,23	204,33	224,19	280,17	302,99	315,75	327,98	347,34	335,82	255,34	54,00
Denmark	141,15	148,46	151,39	157,35	160,49	173,61	184,24	200,00	204,27	215,77	210,11	200,75	201,43	199,61	182,05	22,83
Spain	112,34	116,42	119,99	128,28	136,73	155,57	173,21	192,64	209,01	222,49	227,49	228,38	220,28	205,08	174,85	40,20
Netherlands	137,70	138,64	144,29	151,05	160,23	167,73	167,41	185,58	183,26	207,20	197,79	197,91	201,70	193,01	173,82	21,38
UK	124,15	130,58	135,51	138,69	146,87	153,05	162,40	178,00	201,55	215,57	209,09	199,28	195,65	184,09	169,60	28,00
Ireland	104,12	105,50	105,63	111,33	128,87	153,64	173,75	188,23	199,75	213,81	220,57	206,40	191,39	186,08	163,51	38,85
Portugal	126,75	135,61	135,81	135,54	136,43	139,98	150,21	159,79	170,85	187,34	200,63	198,01	193,52	183,27	160,98	23,96
Luxembourg	85,59	117,10	94,83	94,51	97,75	129,62	154,40	190,73	192,92	196,65	190,15	173,27	170,01	163,94	146,53	37,11
Malta	128,51	139,05	131,64	128,20	134,18	127,51	132,26	136,04	144,01	157,42	155,83	152,10	151,70	146,70	140,37	9,36
Germany	141,92	139,76	138,29	137,27	134,35	132,77	127,52	120,63	122,46	128,64	126,88	119,91	118,83	113,52	128,77	7,39
Austria	122,32	120,80	119,10	118,40	118,84	126,27	126,00	123,16	126,73	135,26	133,73	131,85	130,67	127,89	125,79	4,59
Italy	92,63	93,47	93,13	98,41	99,28	103,54	107,54	123,70	127,34	136,72	150,63	151,52	161,50	161,84	121,52	23,23
Sweden	46,26	100,73	101,03	100,96	102,62	111,88	116,15	123,67	127,32	136,14	134,67	136,32	139,92	138,06	115,41	18,42
France	100,33	102,35	100,12	102,18	102,69	105,70	111,65	118,35	120,44	125,25	128,64	129,40	132,54	130,75	115,03	11,45
Greece	86,72	95,13	95,23	89,79	90,75	103,34	104,45	108,91	111,48	112,79	146,20	153,79	135,19	134,29	112,00	17,46
Belgium	123,00	116,34	109,57	105,59	99,74	100,86	105,77	108,67	110,29	115,75	113,48	113,74	113,01	111,23	110,50	4,72
Finland	54,04	59,57	60,95	64,21	66,79	74,20	79,13	82,05	84,26	93,40	96,79	97,71	101,73	104,86	79,98	14,42
Estonia	34,50	38,26	43,92	50,48	60,10	67,81	80,39	89,39	94,68	103,17	96,20	83,42	76,19	71,60	70,72	18,47
Slovenia	41,98	44,63	42,85	46,61	55,06	64,29	71,93	80,44	85,55	91,15	95,23	91,57	91,98	82,78	70,43	18,17
Croatia	39,98	45,11	53,19	54,39	56,83	62,85	68,59	70,76	73,90	77,38	90,74	96,10	96,19	94,11	70,01	15,59
Hungary	54,48	48,85	52,35	56,67	57,39	61,39	67,36	74,30	79,72	79,63	81,09	76,10	67,51	64,69	65,82	9,28
Latvia	23,28	28,48	35,70	44,93	53,94	71,87	89,70	89,52	89,44	94,31	89,64	78,71	62,91	58,57	65,07	21,10
Czech Republic	45,58	41,94	38,93	44,71	41,15	39,84	44,60	49,02	53,27	57,73	60,03	64,39	65,03	66,97	50,94	8,82
Slovakia	55,78	58,96	50,39	42,77	41,96	47,06	48,75	50,44	53,07	-	-	-	-	-	49,91	4,24
Poland	34,35	36,86	37,06	38,29	37,48	37,36	41,83	45,88	59,85	60,63	62,61	64,98	63,00	65,77	49,00	11,84
Bulgaria	16,82	19,23	22,56	28,04	33,70	39,68	40,20	53,70	62,47	67,42	69,57	68,49	68,81	71,08	47,27	18,67
Lithuania	15,16	15,58	17,80	23,18	30,36	42,88	48,69	59,57	63,95	69,61	63,88	57,02	51,99	51,05	43,62	16,68
Romania	13,88	12,86	13,83	15,86	16,84	20,71	24,04	34,75	46,37	51,63	53,84	54,12	54,27	51,97	33,21	16,35
USA	190,96	198,59	191,79	206,58	212,92	216,33	226,32	235,72	216,76	231,36	227,13	227,22	232,40	240,55	218,19	13,34
Switzerland	158,19	153,88	154,87	158,87	159,99	161,78	165,53	168,12	165,84	176,14	173,54	175,64	182,83	173,43	166,33	7,39
Iceland	95,43	97,00	101,60	126,21	158,38	235,02	296,55	299,04	177,82	172,67	157,95	141,74	137,82	130,88	166,29	49,95
European Union (28 countries)	112,14	115,10	115,33	117,50	119,68	124,52	129,12	136,98	142,81	152,15	153,87	150,52	150,67	145,15	133,25	14,20
Zona do Euro (19 countries)	115,29	115,84	114,97	116,97	118,00	122,98	126,70	133,43	137,57	147,02	150,29	147,92	148,07	143,23	131,31	12,63
Norway	68,18	73,13	80,78	81,06	80,26	83,18	86,96	-	-	-	-	-	-	-	79,08	4,81

* Includes all private sector credit to various sectors according to the gross criterion, with the exception of credit to the central government (net criterion).

Source: World Bank.

two groups following average dispersion in relation to Germany's sovereign bonds rate of interest. Data and comments are available in the Data Appendix.

Graph 1
Interest rates - Annual targets set by central banks (2001-2012)



Source: Eurostat.

Distressed countries present high interest rates for their sovereign bonds, a much lower daily volume of euros borrowed through the EONIA rate (Euro Overnight Index Average Rate), as well as higher levels of domestic operations. Non-distressed countries, in turn, present low and intermediate interest rates for their sovereign bonds, equally high volume of daily euros traded and perform more transactions focused abroad, nonetheless within the Eurozone. This is a prime indication that financial markets are fragmented in the Eurozone, mainly within countries.

Notwithstanding, a general trend of increasing unsecured operations on the financial markets confirms liberalisation and globalisation effects in Europe, while both private equity and government bond markets presented, since the 2000s, a movement of deepening

integration, according to a price average indicator among countries. In the latter case, it reversed with the crisis of sovereign debts.

It is important to say that the banking market as a whole is highly integrated in the Eurozone, although their role, according to the national criterion, is concentrated. As mentioned in the first section of this paper, German and French banks prevail with more than half of assets share (34% and 23%, respectively), followed by Italy (14%) and Spain (12%), according to the Bankscope data. Moreover, Germany, France, Spain and Italy are the main nations figuring the 15 major institutions.

Further empirical evidence of integration gaps presented in this section can be found in the Data Appendix.

5. Advances in financial and banking regulation in the EU

It is important to note the relevance of the links between the balance sheets of monetary financial institutions. On one hand, European banks are increasingly internationalised, after all of them opened financial transactions to all Eurozone countries. On the other, both the scope of supervision and deposit guarantee systems remain at the national level (Plihon, 2013, p. 34). The role of the ECB should be reviewed, because the regulation system should be broader.

One implication of the ECB's framework is that the bank has got a European monetary authority status, acting independently, since their spending decisions are a result of the each member's spending decisions taken separately. However, discussions raise the question of ECB's legitimacy and policy sovereignty to launch bonds, that is, on behalf of all Eurozone (Aglietta, 2012, pp. 22-23), which would imply in a collective debt. Actually, the ECB opposes to Eurobonds and even so to act as lender of last resort (Dullien, Guerot, 2012, pp. 1-2) in the same way it discourages national central banks to trade treasure bonds in primary and secondary markets (Bellofiore, 2013, p. 508).

Inexorably, the economic crisis of the Eurozone raised up the po-

litical dimension of EU's framework failures. At the middle of governments' crisis, speculation and market pressure resulted in an official aid to Greece, Ireland, Portugal, Spain and Italy for the recapitalisation of banks, from the European Stability Mechanism. ECB President Mario Draghi's speech, in London on June 26th 2012 is still recognised as one of the most important movements to shift expectations about the euro's sustainability (Dullien, 2013).

5.1 The European Banking Union (EBU)

Also in June 2012 the European Systemic Risk Board and the Eurozone members proposed an agreement in order to review regulatory framework and create the EBU, in which the ECB would supervise, at least systemically, relevant financial institutions. The EBU proposal in the long run aims strengthening banking policy, unity, solidarity, the banking market as a whole, by preventing recurrent "traps" of self-deterioration commonly caused by deflationary spirals and crises of confidence. In the short term, it aims to establish supervisory arrangements and crisis resolution. At that moment, fiscal policy coordination, although not conclusive, was also rehearsed (Dullien, Fritz, Mülich, 2013, p. 11).

The answer to inherent problems of globalisation and market integration at the European and international levels is cooperation, coordination and coherence between national supervisory authorities. On September 12th 2012, EBU's five goals[8] were presented and EU authorities consolidated them later in December. The general objective is to prevent fragmentation of financial markets (Quelhas, 2012). Proposals focused on reducing contagion effects, detaching sovereign and bank debt, avoiding bail-out operations based on public resources and creating political institutions with key responsibilities. The main ones orbit around the European Systemic Risk Board (2010), in charge of debating such measures, to link micro-prudential supervision of banking, insurance and equity markets with macro-

[8] Quelhas (2012) systematised these proposals.

prudential supervision. The European Financial Stability Facility (2010) is meant to be a fund for countries and institutions in critical situation, triggered if the European Stability Mechanism (2012) authorises sovereign bail-out so that contagion may be prevented.

The European Banking Authority (2011), which is yet to operate, should apply stress tests over financial institutions and would pursue for them a growing resilience. Public debt monetisation of member countries is prohibited. The sovereign rating determinates the corporate rating so stress tests try to check if banks are strong enough therefore financial markets do not fragment on a national scale.

The alternative to the impact that bank bail-outs generate on public budgets is to internalise their costs with the introduction of taxes on financial institutions. The European Commission proposes taxes on financial transactions and activities (Quelhas, p. 269), based on the arguments of correcting negative externalities that the financial sector imposes on the economy, and requires consolidation budget from financial institutions in return both for the aid given by the public sector and also to tax arbitrage, which terms are still to be defined.

One key idea lies on the Single Supervisory Mechanism (2013) proposing the ECB as supervisor, letting Single Resolution Mechanism (2016) to establish the bankruptcy rescue apparatus (e.g. the uses of European Resolution Fund). Such point, however, is yet to be evaluated. The ECB would have specific responsibilities to oversee primarily the financial system and establish the European Banking Authority.

5.2 Criticism of the EBU proposal

It is known that European financial system stabilisation only entered the EU agenda after the outbreak of the 2007 crisis. Despite of the growing coordinative efforts so far, regulation of the EBU is rudimentary; to be implemented, it depends on a lot of political settlements. Resistance and disagreements within negotiations might lead to a fragmented framework, jeopardising European internal market consolidation (Quelhas, 2012). For instance, resolution of bank failu-

res involves the application of resources, which can create conflicts of interest both concerning the origin of money and who is going to be aided, while nothing is mentioned about a "pan-European" bankruptcy regime as originally indicated by the EC (Serfati, 2014b).

Effectiveness of the ECB's supranational control institutions such as the European Banking Authority is not guaranteed because of problems in unifying its regulatory characteristic. The bankruptcy regime for banks is taken under national procedures, that is, each country has autonomy to decide how aid is going to be managed. But failures in this process involve systemic risk and spread internal crises across borders, because banking activities are certainly connected in an international dimension (Plihon, 2014). For its part, the Single Resolution Mechanism may favour countries such as Germany, privileged by the proposal that would aid in a unified way only the big banks, known to be from "core" countries. It prevents distressed countries to be equally aided by profit transfers in comparison to non-distressed ones (id., 2013, p. 35).

Finally, centralising supervision of financial institutions means once again to strengthen both the ECB as lender of last resort (Aglietta, 2012, pp. 35-36) and the EC to formulate Long-term plans, e.g. an autonomous budget for the Eurozone, which in turn means stricter central controls on domestic spending and depends on a popular referendum, because a wider objective of federalisation is concerned (Watkins, 2013).

Advances from the EC and the ECB progress slowly. In response to a very large pressure generated by uncertainty regarding Eurozone economy, and worsened by Greek elections, the ECB took its boldest measure in January 2015, announcing the so-called "European Quantitative Easing", a sovereign assets buying program totalling € 1.1 trillion during a period of one year. However, such action is blunt[9] in comparison to the effective consolidation of real proposals for better regulation, such as EBU. Something more inci-

[9] This action helps short-term expectations, nonetheless in the European political context it only worsens relations between the ECB role and Germany's intentions to carry

sive would target the review of banking sector, separating retail activities, where essential functions are concentrated, and investment operations, taken under speculation and risk (Plihon, 2013; Serfati, 2014b). Public development banks and a European Public Bank, ruled by non-financial decision criteria, should be created in order to counter-balance ECB's market logic of supervision (Plihon, 2013, p. 35). Similarly, the already mentioned Eurobond market, as well as an expansion of the ECB's tasks, would be an alternative to lighten the critical scenario and also an improvement in the fiscal and monetary union, in a federal perspective.

6. Conclusion

This paper analysed the level of financial integration in the EU from a Keynesian perspective, taking into account the role of the ECB, the current stage of banking regulation in the Eurozone and the financial dynamics. The conventional debate, based on one hand the idea of the "optimum currency area" and, on the other, in an alternative interpretation, namely the Keynesian critical view, set place for another approach of the issue in the EU, specifically one that takes into account money and finance. So focusing the discussion on the future of the euro as common currency in the EU and the financial dimension of integration, "financialisation" emerges as a key interpretation stream, pointing finance as the main wealth evaluation criterion in the contemporary capitalism. This euro-centred debate within the "optimum currency area" theory proved to be limited, or even wrong. The main question is how financial wealth connected itself integrating very different countries under the same monetary standard, but without a sovereign institution that, in Minsky's terms, can mitigate the instability inherent to capitalism. That is central in understanding the EMU.

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Since the end of World War II, continuous integration guided political organisations in Europe. The idea of a federation would be a step forward because it implies a coordinated political arrangement, not only economical but also administrative and fiscal, especially in the issue of a new role for the ECB, whose sovereignty should be ratified through more effective actions on the financial sector.

The Eurozone banking regulation puts together monetary integration and fiscal autonomy. So far, the official proposal is "common rules" for all members, which is plausible. The evidence presented here based on the ECB reports showed that financial integration is in progress. But the remaining differences between member countries politically affect Eurozone's equilibrium. At ECB's optic, the emergence of "subgroups" inhibits the "optimum currency area" of functioning properly. According to the finance-led approach, however, such "subgroups" are consequence of regional fragmentation which emerges from the accumulation process driven by finance, something that will only be overcome with isonomic policies that take into account the varying degrees of liquidity preference within the Eurozone.

EBU's proposal is admirable as it contributes in some way to prudential supervision rules that aim a more equal EU. It needs to move forward in order to consolidate a broad effort to control capitalism's fluctuations, as well as to effectively integrate Europe, the most arduous task.

Common interest must prevail if member countries want the EU to be successful. If it does, then it will ratify itself as a global paradigm. However, as the effects of integration seem to point to standardisation, on one hand, but also clearly to inequality, on the other, favouring mainly Germany, Eurozone's leader, it seems necessary to advance the fiscal issue.

Once a historic option for coordinating different economies was made, the federalisation of the Eurozone is not only the next step, but also a reasonable fate if one takes into account the real danger represented by potential exit of member countries. Federalisation enables both a more efficient reallocation of resources that will re-

cover public spending dynamics sustainably and can provide a stable stimulus for private investment.

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Data Appendix

Eurozone GDP Share - Eurozone (2014)

	Million €	%
Eurozone (19 countries)	10,103,473	100.0
Germany	2,915,650	28.9
France	2,132,449	21.1
Italy	1,616,254	16.0
Spain	1,058,469	10.5
Netherlands	662,770	6.6
Belgium	402,027	4.0
Austria	329,296	3.3
Finland	205,178	2.0
Ireland	185,412	1.8
Greece	179,081	1.8
Portugal	173,044	1.7
Slovakia	75,215	0.7
Luxembourg	49,428	0.5
Slovenia	37,246	0.4
Lithuania	36,309	0.4
Latvia	24,060	0.2
Estonia	19,525	0.2
Cyprus	17,506	0.2
Malta	7,912	0.1

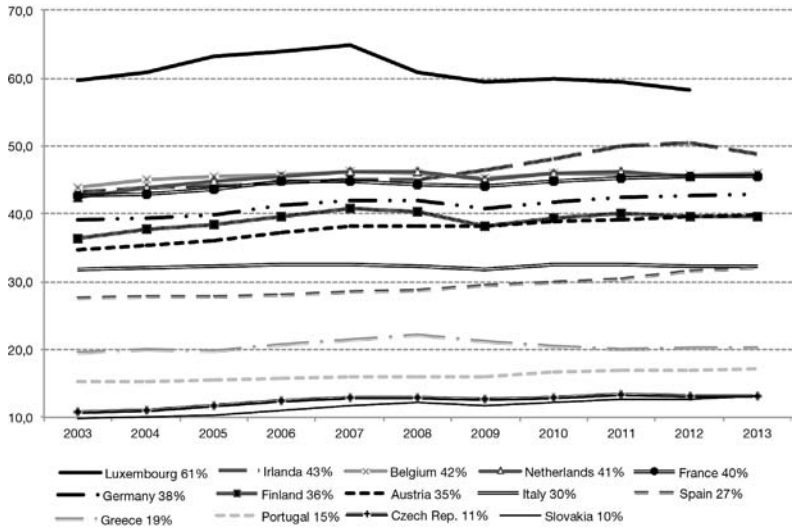
Source: Eurostat.

GDP Annual Growth (%) - EU, Eurozone and selected countries (2003-2014)

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Mean	St. Dev.
European Union (28 countries)	1,5	2,5	2,0	3,4	3,1	0,5	-4,4	2,1	1,7	-0,5	0,0	1,3	1,1	1,5
Eurozone (19 countries)	0,7	2,2	1,7	3,3	3,1	0,5	-4,5	2,0	1,6	-0,8	-0,4	0,9	0,9	1,5
Slovakia	5,4	5,2	6,5	8,3	10,7	5,4	-5,3	4,8	2,7	1,6	1,4	2,4	4,1	2,9
Latvia	8,6	8,9	10,2	11,6	9,8	-3,2	-14,2	-2,9	5,0	4,8	4,2	2,4	3,8	5,5
Estonia	7,5	6,5	9,5	10,4	7,9	-5,3	-14,7	2,5	8,3	4,7	1,6	2,1	3,4	5,1
Iceland	2,7	8,2	6,0	4,2	9,7	1,2	-5,1	-3,1	2,4	1,3	3,6	1,9	2,8	3,0
Lithuania	-	-	-	7,4	11,1	2,6	-14,8	1,6	6,1	3,8	3,3	2,9	2,7	4,1
Luxembourg	1,2	4,9	4,1	4,9	6,5	0,5	-5,3	5,1	2,6	-0,2	2,0	-	2,4	2,5
Malta	2,5	0,4	3,8	1,8	4,0	3,3	-2,5	3,5	2,3	2,5	2,7	3,5	2,3	1,2
Ireland	3,0	4,6	5,7	5,5	4,9	-2,6	-6,4	-0,3	2,8	-0,3	0,2	4,8	1,8	3,1
Slovenia	2,8	4,4	4,0	5,7	6,9	3,3	-7,8	1,2	0,6	-2,6	-1,0	2,6	1,7	3,0
Austria	0,8	2,7	2,1	3,4	3,6	1,5	-3,8	1,9	3,1	0,9	0,2	0,3	1,4	1,4
Belgium	0,9	3,4	1,9	2,6	3,0	1,0	-2,6	2,5	1,6	0,1	0,3	1,0	1,3	1,2
Cyprus	2,8	4,4	3,9	4,5	4,9	3,6	-2,0	1,4	0,3	-2,4	-5,4	-2,3	1,1	2,9
Germany	-0,7	1,2	0,7	3,7	3,3	1,1	-5,6	4,1	3,6	0,4	0,1	1,6	1,1	1,8
Finland	2,0	3,9	2,8	4,1	5,2	0,7	-8,3	3,0	2,6	-1,4	-1,3	-0,1	1,1	2,7
Spain	3,2	3,2	3,7	4,2	3,8	1,1	-3,6	0,0	-0,6	-2,1	-1,2	1,4	1,1	2,2
Netherlands	0,3	1,9	2,3	3,8	4,2	2,1	-3,3	1,1	1,7	-1,6	-0,7	0,9	1,1	1,6
France	0,8	2,8	1,6	2,4	2,4	0,2	-2,9	2,0	2,1	0,3	0,3	0,4	1,0	1,2
Portugal	-0,9	1,8	0,8	1,6	2,5	0,2	-3,0	1,9	-1,8	-4,0	-1,6	0,9	-0,1	1,8
Italy	0,2	1,6	0,9	2,0	1,5	-1,0	-5,5	1,7	0,6	-2,8	-1,7	-0,4	-0,2	1,7
Greece	6,6	5,0	0,9	5,8	3,5	-0,4	-4,4	-5,4	-8,9	-6,6	-3,9	0,8	-0,6	4,4
Poland	3,6	5,1	3,5	6,2	7,2	3,9	2,6	3,7	4,8	1,8	1,7	3,4	4,0	1,2
Romania	5,1	7,1	4,7	7,4	7,1	7,2	-6,3	-1,7	1,1	1,6	3,4	2,6	3,3	3,2
Bulgaria	5,4	6,6	6,0	6,5	6,9	5,8	-5,0	0,7	2,0	0,5	1,1	1,7	3,2	3,0
Czech Republic	3,6	4,9	6,4	6,9	5,5	2,7	-4,8	2,3	2,0	-0,8	-0,7	2,0	2,5	2,5
Sweden	2,4	4,3	2,8	4,7	3,4	-0,6	-5,2	6,0	2,7	-0,3	1,3	2,1	2,0	2,1
United Kingdom	4,3	2,5	2,8	3,0	2,6	-0,3	-4,3	1,9	1,6	0,7	1,7	2,8	1,6	1,5
Hungary	3,8	4,8	4,3	4,0	0,5	0,9	-6,6	0,8	1,8	-1,5	1,5	3,6	1,5	2,2
Croatia	5,6	4,1	4,2	4,8	5,2	2,1	-7,4	-1,7	-0,3	-2,2	-0,9	-0,4	1,1	3,2
Denmark	0,4	2,6	2,4	3,8	0,8	-0,7	-5,1	1,6	1,2	-0,7	-0,5	1,1	0,6	1,6
Serbia	4,4	9,0	5,5	4,9	5,9	5,4	-3,1	0,6	1,4	-1,0	2,6	-1,8	2,8	3,0
USA	2,8	3,8	3,3	2,7	1,8	-0,3	-2,8	2,5	1,6	2,3	2,2	2,4	1,9	1,2
Switzerland	0,0	2,8	3,0	4,0	4,1	2,3	-2,1	3,0	1,8	1,1	1,9	-	1,8	1,3
Norway	0,9	4,0	2,6	2,4	2,9	0,4	-1,6	0,6	1,0	2,7	0,7	2,2	1,6	1,2
Albany	-	-	-	-	-	-	3,4	3,7	2,5	1,6	-	-	0,9	0,8

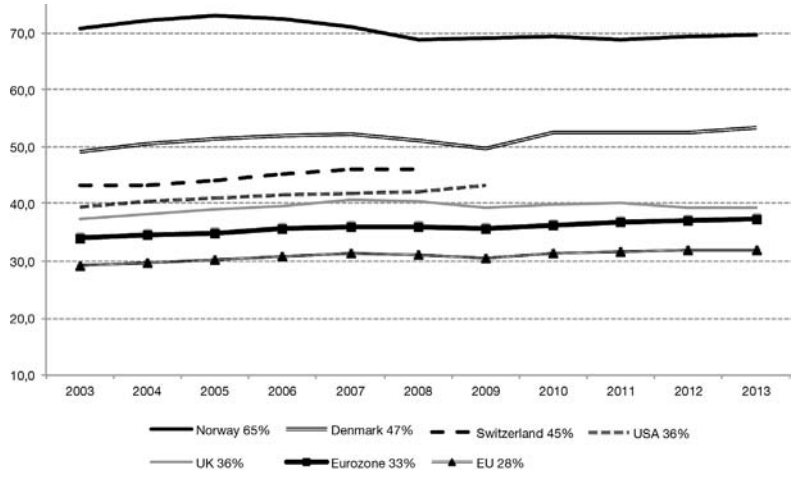
Source: Eurostat.

Labour Productivity Annual Variation (%) - Selected Eurozone (2003-2014)



Source: Eurostat.

GRAPH 2
Labour Productivity Annual Variation (%) - Eurozone and Selected countries (2003-2014)

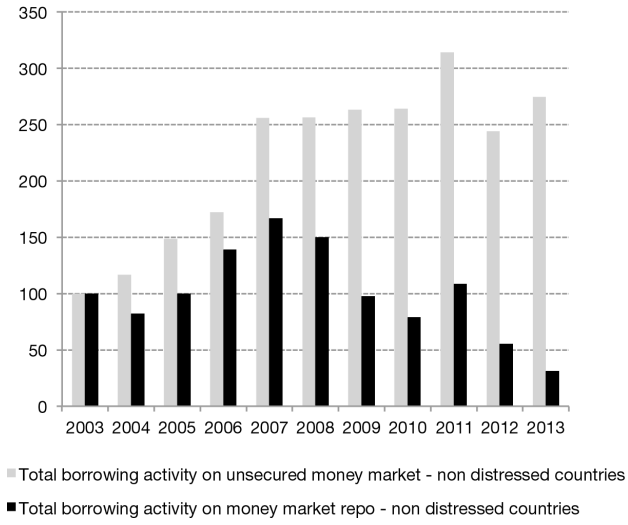


Source: Eurostat.

Analysis of European integration in financial markets

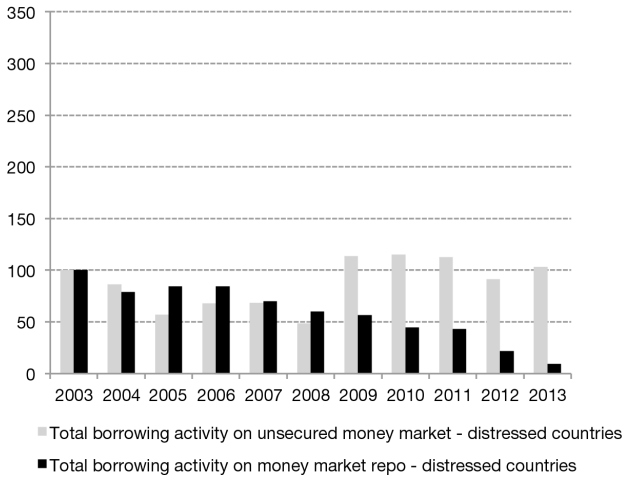
The ECB Financial Report (ECB, 2015) analyses financial integration in the EU countries. The main variable is long-term interest rates of government bonds maturing in about ten years. There have been identified two groups according to the average dispersion in relation to Germany's rate: a) "distressed" countries, with high rates (Cyprus, Greece, Ireland, Italy, Portugal, Slovenia and Spain); b) "non-distressed" countries, with low or intermediate rates (Austria, Belgium, Estonia, Finland, France, Germany, Luxembourg, Malta, the Netherlands and Slovakia).

Graph a
Borrowing activity in the Eurozone (average daily turnover, indexed on 2002 = 100) - "non-distressed" countries (2003-2013)



Source: ECB (2015).

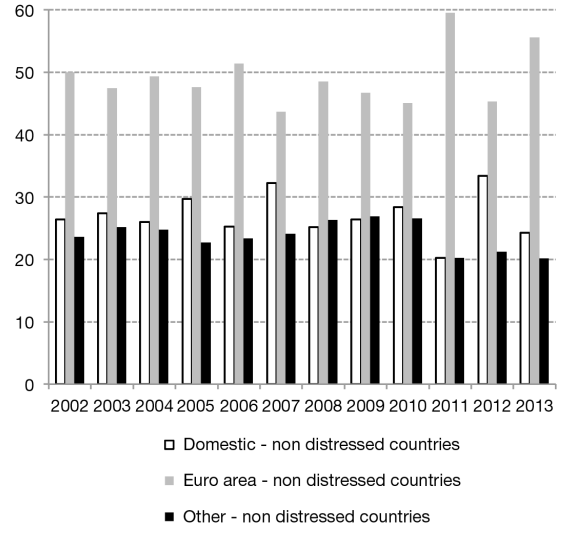
Graph b
Borrowing activity in the Eurozone (average daily turnover, indexed on 2002 = 100) - "distressed" countries (2003-2013)



Source: ECB (2015).

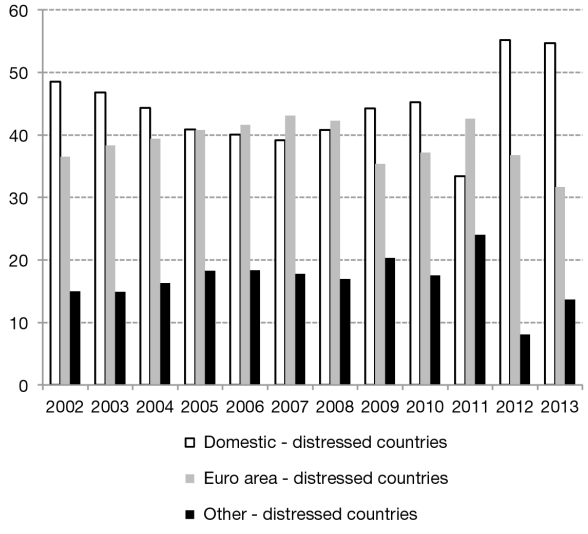
The quantity-based borrowing indicator of daily volume of euros, with its 30-day moving average, traded by the Euro Overnight Index Average Rate (EONIA) shows borrowing for both groups of countries in the graphs a and b, respectively. The volume of loans is very different between them. There was an increase for insured activities (identified by the EUREPO criterion, which is the rate at which one prime bank offers funds in euro to another prime bank if in exchange the former receives from the latter securities as collateral) in both groups of countries by 2007, however it is retracting since then in favour of the unsecured ones, less regulated and less complex. Both difference of volumes and the "unsecured" trend might be evidences of fragmentation on these markets (ECB; 2015).

Graph c
Geographical counterparty breakdown for transactions (% of total transactions) - "non-distressed" countries (2002-2013)



Source: ECB (2015).

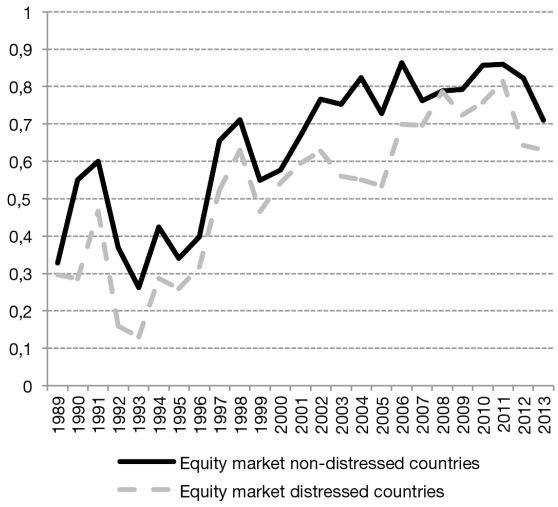
Graph d
Geographical counterparty breakdown for transactions (% of total transactions) - "distressed" countries (2002-2013)



Source: ECB (2015).

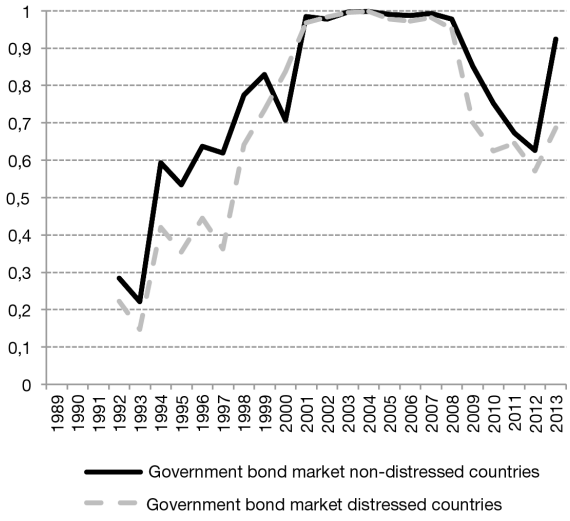
Quantity-based indicators concerning geographical counterparty breakdown show that monetary transactions are usually combined in such a way that the secured ones have a greater weight (Graphs c and d). Domestic operations have a higher percentage in "distressed" countries and the "non-distressed" ones perform more transactions focused abroad, nonetheless within the Eurozone. The latter's better ability in conducting operations across borders might reveal financial fragmentation between the two groups.

Graph e
Equity market integration based on common factor portfolios (econometric index) - (1989-2013)



Source: ECB (2015).

Graph f
Government bond market integration based on common factor portfolios (econometric index) - (1989-2013)

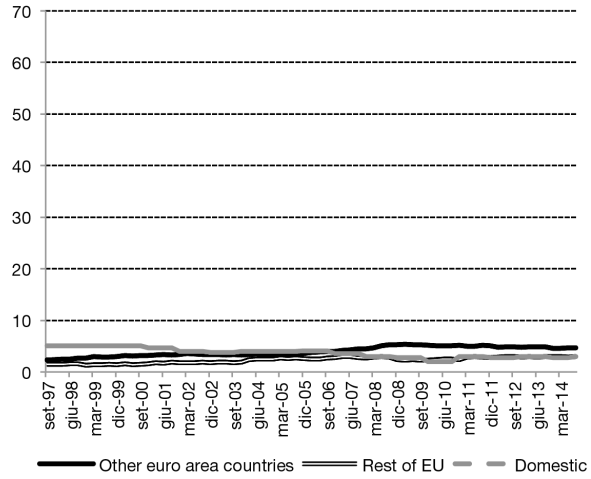


Source: ECB (2015).

Notwithstanding previous indicators showed fragmentation trends between the groups, price-based security markets indicators (Graphs e and f, according to a price average between countries, ranging from 0, which is not integrated, to 1, which means full integration), show the deepening of integration in the private equity market. On the other hand, in the government bond markets the increasing integration movement that lasted until mid-2008 reversed with the crisis of sovereign debts and returned to higher levels in 2013.

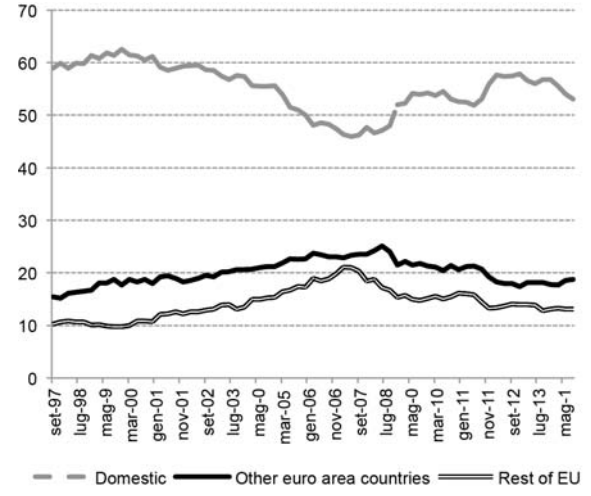
Activity-based indicators (Graphs g and h) show that the banking market in the Eurozone is more integrated than the retail market, because monetary financial institutions (MFIs) lend considerably more to their congeners that to non-financial ones (non-MFIs).

GRAPH G
MFI loans to non-MFIs: outstanding amounts by residency of the counterpart (%) - (1997-2014)



Source: ECB (2015).

GRAPH H
MFI loans to MFIs: outstanding amounts by residency of the counterpart (%) - (1997-2014)



Source: ECB (2015).

Active banks gathered by country - Selected Eurozone countries (2014)

	Total assets (US$ million)	Total number of institutions	Share of total assets (%)
Germany	11.010.211	608	33,97
France	7.317.883	70	22,58
Italy	4.459.233	73	13,76
Spain	3.754.250	47	11,58
Netherlands	1.440.502	16	4,44
Belgium	1.049.859	17	3,24
Austria	710.423	35	2,19
Ireland	702.328	8	2,17
Finland	618.328	9	1,91
Luxembourg	534.033	38	1,65
Portugal	424.477	10	1,31
Greece	177.668	4	0,55
Slovakia	94.124	9	0,29
Cyprus	50.988	5	0,16
Latvia	23.364	9	0,07
Estonia	19.586	4	0,06
Malta	17.598	7	0,05
Slovenia	7.470	3	0,02

Source: Bankscope.

15 Major banks according to total assets (2014)

	US$ billion
1. Deutscher Sparkassen-und Giroverband eV	3.185
2. BNP Paribas	2.483
3. Deutsche Bank AG	2.222
4. Société Générale	1.704
5. Banco Santander SA	1.539
6. Genossenschaf tlicher FinanzVerbund	1.439
7. UniCredit SpA	1.167
8. BPCE SA	988
9. Cooperatieve Centrale Raif feisen-Boerenleenbank B.A-Rabobank Nederland	930
10. Intesa Sanpaolo	864
11. Banco Bilbao Vizcaya Argentaria SA	803
12. Banca d'Italia	765
13. Commerzbank AG	758
14. Fédération du Crédit Mutuel	704
15. DZ Bank AG-Deutsche Zentral-Genossenschaf tsbank	534

Source: Bankscope.