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Are Austerity Measures Leading to a North-South Divide?

In recent years, notions of a north-south divide within the European Union – and in particular within the eurozone – have increasingly gained attention in the European discourse. On the surface, this north-south divide has been discussed on the foundation of diverging economic performances between northern and southern European countries as a consequence of the euro crisis. And indeed, the southern European countries Portugal, Spain, Italy, Cyprus and Greece have been hit disproportionally hard by the crisis, while their northern European partners have managed to sail rather calmly through these choppy waters.

This is illustrated well when comparing major economic indicators of eurozone countries over time since the outbreak of the euro crisis in 2009. These figures highlight that the eurozone's north (Germany, Finland, the Netherlands and Austria) performs considerably better than its south. While public debt has soared in the whole eurozone, the development in southern Europe has been particularly worrying. Greece (169.1% of GDP), Italy (133.3% of GDP) and Portugal (131.3% of GDP) are facing much higher public debt than the eurozone-17 average (93.4% of GDP). Spain and Cyprus have nearly doubled their public debt since the outbreak of the euro crisis. The serious fiscal situation of the southern European countries has undermined their creditworthiness thus constraining their activities on the financial markets. As a result, yields for 10-year bonds of southern European states have skyrocketed and have burdened them with high borrowing costs. In contrast to these developments, northern European countries have benefited from the safe-haven impact and can continue to borrow at the same or even lower costs. For example, Portugal's 5.675% yield on 10-year bonds differs significantly from Germany's 1.944% interest rate. The division on the financial markets has also impaired the economic performance in southern European countries that have experienced a much harsher economic recession than their northern European partners, which have benefited from capital and investment shifting away from the south and improved borrowing conditions for their companies. The Greek economy has been suffering in particular, undergoing the sixth consecutive year of recession, while Germany or Austria have been able to withstand the economic turbulences that have surrounded them fairly well maintaining robust growth. The harsh recession quickly trickled down onto the labour markets in the south where unemployment rates have sharply risen – 15.8% in Portugal, 16.8% in Cyprus, 26.6% in Spain and 27.4% in Greece. These rates are significantly higher than the eurozone average of 12.2% and the unemployment rates in northern European countries like Austria (5%), Germany (5.2%) or Finland (7%). Even worse, the youth in southern Europe has been hit particularly hard by the recession in their home countries: Greece (54.8%) and Spain (56.8%) where more than half of young people under 25 are unemployed are particularly affected.

Certainly, traces of a north-south divide in the eurozone with regard to economic fundamentals such as (youth) unemployment, purchasing power, income per capita or GDP per capita have existed long before the European sovereign debt crisis unfolded. However, the dividing lines always seemed bridgeable for the south as the European project promised a rapprochement and the prospect of growth and prosperity. Today, however, the EU's potential to achieve economic and social convergence is challenged more and more because the euro crisis has deeply aggravated the division between north and south but also between the different regions within these two poles itself. Furthermore, taking stock of the EU's crisis management 5 years into the crisis, one has to assess that the austerity measures that were agreed between the Troika and the southern debtors have so far rather cemented this divide.

Lack of a common analysis

However, the north-south divide in the Eurozone goes deeper than pure economic figures. More fundamental is the disunity about a common analysis for explaining the underlying causes of the euro crisis. On the one hand, the debate in northern Europe has almost solely revolved around the profligacy of the south that – according to the northern perception – has lived considerably above its means and has missed out on essential structural reforms for years. On the other hand, southern European member states nearly solely emphasise the systemic weaknesses of the eurozone, the role of trade imbalances in the eurozone and the impact of the global financial crisis on their national economies when explaining the causes for the crisis, while mostly neglecting domestic problems. Consequently, both diverging narratives touch upon the realm of identity, responsibility and perceptions leading to a resurgence of long forgotten stereotypical regionalism and nationalism. This disunity holds true despite numerous actions on which the member states have commonly agreed on in the course of the crisis management (i.e. Fiscal Compact, European Semester, Stability and Growth Pact, Euro Plus Pact, ESM) as these solutions seem not to reflect a preceding balanced and common analysis, debate and negotiation process. After 5 years of opposing narratives, which have penetrated the respective thinking of the north and south, it has become more and more difficult to achieve an inclusive process which is necessary in order not to leave the south with the subtle feeling that decisions in the EU have been taken over its head in this crucial time of the euro crisis. Otherwise, the southern European countries might come, in the end, to the conclusion that further structural reforms and efforts for fiscal consolidation do not pay off in the light of the hardship that their citizens have to cope with, as well as political instability and frequent government changes these countries have been struggling with. Likewise, what if the belief establishes itself in northern European countries that solidarity with the south is leading nowhere, as the situation in the crisis-stricken south fails to improve and further rescue packages become more likely?

And, indeed, it can be observed that the EU Member States have been caught in a battle of ideas about the proper remedies for the eurozone. This cleavage runs along the question of the right balance between austerity and growth. Greece, Cyprus, Italy, Spain and Portugal are increasingly struggling to balance their policies between the demands of their creditors and a public opinion that is expressing strong criticism of the euro crisis management. A large part of the public and political opposition forces in these countries blame first and foremost Germany for increasingly imposing its economic preferences on others in the eurozone. In their view, the German insistence on a policy of conditionality, based on stringency and fiscal consolidation, in return for financial rescue packages has a causal role in the ongoing economic crisis in their countries and the deteriorating social situation. Thus, an immediate turn-around of the crisis management including substantial growth stimuli and a mutualisation of debt would strongly be necessary. Even the Franco-German relationship, the crucial engine for European integration, has been caught in this battle. While the French President François Hollande wants to boost the economy through additional public spending, the German government has emphasised that austerity and growth do not oppose but condition each other as sound public finances build the foundation for sustainable economic growth. It is very likely that the new 'Grand Coalition' in Germany intends to pursue this current policy strategy in the euro crisis management, as long as the ultimate moment arrives when the crisis-stricken countries of the south experience sustainable growth and consolidated public finances. At least for the foreseeable future, Germany will continue to push for applying the thumbscrews until a growing isolation within the European Council could lead to a policy change. Other northern European countries like the Netherlands, Finland and Austria have been, perhaps, quite happy to hide behind the broad back of Germany and do not promote Berlin's strict policy approach in the course of the crisis management that pronouncedly. Nevertheless, all of these countries are united by the mutual interest in preserving the stability of the eurozone thus holding on to strict conditionality.

The EU has responded to the euro crisis in its very own incremental step-by-step approach carefully aware to integrate the interests of all Member States. However, the austerity policies that have been implemented in the south have so far been of limited success. But what could a blueprint of a recalibrated crisis management approach look like? Many proposals are on the table and have been widely discussed. While there has already been general agreement on the importance of a dual-strategy combining short-term measures to stabilise the crisis-stricken Member States and long-term measures that aim to establish a crisis-resistant institutional framework, disagreement remains regarding the concrete policy content. The main point of contestation is the question whether or to what extent existing or future public debt of the crisis-stricken countries should be mutualised – be it i.e. by introducing Eurobonds in order to facilitate the refinancing of governments on the financial markets or by introducing joint liability mechanisms within the framework of a banking union. A more growth friendly strategy could entail i.e. the upgrading of the European Investment Fund or the establishment of a European Investment and Construction Fund financed by the Financial Transaction Tax. Whether a policy change will come about, however, also depends on the future economic situation in the north. It will be interesting to observe to what extent the Member States of the north will preserve their unity or whether more growth-friendly policies gain ground in case the economic downturn spreads more and more northwards such as has already been happening in the Netherlands.

Conclusions

European integration used to be about bringing greater economic and social convergence to Europe. The customs union, the Single Market and the Economic and Monetary Union are all major stages in this process. The current economic and financial crisis seems to have reversed this positive development and greater convergence has been replaced by growing economic and political divisions in Europe, mostly visible in a growing north-south divide. Even if there should finally be light at the end of the tunnel of the Euro crisis, visible scars will remain as this division does not only reflect pure economic performance but the resurgence of nationalist stereotyping at the expense of European solidarity.

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