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Asymmetric paths of public debts and of general government deficits across countries *within* and *outside* the European monetary unification[☆]

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ABSTRACT

The main aim of this study is to analyze the evolution of public debts and of government deficits/surplus across European countries *within* and *outside* the monetary unification. In particular, this study compares the dynamics of public debts and of general government deficits between European countries *within* and *outside* the monetary unification for the preceding and subsequent period the introduction of the Euro currency. Statistical analyses show that the evolution of public debts and government deficits/surplus is significantly different between European countries. Nations *within* the European monetary unification seem to have, from 2001 onwards, a deteriorated sovereign debts and government deficits in comparison to countries *outside* the European monetary unification. This dissimilar evolution of public debts and of government deficits between European countries can be due to manifold factors. Moreover, these asymmetric paths of public debts and of government deficits across European countries may be one of contributing factors that generates uncertain scenarios and negative socio-economic effects on patterns of growth of the overall European Union economy.

> A state debtor to foreigners is a serious evil, this economic fact is so evident that does not require proof.
>
> (Galiani, 1780, p. 361).

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1. Introduction

This essay has two goals. The first is to show the dissimilar evolution of public debts and of general government deficits across European countries *within* and *outside* the European monetary unification. The second is to show the deteriorated paths of public debts and of general government deficits of countries within European monetary unification and possible causes, and to stress the importance of measures of expansionary political economy, rather than austerity programs, directed to ameliorate European economic growth and debt over the long run (Coccia, 2005, 2007, 2009). These topics are basic to explain the factors that are increasing debt-to-GDP ratios and unemployment in the Euro zone with several socioeconomic problems (*cf.*, Coccia, 2013). The analysis of the evolution of public debts and of government deficits is also important to European policy makers to design financial measures for the stability and growth over the long run (*cf.,* Equiza-Goñi, 2016; Paniagua, Sapena, & $2 Tamarit, 2016). As a matter of fact, public debt is a vital instrument for governments to finance public expenses, especially when it is difficult to increase taxes and/or reduce the public expenditure (Gnegne & $2 Jawadi, 2013). However, a high public debt is also a critical problem for countries with weak economic system because it may generate economic instability into inter-related economies (Domar, 1944; Hall & $2 Taylor, 1993; Amaral & $2 Jacobson, 2011). In addition, high Public Debt-to-GDP ratio of countries is also considered a crucial issue for investors and policymakers, since it can negatively influence capital market and, in the long run, reduce productive investments (*e.g.*, R & $2D investments) , employment and economic growth (Coccia, 2013, 2005, 2007, 2008, 2009, 2010, 2010a; 2010b; 2012, 2012a, 2012b, 2012c, 2012d; Coccia & $2 Rolfo, 2007; Coccia, 2015, 2016; Calabrese et al., 2005).

The vast literature in public economics and political economy has analyzed several factors of public debts and of government deficits among European countries (Égert, 2015; Buiatti, Carmeci, & $2 Mauro, 2014; Elgin & $2 Uras, 2013; Coccia, 2010c, 2010d, 2014a, 2014b, 2014c; Coccia and Rolfo, 1999; Rolfo and Coccia, 2005). However, the precise evolution of public debts and of government deficits between countries *within* and *outside* the European monetary unification, *before* and *after* the introduction of the Euro currency, is hardly known. In light of the continuing importance of economic analyses concerning the evolution of public debts and government deficits in current economies, this study focuses specifically on following research questions:

- How is the dynamics of public debt across European countries, *before* and *after* the monetary unification?
- Have countries within European monetary unification an evolution of public debts and of government deficits similar or different to other countries?

The underlying problem of these research questions is to analyze and evaluate the economic consequences of the European monetary unification on debt, economic growth and employment into European countries. This study endeavours to explain whenever possible, this problem to shed some empirical light on recent trends and/or dissimilar dynamics of national debts and government deficits. Results can clarify the different evolution of public debts and deficits in European Union (E.U.) nations for supporting an appropriate political economy of growth directed to increase employment, economic growth and stability of overall European economic system over the long run.

2. Theoretical framework

Public debt encompasses all liabilities that are debt instruments owed by governments and public administrations, companies and other economic subjects (Barro, 1979). The deterioration of the debt in many Western countries in the aftermath of the economic recession, over 2007–2008 period, has brought the spot light on the long-term effect of high public debts and political economy of deficit reductions on the real economy (Coccia, 2013). In particular, high public debts and large government deficits are a common feature among countries in Europe, in the U.S.A. and also other countries (Tamegawa, 2016). Cornand, Gandré, and Gimet (2016) argue that some consequences of the recent sovereign debt market stress in the Eurozone have been the increase in the share of public debt held by the domestic sector in fragile economies with negative effects on productive investments (*e.g.,* R & $2D investments in strategic sectors; *cf*., Cavallo et al., 2014, 2014a, 2015; Coccia, 2008, 2010a, 2012, 2012a, 2012b, 2012c, 2012d). Equiza-Goñi (2016) finds that the high return on long-term debt has been the factor that contributed the most to changing (increasing) the debt ratios in the Eurozone compared to the US economy. Moreover, Equiza-Goñi (2016) indicates that higher (lower) inflation in Eurozone countries would lower (raise) their fiscal burden much more than in the US economy. The patterns of high debt influence the growth and employment of countries and have led in 2014 to the so-called Fiscal Compact in Europe and in 2011 to the U.S. Budget Control Act, which trigger automatic cuts in public spending in the absence of specified deficit reductions (Barseghyan & $2 Battaglini, 2016). In general, the main economic issue about international lending of countries is a sustainable commitment within international financial markets: it is necessary a commitment to repay the borrowers and a commitment to enforce repayment at the lenders in order to keep low interest rates on sovereign debt. The financial and economic crisis, over 2007–2008, increased the debt-to-GDP ratios of the Eurozone, raising serious problems about the sustainability of some countries' debts and the survival of the European Monetary Union as well (cf., Equiza-Goñi, 2016). Gogas, Plakandaras and Papadimitriou (2014, p. 1) argue that weak expansionary fiscal contractions by several European nations in the last decades have led to sovereign debt crises and some countries have faced the threat of default. Moreover, the European sovereign debt crisis, associated to other socioeconomic problems (*e.g.,* high employment, low economic growth, huge flows of migration from poor countries, etc.), is generating repercussions on economic and political integration of Europe (Kräussl, Lehnert, & $2 Stefanova, 2016; *cf.*, Paniagua at al., 2016; Melina, Yang, & $2 Zanna, 2016).

In general, European public debt ratio has increased from 67.4% in 2008 to 93.9% of Gross Domestic Product (GDP) in 2014 but

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