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The quiet, unexpected vindication of the euro

COMMENTARY | BY GEORGE PAGOULATOS *

Behind the horrors of war, amidst successive international crises, a favorable reality for Europe (and Greece) is quietly unfolding. What was once a factor of division and weakness for the European Union is now a pillar of unity and strength. The euro, at the heart of the EU's first major crisis of the 21st century, has evolved from a weak core to a European unifier. Faced with the worst combination of war, energy crisis and stagflation in at least five decades, the euro area is not only enduring but expanding.


ARMIN DURGUT/AP

A new euro coin depicting a map of Croatia is showcased at the Croatian central bank in Zagreb. Croatia adopted the euro and joined the Schengen zone on January 1.

It was not that long ago when serious analysts were competing in dismal predictions of Grexit and eurozone disintegration at the two peak phases of the Greek crisis (2010-12 and 2015). It was not only the Greek political drama that fueled these scenarios, but also the severe weaknesses of an imperfect monetary union, with no fiscal, banking or political integration to hold it together.

When the Greek crisis erupted, commentators and markets focused on the structural flaws of the eurozone: an imperfect currency area, suffering macroeconomic imbalances, in the absence of risk sharing, lacking a mechanism to recycle surpluses of exporting countries, those surpluses mirroring the external deficits of peripheral countries whose competitiveness declined under the euro. Cheap borrowing had created debt bubbles in the periphery, capital inflows had fueled over-indebtedness, inflating nontradables, real estate, consumption and imports.

Fast-forward a decade later: Greece is still in the euro, receiving the largest (in GDP percentage terms) inflows from the Recovery Fund; and those who bet on Grexit lost their money. As the crisis was unfolding, the eurozone was gaining three new (Baltic) members. And on January 1, the eurozone welcomed Croatia as its 20th member, with the rest of the EU (except Denmark and Sweden) maintaining the objective of joining the euro.

What happened? How were the Cassandras disproved? First, the countries under austerity bailout programs – the last of which was Greece – stabilized their economies, at a much heavier cost than they should have. Second, Mario Draghi's European Central Bank saved the euro, first by promising to do "whatever it takes" and then by doing what was needed, activating a far-reaching asset purchase program. Third, by keeping Greece in the euro, the EU demonstrated credibility and commitment to the integrity of the eurozone. Fourth, during the eurozone debt crisis, the EU adopted reforms (ESM, banking union) that, while not turning the euro into a full economic union, nevertheless filled some important gaps. Fifth, in the face of subsequent crises, the EU has shown flexibility and resilience. Brexit, Trump, Covid-19 and Putin acted as external threats, forging political unity and sharpening the EU's geopolitical reflexes. And the Recovery Fund makes up for the lack of fiscal stabilization capacity and a development finance tool.

Commentators are rediscovering the virtues of the euro. In international crises, without the euro, fluctuations would have been violent, economic cycles extreme, the turbulence devastating for middle and weaker incomes. In an environment of high inflation, the credibility of the euro allows its members lower borrowing rates – as Slovakia enjoys, compared to the Czech Republic, Poland or Hungary, which all have their own currency. The strong dollar squeezes countries with foreign debt denominated in US dollar – but euro members eschew the exchange rate risk because their debt is in euros. As Martin Sandbu wrote (Financial Times, 8/01), the advantages of having your own currency are highly illusory: A devaluation makes your imports more expensive and your population poorer, without making your exports cheaper and more competitive, as they depend on imported raw materials, energy and intermediate goods. This was, after all, one of the main arguments why Grexit would not have solved (but would have indeed exacerbated) Greece's economic predicament.

When the dust settles, the euro's greatest advantage is clear to see: It is a shield behind which small and medium-sized economies can shelter together from the storms of international financial interdependence, in a world of geopolitical competition in which the dollar remains dominant and Europe not-exactly-a-superpower. Who would abandon this safe haven to venture out into the storm alone? That is the main argument for the euro, and it's enough.

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