

Complete and incomplete monetary unions: a
comparison between US and the Eurozone
Abstract

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1 Introduction

The recent economic, political and social context in the European Monetary Union appears to be strongly jeopardized by the aftermath of the global financial crisis. The dramatic consequences that European countries have endured have made the structural flaws of the EU construction clearer than ever. As a result, the urgent necessity of paramount reforms has been considerably advocated not only by the most sceptical part of the literature (Pisani-Ferry, 2014, and Majone, 2014). Very often, for example by De Grauwe (2013 and 2016) and Juncker (2015), the incompleteness of the EMU has been blamed as the crucial source of European fragility and internal asymmetry. In fact, the inconsistency between the shared monetary policy and the national fiscal manoeuvres plays undoubtedly a leading role in explaining the great heterogeneity in competitiveness, account imbalances, interest rate and price systems, sovereign debt levels etc. Therefore, when the crisis struck, the EMU suffered from unprecedented asymmetric shocks and the resulting centrifugal forces put in serious danger the survival not only of the MU but of the European Union as well. A possible medicine may be the completion of the EMU by means of a fiscal union, as suggested by De Grauwe (2016).

2 Research questions

Throughout my thesis work, it is my intention to contribute to the existing literature by attempting to address the question as to whether a complete fiscal union would be beneficial for EMUs survival and prosperity. What are the different fruits of a complete and an incomplete MU?

More specifically, the project develops this analysis from a two-folded point of view: first, considering the short run, I compare the shock absorption ability of the two MUs observing stock values of some indicators in a specific time range. The examined interval coincides with the birth and evolution of the crisis.

Therefore, from a static perspective, I first endeavour to discover which MU presents a superior protection and counteraction against the surge of asymmetric shocks and the harm of the business cycle.

The second perspective of the thesis work is centered on a long-run analysis. My project studies the presence of persistent effects of some structural variables on regional GDP asymmetries. In other words, given the asymmetric shocks damage, I focus on how these two unions perform in curbing these asymmetries over time. Thus, the second perspective maintains the analytical enquiry trying to address it by a diverse technique.

What differences in regional trend rates of growth exist between US and EMU? Can long-run average regional inequalities be a further field of com-

parison? If so, and if a complete MU performs better in these terms, are the explaining structural factors related to the existence of a fiscal union?

3 Methodology

My methodology hinges on comparing the different performances of US and EMU in cushioning the asymmetric shocks consequences on the GDP, both from a short-run and a long-run perspective, from a national to a regional one.

Starting with the first part, the comparison focus is on the diverse reaction of the two monetary unions to the burst of the worldwide economic crisis. I carry this out by comparing relevant indicators for four risk-sharing mechanisms. As convincingly highlighted by Schelkle (2017), these mechanisms play a key role in each monetary union, since they permit to dampen its costs by sharing them. A fiscal union would add an important risk-sharing channel that is the issuing of centralised fiscal transfers. The assessed channels are the federal fiscal transfers and the national (or decentralised) ones, the interest rate management by the CBs (as suggested again by Schelkle, 2017) and the functioning of the financial markets as a private risk-sharing mechanism. This perspective is appreciably vast and it leads us to indicative evidence, useful for highlighting the advantages of a complete monetary union and therefore, for considering further integration.

In the second part, differently, I resort to a multivariate regression model. The technical procedure is the following: first, I compute the different regional inequality of US and EMU by considering the variance of a specific item, that is, the regional average growth rate during the recent crisis. Then, starting from the evidence obtained in this manner, I attempt to explain each of the two variances, building two respective multivariate regression models. I examine closer how statistically significant the proposed regressors are within both the MUs, detecting whether the values of those belonging to the incomplete EMU are particularly enlightening. On the other hand, I also examine how the regressors coefficients change when switching from a complete to an incomplete union. These models contain specific control variables for preventing other factors from undermining the values of the meaningful regressors coefficients: among these factors is the initial GDP regional stock level, a variable for human capital, one for the sector specialisation and, finally, one for R&D intensity. Differently, among the meaningful structural regressors, I employ a variable for productivity discrepancies, one for the employment protection and the last one for the balance of the current account; all these regressors relate somehow to the incompleteness of a MU. Heteroscedasticity of residuals is clearly taken into account and properly corrected.

The quantitative scope is to analyse how well the monetary unions work

in smoothing inner heterogeneity; hence, I employ regional items and study the macro-factors that affect their unequal performance. My hypothesis is that an incomplete monetary union suffers from issues that undermine regional equality with a certain persistence; then, in order to verify this hypothesis, I assess if a complete federal union shows better outcomes. This is supposed to be due to the presence of additional instruments and tools, such as a common federal budget and a coordinated fiscal policy, which can compensate wealth gaps among regions.

4 Conclusions

I bear a considerable interest about this field of research since I believe that the fate of current monetary unions, as well as the oncoming crucial decisions that the policy-makers will have to tackle, are deeply connected to the development of literature. I am firmly convinced that key discoveries over these topics could be highly beneficial for the prosperous management of monetary unions.