PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS

INSIDE THE EURO CRISIS

AN EYEWITNESS ACCOUNT

SIMEON DJANKOV

INSIDE THE EURO CRISIS

AN **EYEWITNESS** ACCOUNT

SIMEON DJANKOV

PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS
Washington, DC
June 2014

Simeon Djankov, visiting fellow at the Peterson Institute for International Economics, was deputy prime minister and minister of finance of Bulgaria from 2009 to 2013. In this capacity, he represented his country at the Ecofin meetings of finance ministers in Brussels. Prior to his cabinet appointment, Djankov was chief economist of the finance and private sector vice presidency of the World Bank. In his 14 years at the Bank, he worked on regional trade agreements in North Africa, enterprise restructuring and privatization in transition economies, corporate governance in East Asia, and regulatory reforms around the world. He is the founder of the World Bank's Doing Business project. He was also principal author of the *World Development Report 2002*.

Djankov is rector of the New Economic School in Russia and a visiting lecturer at Harvard University's Kennedy School of Government. He was associate editor of the *Journal of Comparative Economics* from 2004 to 2009 and chairman of the Board of the European Bank for Reconstruction and Development in 2012–13. He is also a member of the Knowledge and Advisory Council at the World Bank. He has published over 70 articles in professional journals. He obtained his doctorate in economics in 1997 from the University of Michigan at Ann Arbor.

PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS
1750 Massachusetts Avenue, NW
Washington, DC 20036-1903
(202) 328-9000   FAX: (202) 659-3225
www.piie.com

Adam S. Posen, *President*
Steven R. Weisman, *Vice President for Publications and Communications*

Cover Design by Sese-Paul Design
Cover photo by © Rao Aimin/Xinhua Press/Corbis
Printing by Versa Press, Inc.

Printed in the United States of America
16 15 14   5 4 3 2 1

Library of Congress Cataloging-in-Publication Data
Djankov, Simeon.
Inside the euro crisis / Simeon Djankov.
pages cm
ISBN 978-0-88132-685-7
1. Monetary policy—European Union countries. 2. Debts, Public—European Union countries. 3. Financial crises—European Union countries. 4. Banks and banking—European Union countries. I. Title.
HG230.3.D583 2014
330.94—dc23
2014009203

This publication has been subjected to a prepublication peer review intended to ensure analytical quality. The views expressed are those of the author. This publication is part of the overall program of the Peterson Institute for International Economics, as endorsed by its Board of Directors, but it does not necessarily reflect the views of individual members of the Board or of the Institute's staff or management. The Peterson Institute for International Economics is a private, nonprofit institution for the rigorous, open, and intellectually honest study and discussion of international economic policy. Its purpose is to identify and analyze important issues to making globalization beneficial and sustainable for the people of the United States and the world and then to develop and communicate practical new approaches for dealing with them. Its work is made possible by financial support from a highly diverse group of philanthropic foundations, private corporations, and interested individuals, as well as by income on its capital fund. For a list of Institute supporters, please see www.piie.com/supporters.cfm.

Contents

Table

Figures

Box

Preface

The problems inherent in the partial union of the euro area were foreseen by many experts over many years. But when its sovereign debt and financial crisis engulfed the region in 2010, the policy response was often chaotic, short-sighted, and hampered by political and ideological constraints. For now, the euro area has stabilized, and it may be setting out on a new path, thankfully. But as is made clear by this unusual and perceptive book by Simeon Djankov, an insider in the decision-making process, the costs of the crisis were higher than needed, and the euro area is far from out of danger. *Inside the Euro Crisis: An Eyewitness Account* offers some important suggestions for repairing the damage and minimizing the chances of crisis in the future. More than that, it tells a dramatic story of one individual economist's experience as part of the high-level decision-making process as the crisis unfolded.

Djankov, formerly a widely cited and senior economist at the World Bank, became finance minister and deputy prime minister of Bulgaria in July 2009, without previously knowing any politicians in his native country. Indeed, as he notes wryly, his only connection with the political world was through an ancestor who served as a legislator at the end of the 19th century. While at the World Bank, Djankov had spent no time dealing with the problems of the European Union as it made its historic transition toward a single currency in the previous dozen years. Yet, suddenly he was thrust into managing not only a financial crisis in Bulgaria but also an existential crisis for Europe itself, as he participated in dozens of monthly meetings and emergency communications of Ecofin, the powerful gathering of EU finance ministers.

As Djankov notes, the crisis revived old questions about the advisability of the unified currency zone—questions that had been raised in Europe a decade earlier. "Whether our countries were in the eurozone or not, all of us in Ecofin were forced to confront issues of how to save the eurozone, establish greater powers for the European Central Bank (ECB) to prevent bank runs, undertake structural reforms, and create a European fiscal union," he writes. Djankov also discusses his painful experience to try to reform some ailing sectors of the Bulgarian economy during this tumultuous period, notably his ultimately successful experience with pension reform in 2010–11.

Djankov takes the reader inside the process to describe what ideas were considered and how they got rejected or implemented as he and other economic officials struggled to deal with problems spreading through Greece, Ireland, Portugal, Spain, and Cyprus, and as unemployment soared throughout the region. He discusses how progress was made in some areas—for example, in steps toward establishing a banking union and making constitutional amendments in several eurozone countries to institute budget rules. In other areas—for example, the establishment of a fiscal union—little was achieved. The process by which these successes and failures came about has not been the subject of previous writings, as few scholars could lift the veil on Ecofin decision making and the strong personalities of those involved, and fewer EU insiders could write with such insight and analytical clarity.

The main contribution of this book thus lies in documenting what went on behind the European Union's closed doors, before investors and the public learned of the politically made decisions. It complements an already voluminous journalistic and academic literature on whether these decisions were the right ones and how they affected the resolution of the euro area crisis. One thing the author makes very clear: European economic decision making was too slow and inhibited by poor understanding of what was going on in the markets and throughout the region. Creating a more resilient euro area requires not only reining in fiscal imbalances in some euro area countries, Djankov argues, but also a different structure of the European institutions themselves.

We at the Peterson Institute are proud to have made important ongoing contributions to the policy debate on how to resolve the euro area debt crisis. In June 2009, Nicolas Véron and I published "A Solution for Europe's Banking Problem," a Policy Brief that set out a vision for unified bank supervision and regulation in Europe, one now coming to fruition in the asset quality review and the Single Supervisory Mechanism. From 2010 through early 2014, PIIE published two dozen Policy Briefs and Working Papers on the crisis as well as a conference volume on policy options in March 2012 (*Resolving the European Debt Crisis*, Special Report 21, ed. William R. Cline and Guntram Wolff). The Institute has been the leading US forum for serious discussion of euro issues. We hosted speeches and discussions on the issues by euro area finance ministers, central bank governors and board members, EU commissioners, two ECB presidents, and three heads of state. Several senior members of the Institute staff—notably Anders Åslund, C. Fred Bergsten, William Cline, Jacob Kirkegaard, Ángel Ubide, and Nicolas Véron—have provided widely followed commentary on the crisis as it has evolved. In tandem with this book, PIIE is publishing *Managing the Euro Area Debt Crisis*, a rigorously analytical account of the crisis and its decision making by William R. Cline, our long-standing expert on sovereign debt and financial crises over many years and regions.

The Peterson Institute for International Economics is a private, nonprofit institution for rigorous, intellectually open, and honest study and discussion of international economic policy. Its purpose is to identify and analyze important issues to making globalization beneficial and sustainable for the people of the United States and the world and then to develop and communicate practical new approaches for dealing with them. The Institute is completely nonpartisan.

The Institute's work is funded by a highly diverse group of philanthropic foundations, private corporations, and interested individuals, as well as income on its capital fund. About 35 percent of the Institute's resources in our latest fiscal year were provided by contributors from outside the United States. Interested readers may access the data underlying Institute books by searching titles at http://bookstore.piie.com.

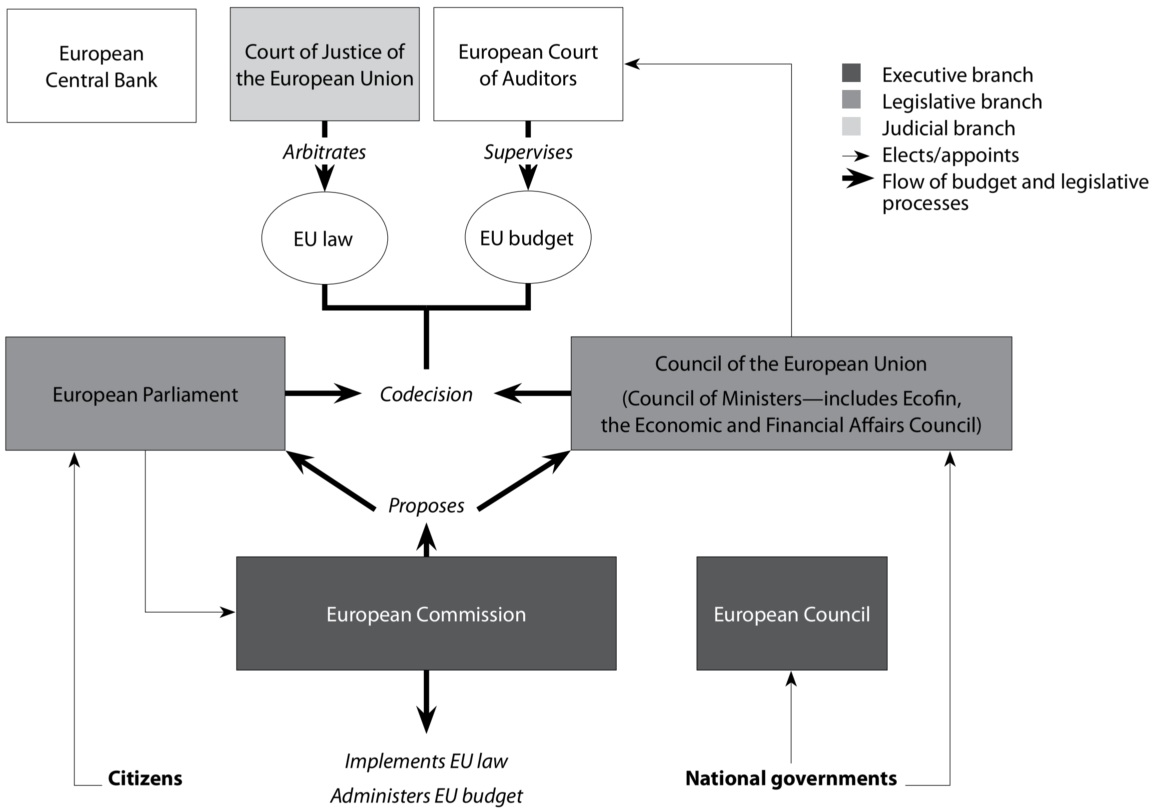
The Executive Committee of the Institute's Board of Directors bears overall responsibility for the Institute's direction, gives general guidance and approval to its research program, and evaluates its performance in pursuit of its mission. The Institute's President is responsible for the identification of topics that are likely to become important over the medium term (one to three years) that should be addressed by Institute scholars. This rolling agenda is set in close consultation with the Institute's research staff, Board of Directors, and other stakeholders.

The President makes the final decision to publish any individual Institute study, following independent internal and external review of the work.

The Institute hopes that its research and other activities will contribute to building a stronger foundation for international economic policy around the world. We invite readers of these publications to let us know how they think we can best accomplish this objective.

Adam S. Posen
President
May 2014

Overview of the European Union's Organizational Structure



1

Introduction

In July 2009, I became the finance minister and deputy prime minister of Bulgaria. I had left Bulgaria nearly 20 years earlier and had spent my entire adult life in the United States, first studying international economics and then joining the World Bank to work on corporate and bank restructuring, regulatory reform, and financial crises. I travelled widely while at the Bank and advised many governments, but had not worked in Bulgaria. As a result, I did not know any Bulgarian politicians. The only politician in my family was my great-great-great-grandfather, who was a member of four consecutive parliaments in the 1880s and 1890s.

Nor had I spent any time dealing with the problems of the European Union, which over the last dozen years had undertaken a transition to a single currency and the establishment of the European Central Bank (ECB). As I arrived at the finance ministry in Sofia, this unprecedented effort at European integration was facing an existential crisis that would require my full attention as a member of the Economic and Financial Affairs Council of the European Union (Ecofin), the monthly gathering of EU finance ministers. Bulgaria had become a member of the European Union in 2007, and so it was still a newcomer at the tables of various European gatherings. Meanwhile, the crisis emerging in Europe was raising doubts about the ability of Greece and other countries in southern Europe to survive continued membership in the eurozone. It also was reviving old questions about the advisability of the unified currency zone—questions that had been raised in Europe a decade earlier. Whether our countries were in the eurozone or not, all of us in Ecofin were forced to confront issues of how to save the eurozone, establish greater powers for the ECB to prevent bank runs, undertake structural reforms, and create a European fiscal union. My leadership position in the Bulgarian government thus bestowed on me an active role in the historic moment unfolding in Europe—a role I had not anticipated when I accepted the job.

This book is an eyewitness account of events in Europe from July 2009 to the spring of 2013. Specifically, it is an insider's view of how some decisions were made, or not, and what thinking lay behind them. In the narrative, I also draw on my own experience in reforming some sectors in Bulgaria—for example, the painful but ultimately successful experience with pension reform in 2010–11. Meanwhile, during my term as finance minister Bulgaria was actively pursuing the idea of entering the waiting room to the eurozone, the Exchange Rate Mechanism II (ERM II), and therefore I was quite engaged in the euro crisis as it affected Bulgaria's path to entry.

This book follows chronologically the events leading to the euro crisis and the various attempts at resolving the crisis until the spring of 2013, when my term as finance minister ended. Each chapter describes the important events that shaped the agenda in Ecofin and details the main policy responses whether implemented or not. In fact, many policy prescriptions during the euro crisis were never implemented, either because they were, upon further consideration, discarded as inadequate or because they were too bold and did not have enough political support. Their description here is, in my view, one of the main contributions of this book. It reveals how much energy was spent generating and refuting ideas on resolving the crisis and the small proportion of those ideas that ever turned into concrete actions.

A caveat—upon entering the Bulgarian government, I quickly learned that every day spent out of the country brought trouble at home. For this reason, I was forced to miss some important discussions with fellow finance ministers and European Commission experts. These discussions may have changed my mind on some of the topics discussed in this book. But this was the reality not just for me—one or another finance minister was absent for long stretches of Ecofin meetings. And one did not even have to wonder why: The international media would dutifully report rifts within the particular government or difficulties in upcoming elections. Domestic politics came first. Thus the view presented here is not objective. It shows the euro crisis through my eyes, and is limited by the great difficulties I faced in participating in euro crisis discussions while surviving Bulgarian's rough and tumble politics.

How the Crisis Unfolded: Seven Tipping Points

Before describing my own involvement in the unfolding of the euro crisis, I briefly describe in this section the chronology of the crisis itself by framing it in seven tipping points that determined how it progressed.

Tipping Point 1. The first came on October 23, 2009, when Greek prime minister Georgios Papandreou admitted that Greece had lied about its budget deficits and debt for over a decade, and that the country's public deficit would exceed 12 percent of GDP, or twice the level announced by the Greek government just a month earlier. Financial markets responded strongly to the admission of false statistics by demanding much higher rates on Greek bonds. Soon, the situation spread to three other countries with high government debt ratios and wobbly banking systems—Italy, Portugal, and Spain.

Tipping Point 2. This tipping point also came in October, but in 2010, when German chancellor Angela Merkel and French president Nicolas Sarkozy met in Deauville, France, and declared that the establishment of a permanent crisis management mechanism, to take over the temporary European Financial Stability Facility (EFSF) in 2013, was conditioned on amending the EU treaty to provide for the participation of private creditors. Introducing this idea publicly in the midst of a volatile market and without detailing how it would work was a mistake. Ecofin was blindsided—it did not have such a discussion in September. After Deauville, the crisis in Ireland spread outside the banking sector.

Tipping Point 3. A year later, on October 13, 2011, Slovakia became the 17th and final country to approve the expansion of the eurozone's rescue fund, two days after its parliament rejected the plan. Legislators in Bratislava ratified expansion of funding for the EFSF to €440 billion ($610 billion). Ratification came at a high cost, however—the conservative government of Iveta Radičová fell as a result, less than a year into its term. But the eurozone now had a powerful instrument for acting quickly in case trouble befell another one of its members.

Tipping Point 4. The same month, on October 31, 2011, in a move that caught people by surprise, Greek prime minister Papandreou, announced plans for a referendum on the new bailout plan. Even his finance minister, Evangelos Venizelos, was unaware of this plan in advance. The eurozone leaders were seething. All the work in past months to show European resolve in dealing with the Greek crisis was put in jeopardy. Public opinion in Greece was clearly against the proposed conditions of the bailout, and the referendum would probably result in a rejection of these terms. But where to go from there? A suspension of aid to Greece and a subsequent default and exit from the euro seemed the most likely route.

Tipping Point 5. The fifth and most positive tipping point arrived on July 26, 2012. By then, the crisis was getting out of control, and so ECB president Mario Draghi announced that the bank would do "whatever it takes" to keep the eurozone together. The markets were relieved, and yields in the troubled European countries fell sharply. Responding to Draghi's statement, investors became more comfortable buying bonds of the region's southern rim governments. This was the single key decision that saved the eurozone and changed the course of the crisis. Draghi's determination made everyone more confident that the remaining issues would be resolved with time.

Tipping Point 6. Another tipping point was the decision by Ecofin on December 14, 2012, to adhere to a single banking supervisor. Ecofin's decision was confirmed by the heads of state the following day. This decision wiped out any remaining questions about whether European politicians were united in strengthening the euro. The reform required governments to yield control over the supervision of national banks to the ECB in November 2014.

Tipping Point 7. The seventh and final tipping point came on March 25, 2013, when the Eurogroup, European Commission, ECB, and International Monetary Fund (IMF) agreed on a €10 billion ($14 billion) bailout for Cyprus. It safeguarded small savers, but inflicted heavy losses on uninsured depositors, including wealthy Russians. The European Union was moving toward putting more burdens on bondholders and fewer on taxpayers. That approach was directed as much at Cyprus as at Slovenia, Spain, and other countries that might fall into further difficulties. The remedy in Ireland was quite different—the taxpayers footed the whole bill.

My First Impressions from Ecofin

How did these events look from my seat in Ecofin? Before providing these impressions, I will fill in the backdrop. In addition to the euro crisis, my team at the finance ministry had to deal with several other international issues. Relations with Russia on various energy projects occupied the top spot. In the course of my term in government, we cancelled a deal to build a second nuclear power station with Russian technology and terminated a project to build an oil pipeline transporting Russian oil to the Greek coast of the Adriatic. The second issue was one of continuous worry about the Bulgarian subsidiaries of several Greek banks. Analysts and investors feared that these subsidiaries would bring down the Bulgarian banking system, and we spent a lot of time arguing otherwise. Third was the euro crisis. I rank these issues to make the point that the euro crisis was not my foremost concern while in government, but it had an effect on most other decisions.

Ten days after my inauguration in July 2009, I went to my first Ecofin meeting in Brussels. Two things made an immediate impression. First, few of my colleagues had a formal education in economics or finance—5 of the other 26 finance ministers to be exact. Second, there was little urgency. We had to work around the expansive holiday schedules in Europe, and so my second Ecofin was in late September. By then, the Greek government had become mired in corruption scandals, and a week later, on October 4, 2009, Prime Minister Konstantinos Karamanlis resigned halfway through his second term.

During the next four years, Ecofin met over 40 times, and so I had plenty of opportunities to consider the main topic of the moment: the euro crisis. There was a constant focus on keeping Greece afloat and building a common fiscal policy to save the eurozone. In late 2011, the idea of a banking union surfaced and gathered speed the following autumn. The remaining agenda varied: saving Hungary, saving Ireland, saving Portugal, punishing Hungary, becoming worried about Spain, becoming worried about Italy, wondering when France would face up to its banking problems. By the time Cyprus blew up, we had been in the saving business for too long, and this is why Cyprus got the short stick.

There were moments of joy such as Estonia adopting the euro in January 2011. "A political decision," the Estonians would say. "We want to be as far from Russia as possible." During my last Ecofin, Latvia applied as well and was given the go-ahead to join the eurozone in January 2014. Latvia fully deserved it. It had suffered an 18 percent drop in output, accompanied by a rise in unemployment in 2009 and further fiscal tightening in 2010 and 2011, to maintain its version of a currency board.

There was success at home as well. After recording a 4.4 percent budget deficit in 2009 because of the previous government's preelection spending spree, Bulgaria reduced its deficit to 2 percent in 2011 and 0.5 percent in 2012 and exited the excess deficit procedure at the same time as Germany. That put Bulgaria in the small group of fiscally responsible countries. Moody's raised Bulgaria's credit rating to BB+, the only rating increase in Europe between 2009 and 2012, before Estonia and then Latvia received upgrades. The ECB's *Convergence Report* in 2012 noted that Bulgaria met all the quantitative Maastricht criteria, one of only three EU countries to do so. The remaining step was entry into ERM II. But I decided that this step had to wait until it was clear what the evolving eurozone rules and institutions would be. Over time, Bulgarians' views on the euro darkened, as elsewhere in Europe, and fewer and fewer of them thought we should adopt the euro. But today I think we should, now that the worst of the euro crisis is over.

The most memorable moment of my work in Brussels was in mid-December 2012, when Ecofin agreed to move toward a single banking supervision authority for the European Union. This was the third meeting called in a span of 10 days; the previous one had been cancelled because the positions were too far apart, and the first meeting, in November, had ended in an impasse. As one minister later remarked, "It was the most relaxed Ecofin meeting ever. The differences in opinion were so large, that there was no point arguing." Indeed, the third time was a charm—perhaps because of the coming Christmas holidays and because the meeting of heads of state was scheduled for the next day. The functioning of the single supervisor was hotly debated and then agreed on. By that time, it was early morning, and the heads of state were flying in.

But in April 2013, there was a change of view. The German finance minister, Wolfgang Schäuble, and the head of the Bundesbank, Jens Weidmann, suggested that the single banking supervisor agreement was illegal under the Lisbon Treaty and thus necessitated a treaty change. Perhaps upcoming elections for the Bundestag had something to do with their concerns—and their fears that regional German banks, the Landesbanken, would be harshly supervised. In truth, Schäuble had made this point several times during Ecofin discussions. But he had not made it so forcefully and certainly not during the December 2012 meeting at which the agreement was reached. Schäuble was a thoughtful person and took advice from his staff well. I had on several occasions—including visits to Berlin—witnessed his willingness to alter his views in light of additional analysis. So it is possible that his legal advisors had convinced him of the impossibility of rapid progress on the banking union.

This was, moreover, typical of decision making in Europe during the crisis. An issue would be discussed intensely for a while, but then it would be dropped suddenly for a newer idea. The issue would have arisen from a bilateral meeting between France and Germany ahead of Ecofin gatherings. The newer idea would suffer the same fate a few months later. In a span of three years, the euro-strengthening exercise went through six variations—the Euro Pact, the Euro Plus Pact, the Fiscal Compact, the financial transactions tax, the fiscal union, and the banking union. With the exception of one idea—the Fiscal Compact, which translated the Maastricht criteria into national legislation—all others had small immediate value added. The banking union would take a decade to be properly implemented. Its first feature—the single banking supervisor—was postponed until October 2014 after it had been initially agreed to start in March 2013. And the discussions on a common guarantee fund and restructuring facility started only in July 2013, after I had left the Bulgarian government.

Another feature was the constant repositioning because of upcoming elections. "We can't deal with troubled Greek banks before the French elections [in May 2012]," European Commission bureaucrats would say. Indeed, French banks had a lot to lose if the IMF and the ECB insisted that private creditors share the burden of writeoffs. The result was significant foot-dragging, to the detriment of the restructuring program in Greece. Another example was the parliamentary elections in Finland and the Netherlands, when the Ecofin discussion on bailouts became more extreme in favor of kicking Greece out of the eurozone to suit the ruling parties in their final weeks of campaigning. And yet another example was Cyprus, where the problems with troubled banks had been known and discussed at Ecofin in early 2012. But the European Commission waited until after the presidential elections in Cyprus in February 2013 to agree with the new president, Nicos Anastasiades, on the bailout package. It was too late, however, and the additional loss of value in the banking sector was in the billions, leaving the Cypriot government with a bigger hole to fill.

Throughout my experience in Ecofin, I was constantly reminded of what Daniel Ellsberg wrote about the indecisive approach taken by the Johnson and Nixon administrations to the Vietnam War: "At every juncture [policymakers] made the minimum commitments necessary to avoid imminent disaster—offering optimistic rhetoric, but never taking the steps that even they believed could offer the prospect of decisive victory. They were tragically caught in a kind of no-man's-land—unable to reverse a course to which they had committed so much, but also unable to generate the political will to take forward steps that gave any realistic prospect of success" (Ellsberg 1972, 7). This was how Ecofin felt to me for a long time. For that reason, I hesitated about going to every meeting—there was so much work at home that each day away was costly. In the end, though, I participated in most of the Ecofin meetings because they were the main opportunity I had to learn how other countries were dealing with the crisis. Before each Ecofin meeting, I spoke to Jürgen Ligi, the Estonian finance minister, to Anders Borg, the Swedish finance minister, and to Jyrki Katainen, the Finnish finance minister for most of my term. I had chosen these countries as a comparator group both for their known fiscal discipline and economic success and for their similar country size.

At some point in 2011, the eurozone members became agitated over the remarks of some noneurozone ministers, among them UK chancellor of the exchequer George Osborne and Swedish finance minister Borg, who expressed their views on the slow pace of decisions and on the missing growth plan for Europe. Thus eurozone members' discussions of bailouts moved to the eurozone dinner held the evening before the Ecofin meeting—eurozone members only. At the initiative of Borg and Margrethe Vestager, the finance minister of Denmark, we began to hold a noneurozone dinner to discuss how the European Union could advance beyond the current crisis. (These were among the few gatherings I attended in which the growth prospects for the European Union were considered. It helped that noneurozone countries were in better fiscal and economic shape than the eurozone ones—and that there were not any immediate bailout issues to discuss.)

The Ecofin meeting the next day started with an extensive summary of the eurozone group dinner and again discussions on the various bailout programs. Take pity on the finance ministers of the bailout countries—they had to sit through this grilling twice! And a grilling it was. First, Dutch finance minister Jan Kees de Jager questioned the commitment to belt-tightening and structural reforms in Greece, and later Portugal and Spain. Then Finnish finance minister Katainen, later Finland's prime minister, took the floor with similar remarks, followed by Austrian finance minister Josef Proell (and after the fall of 2011 his successor, Maria Fekter). On their heels was Anders Borg. When one of the southern rim ministers took the floor and explained that in the north things might work differently, I took the floor and listed what Bulgaria had achieved in a short period of time and then what Estonia and Latvia had accomplished in a much more trying situation. That did not win me any favors from the southern rim ministers.

During my term in office, parties belonging to the European People's Party (EPP) Group, made up of center-right parties across Europe, governed 20 of the 27 EU countries. The ministers from these governments met at breakfast the day of Ecofin, often together with the EU commissioners belonging to the EPP parties (Michel Barnier, Algirdas Šemeta, and Janusz Lewandowski). The commissioners informed us of their work, and we updated each other on how the crisis was developing in our countries. At these breakfasts, I would listen to German finance minister Schäuble, Luxembourg's prime minister, Jean-Claude Juncker, and Anders Borg and think Europe was in safe hands. The EPP Group breakfasts had one prominent feature: Common positions would be discussed on the main issues of the day. Although it was never explicit, the breakfasts helped those of us attending prepare the tactics for the subsequent discussions at Ecofin. Because the majority of noneurozone members had center-right governments, Austria, Finland, Germany, and the Netherlands could find significant support for their tougher stance on Greece and other bailout countries—and on the general view that Europe needed more fiscal responsibility.

As the crisis continued, center-left governments tended to be replaced by center-right governments, with their greater expertise and understanding of the demands of markets, deficits, and budgets. At first, none of the ministers from bailout countries were from EPP Group parties; rather, all were from the Party of European Socialists. But by 2013, they were all EPP—the elections had brought in center-right governments. The quality of the debate then shot up because the new ministers had finance backgrounds, unlike their predecessors. Vítor Gaspar, the Portuguese minister, Yannis Stournaras, the Greek minister, and Spaniard Luis de Guindos all had impressive resumés and were straight talkers. This was thankfully a feature of crises: competence in finding solutions was urgently needed, and able professionals had come to the fore.

One could argue that I was as unqualified as many of the other finance ministers because of my lack of experience in Western Europe. After all, the onset of the euro crisis caught up with me while I was serving as chief economist of the finance and private sector vice presidency of the World Bank Group. The crisis took us as much by surprise as anyone else. The problems in the summer of 2008 with subprime mortgages and the subsequent drying up of trade credit globally seemed like isolated problems, far from the eurozone. When Iceland's banking sector collapsed in October, however, it suddenly became a euro problem as well because some continental European investors had much to lose. And they did lose. I had done some work in the Netherlands and Sweden, but it was all related to cutting the red tape for business. The World Bank had not worked in other reform areas in West European countries for 20 years.

My boss at the time, Michael Klein, vice president for finance and private sector at the World Bank, had a great deal of experience in crisis management. From his work at Shell, he had learned that crises quickly become unpredictable. We put together a crisis group from across the World Bank—finance experts, trade economists, small business developers, political scientists—that developed the four scenarios that might unfold (Djankov et al. 2009). The most likely scenario? It was that Greece would collapse and split the eurozone into northern and southern blocs, with the north maintaining a common currency. The south would be pulled in different directions, some countries toward Russia and some toward Turkey and the Middle East. In the fall of 2008, this analysis seemed like science fiction, capturing extreme possibilities. But the work on the scenarios did uncover a fundamental weakness in Europe—the stability of the euro.

The Euro and Its Weaknesses

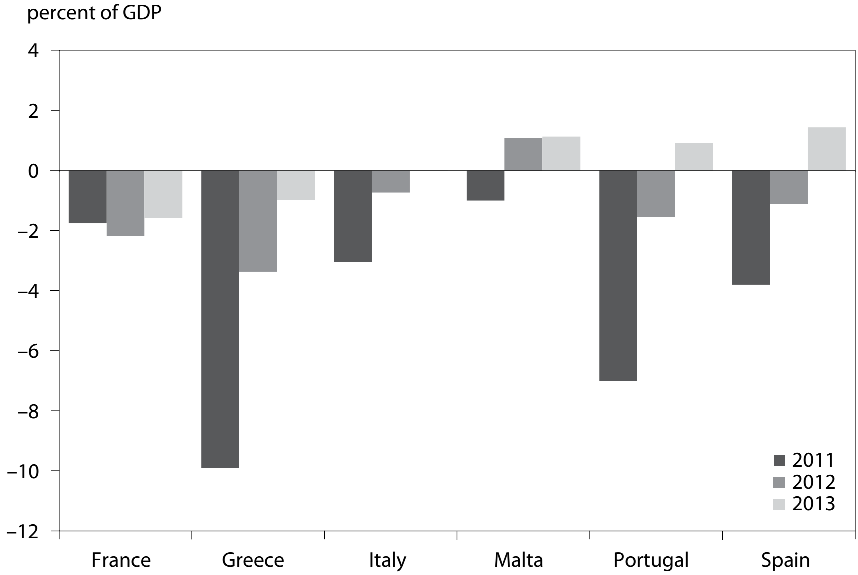
In its conception, the euro has a flaw: It locks in countries on the periphery of Europe in an exchange rate they can ill afford to maintain unless they undertake structural reforms. Put simply, right at the start when Germany and Portugal adopted a single currency, it was obvious that Portugal would not be able to compete in the fixed exchange rate regime unless it reformed its labor market and business regulations. Because its currency would be overvalued, Portugal could not export the goods and services it produced at prices that were competitive on the global market. But in fact it was Germany that adjusted some of its labor regulations and pension rules under Chancellor Gerhard Schröder, while Portugal waited until well into the crisis to do so. And yet even Germany did not make it easy for businesses to start operations or to build investor protections, according to the 2013 *Doing Business* report of the World Bank (2013).

The same applied to France, Greece, Malta, and Spain—the whole southern rim of the eurozone. They were unwilling to adjust their labor markets, and their export-oriented sectors suffered as a result. The external trade data say it all. In 2012 France ran a current account deficit of €82 billion ($114 billion), Greece €20 billion ($28 billion), Portugal €11 billion ($15 billion), and Spain €32 billion ($44 billion). However, depressed consumption and higher taxes reduced the trade deficits in 2013. In May 2013, Spain had its first quarterly current account surplus in 50 years (figure 1.1). This was to a large extent due to a surplus in services, thanks to the tourism sector.

Some supporters of the euro say the original design needs strengthening with a common fiscal policy, a single banking supervisor, and a vetting mechanism for national budgets whereby structural reforms are undertaken to increase competitiveness. For example, if the southern rim countries had undertaken the labor reforms made by Germany under Gerhard Schröder, they would be in much better shape. Youth unemployment, in particular, would be lower. So the main culprit was the regulatory burden on business. And the supporters are right, to a degree. According to World Bank data, it takes 11 procedures and €9,000 ($12,500) to open a small business in Athens. It takes 735 days and 43 procedures to resolve a simple commercial dispute in Larnaca, Cyprus. And it takes 59 days and visits to eight different offices to register a small piece of property in Paris. It is cheaper and faster to do all this in Berlin. But operating in a fixed exchange rate regime probably trumps these concerns as a constraint. Good economists such as Vítor Gaspar, the Portuguese minister, and Yannis Stournaras, his Greek colleague, agreed.

The most ardent supporters of the euro say it is simply experiencing growing pains, and that it is a political project that cannot be judged in terms of optimal currency areas and the like. As the former president of the European Commission Jacques Delors remarked, "Obsession about budgetary constraints means that the people forget too often about the political objectives of European construction. The argument in favor of the single currency

Figure 1.1 Current account balances in the eurozone's southern rim, 2011–13



Source: IMF, *World Economic Outlook*, October 2013, www.imf.org/external/pubs/ft/weo/2013/02/weodata/index.aspx (accessed on February 27, 2014).

should be based on the desire to live together in peace" (Eichengreen 2010, 56). The euro gives Europe's citizens a symbol of their European identity. For this reason, no country could exit the eurozone. This is the view that was often stated to me by both Jean-Claude Juncker, Luxembourg's prime minister and until January 2013 head of the eurozone, and Schäuble, the German finance minister. I gradually came to see it that way as well, although at the beginning of my career as finance minister I was far from this view.

This group of so-called integrationists was quite large both in Ecofin and among the longer-serving heads of state. It included Mario Monti, Italy's technocratic prime minister, and Herman Van Rompuy, the president of the European Council. They firmly believed that any step that brought European countries closer together was a good one. I also shared this view. Bulgaria had greatly benefited from becoming part of the European Union in terms of both its national psyche and the influx of cohesion funds. But once the topic of fiscal union, and the accompanying tax harmonization, came up in late 2011, I adjusted my views. Most integration was good. Some was bad. European countries differed in their economic development, and it would be a mistake to impose the same tax structure on all of them.

On the euro, I continue to subscribe to the optimistic view that the euro should remain a strong currency with some significant reforms both at home and in Brussels. Some of these reforms were in the making during the crisis years—the common fiscal policy and the banking union. And both were in the beginning stages when I left the Bulgarian government in March 2013. Their completion would be a decade-long process, and perhaps even longer for the fiscal union. I think this is the right pace—no reason to rush into ill-conceived adventures. The entry of the East European countries in the eurozone, Bulgaria included, will strengthen the eurozone further. Whatever misgivings economists had at the start of the euro project because of obvious optimal currency area reasons are irrelevant now. The euro is good for Europe, and dismantling it would be a cure worse than the illness. I also support the completion of the banking union in the eurozone: On balance, it also benefits Europe.

One euro-related task remained unresolved in all my Ecofin work. How could Brussels entice governments to undertake the structural reforms needed to maintain the euro? It had failed to come up with the recipe. A new idea that emerged in 2011 was to link structural reforms to the allotments of structural funds: Whoever did not reform would not get money from the European Union's structural funds after 2013. This sounded fine in theory and was even attempted once—on Hungary in 2011. But that attempt failed, and subsequent attempts are likely to fail, too. Imagine Brussels telling France that it would be withholding funds for its farmers until the French government implemented labor reforms. Manuel Barroso, president of the European Commission, would be subjected to vociferous criticism by the French government and the French media.

In fact, President Barroso does not take criticism well, and perhaps that is why he was largely absent during the resolution of the euro crisis. For this reason, he is also absent from this book. He simply was not around when the important issues were being discussed. And not once did he attend Ecofin. I often wondered why. It was equivalent to my prime minister, Boyko Borisov, not participating in discussions on the budget situation in Bulgaria, or on how to resolve the difficulties we experienced in dealing with the revenue shortfall early in our government. Prime Minister Borisov, to his credit, participated in all of these discussions, often staying late at night or over the weekend. I would have expected the president of the European Commission to do the same when the future of the eurozone was at stake.

When in 2011 the European Commission decided to pick on Hungary for being consistently derelict in following the Stability and Growth Pact rules, the Hungarian finance minister, Gyorgy Matolcsy, came to me for advice. Later elected to head up the Hungarian Central Bank, he was new to his post as finance minister and came into office just as Hungary was being singled out as the country to penalize. It was no matter that there were many countries to choose from in the penalty giving, France and Italy included. "Delay," I advised. "Another crisis will come and you will be forgotten." I even helped in Ecofin by insisting in the spring of 2011 that the European Commission produce an extensive analysis of how various EU members had performed in following the rules. Sure enough, the Commission experts took several months to produce the analysis, and by then Italy was getting into trouble and Hungary was quickly forgotten. I soon received a case of Tokaji wine from Hungary's ambassador in Sofia.

Lessons from the Euro Crisis

Perhaps the most important lesson I learned while participating in Ecofin meetings was that the EU institutions were not equipped to make decisions on how to tackle the eurozone crisis, and instead they spent considerable time in delaying tactics, hoping that the problem would resolve itself. When this did not happen, there was a further delay, finger-pointing at various culprits for the crisis—US bankers, credit rating agencies, politicians in southern Europe. It took three years—to the fall of 2011—to get to work.

The second lesson I learned was that a united Europe did not mean a Europe of equals. Germany led all discussions on eurozone issues, sometimes showing token respect for France's views. Germany's main allies—Finland and the Netherlands—played important but secondary roles. No one else mattered much, or at least mattered consistently. This attitude was on view, for example, during adoption of the European Stability Mechanism, the vehicle through which eurozone countries could receive bailout assistance. The process was amateurish and led, as noted, to the fall of the Slovak government. Foreseeing the dangers in the Slovak Parliament, European leaders should have given much more support to Prime Minister Radičová, much like the support that was extended to Finnish finance minister Jyrki Katainen during his election campaign. At the time, Ecofin ministers and heads of state were working hard to find ways to alleviate concerns in Finland over the Greek and other bailouts. Another example was the collapse of Cyprus. It was avoidable. That mishap was due in part to the change at the helm of the eurozone—Jean-Claude Juncker, the previous head of the eurozone, would have handled it smoothly. But what also underlay this disaster was the anger of many European politicians at Greece—and they found a victim in Cyprus. Some eurozone members wanted the Cyprus resolution to be noisy and calamitous to appease their audiences at home.

Today, I am a firm believer in the bright future of the European Union and the eurozone; it is in the interest of the world. Otherwise, Europe starts looking inward and neglects its responsibilities on global issues. But, based on my experience and lessons learned, four things must happen for a strong euro:

1. All eurozone countries have to abide by the fiscal rules. Fiscal profligacy is contagious, and if one country drags its feet, others follow. This is especially true of the larger eurozone countries such as France, which was often negligent in adhering to the Maastricht rules. Historically, however, Germany was the first country to flout the Maastricht rules. Lack of fiscal discipline is what landed many eurozone countries in this protracted crisis.

2. Structural reforms are needed in public administration and in pensions and labor markets. The euro crisis helped with these, but the European Commission's analysis and recommendations remain weak.
3. European governments need to cut the red tape for business. European Council president Van Rompuy made attempts to address this issue in 2011, but otherwise Brussels has remained uninterested in the long-term growth prospects of the European Union. This requires change.
4. Most important, the path for adopting the euro must be part of entry into European Union, not an afterthought. On this point, I had discussions with the integrationists in Ecofin, and by early 2013 the idea was receiving support. Latvia's entry into the eurozone in January 2014 provided further momentum. I admit that the United Kingdom's euro future is beyond my comprehension.

And yet I believe Europe is not ready yet for a fiscal union in which government expenditures are decided in Brussels. This will take time to develop for three reasons. First, no national parliament is ready to hand decision making on budgetary issues to the European Commission. Second, such a move would endanger democracy in the budgetary process by significantly removing the decision making from those who elected the government on whether to pursue certain economic and social policies. And, third, in my work with the European Commission I could compare the quality of bureaucrats in Brussels and in Sofia. The Bulgarian bureaucracy, at least the one dealing with fiscal and tax issues, was significantly better prepared in its specific expertise as well as in its general administrative quality. Until Brussels has fiscal experts at least as well prepared as Bulgaria's, I would not support giving more powers to EU authorities.

The last point is important because it raises questions about how far the European project can advance in its integration. If I were asked to summarize the main conclusion from my years of work on the euro crisis, I would begin by pointing to the difficulty of providing an adequate answer to the question of how Portugal and Germany can compete globally in a single currency. Yes, in the United States Alabama and Massachusetts compete, each using the dollar. But there is a big difference: Unlike in Europe, there is capital and labor mobility in the United States as well as significant federal transfers. Twenty-nine percent of Americans live and work outside the state in which they were born. Only 3 percent of Europeans live in another EU country. Although officially there are few constraints to such mobility in Europe, languages play a big role, as do the inability of Europeans to transfer pension and health care benefits from one country to another and the policies of nationalist parties in countries such as the Netherlands.

In the absence of such mobility, the Europe Union came up with a mechanism of transfers as a way of inducing people to stay put. Each year, in addition to structural funds, the poorer members of the European Union receive cohesion funds, which together are equivalent to about 6 percent of their GDP.

The idea is to create conditions for better life and work in each country so that people do not have to move. So far so good, except that these funds are sometimes wasted: They are viewed as "free" and spent on glossy promotions of luxury resorts such as in Cyprus. Or, worse yet, they fall into the pockets of government officials, as was recorded in Bulgaria, Greece, Italy, Poland, and Romania. Funds were then stopped and the national budgets repaid. These countries ended up worse off.

Bulgaria's cohesion funds stopped flowing in 2008, just a year after it entered the European Union and saw the funds tap open. Much of the money was supposed to go toward road construction. Money was spent, but no new roads were built by the then-Socialist government. It turned out that the head of the road construction agency had contracted with his brother's company (he really did!) to build the roads. The case was referred to the Bulgarian courts, which after three years exonerated both brothers. The same case was also tried in German courts because some German advisors had participated in the embezzlement schemes. They were sentenced to three years in prison. Meanwhile, the Germans were fuming at the inability of the Bulgarian judiciary to defend the EU funds.

From that episode came this joke. A Bulgarian EU funds bureaucrat visited his Romanian colleague. He was surprised to see his big new house and Audi in the driveway. "How can you afford these?" he asked. The Romanian bureaucrat led him to a nearby road. "See this highway?" he asked. "No, I just see a two-lane road," said the Bulgarian. "Well, this is how I can afford a nice house and car," his colleague responded. A year later, the Romanian visited Bulgaria and was stunned to see his friend's mansion and Maserati. "How can you afford these?" he asked. The Bulgarian bureaucrat brought him to a field. "See this highway?" he asked. "No, I don't see anything," said the Romanian. "This is how," the Bulgarian responded proudly. Unfortunately, this is not a thing of the past. In November 2013, Bulgaria saw its flow of funds for environmental development stop.

Even in the absence of corruption, however, transfers are small relative to the issues they are supposed to address. A comparison with the United States is useful. In 2008 during Hurricane Katrina, the federal government made transfers to Louisiana in the form of direct assistance, Social Security, and Medicaid benefits that totaled nearly 30 percent of the state's GDP. This amount is three times higher than the average EU transfer to poorer countries in Europe. And it does not include bank programs organized by the US Federal Reserve System to create cheap credit for reconstruction in the affected areas.

And yet I do not believe that larger transfers are needed for European integration. What is most needed is a long-term view of European competitiveness, combined with instruments for strict fiscal discipline. When reading an earlier draft of this book, well-known economist John Williamson remarked that on the issue of fiscal discipline I was too pessimistic in my views. Brussels could take over from parliaments the powers of designing national budgets for those countries that had breached the Maastricht criteria. Otherwise, the national parliaments would remain in charge. This seems like a reasonable compromise, and I am ready to subscribe to it. But this is not how it was presented by Commissioner Olli Rehn in various Ecofin meetings. So, understandably, he got a lot of pushback.

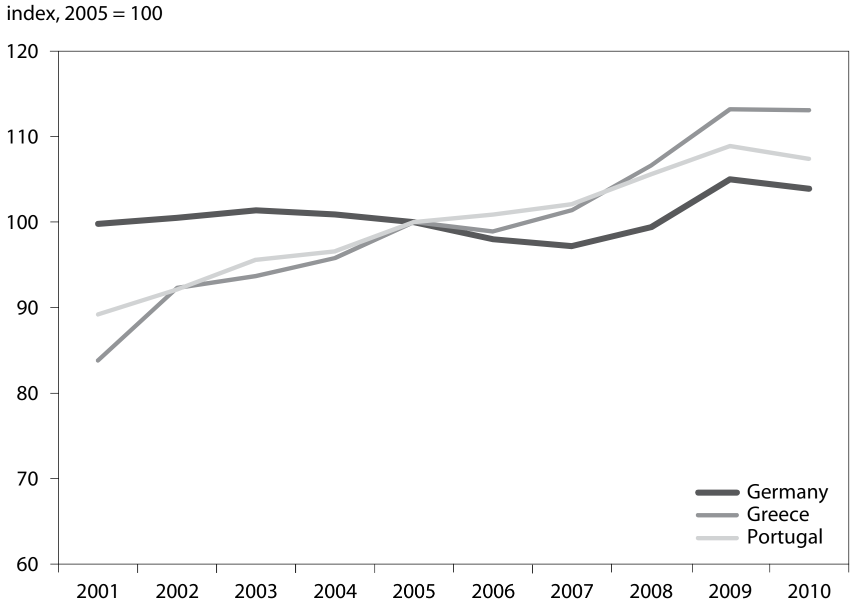
Tax harmonization in the European Union is as unnecessary as a larger transfer system. In the minds of French, Spanish, and Italian authorities, fiscal centralization comes in a bundle with tax harmonization—at least this is what French finance ministers Christine Lagarde and then Pierre Moscovici, Italian finance ministers Giulio Tremonti and then Mario Monti, and Spanish finance ministers Elena Salgado and then Luis de Guindos argued when the topic came up. The German position varied over time, with German finance minister Schäuble sympathetic to the tax harmonization view. My view is the opposite: Tax harmonization is harmful to the convergence of the poorer members of the European Union.

About the Book

This book comes in an expanding field. Thomas Mayer, a former IMF economist and Deutsche Bank manager, has studied the euro crisis from a historical perspective (Mayer 2012). What is his main point? The euro was "an ambitious political project pursued in reckless negligence of economics." He also suggests that the fall of the Berlin Wall distracted Germany, and so the euro came into being despite Germany's doubts. Another book, by Johan van Overtveldt, editor of the Belgian weekly *Trends*, argues that Greece and Portugal were too sneaky to be trusted, and that the political goal of their "crises" was to put an end to the euro and Germany's membership in the European Union (van Overtveldt 2011). McKinsey & Co.'s *The Future of the Euro* (2012), a study frequently cited by both Mario Draghi and Chancellor Angela Merkel, compares the increases in unit labor costs across the eurozone. It found that while German labor costs barely budged during 2001–10, they increased by 25 percent in Greece, and 28 percent in Portugal (figure 1.2). It is no wonder, then, that these countries experienced a loss in competitiveness. McKinsey & Co. also calculates the annual benefits of the euro to be €330 billion ($460 billion), of which about half goes to Germany.

Alberto Alesina, an economics professor at Harvard, was the only academic economist invited by Ecofin to present his views on the euro crisis during my term as finance minister. Perhaps it was because he wrote about Europe's euro troubles before other authors did and painted a rather compelling picture. With his colleague Francesco Giavazzi from Bocconi University, he argued in *The Future of Europe: Reform or Decline* (2006) that a major European decline was coming. Europe emerged from World War II with a per capita income level of less than half (42 percent) that of the United States. But it gradually caught up, to about 80 percent of US GDP per capita in the 1980s. After that, the catching up reversed, and by 2005 the European Union was at less than 70 percent of US GDP because of the lack of structural reforms and the general complacency of Europeans that the dolce vita would continue forever.

Figure 1.2 Nominal unit labor costs in Germany, Greece, and Portugal, 2001–10



Source: Eurostat, http://epp.eurostat.ec.europa.eu/portal/page/portal/statistics/search_database (accessed on February 27, 2014).

In their follow-up book, *Europe and the Euro* (2010), professors Alesina and Giavazzi compiled a collection of essays on the reasons for the euro crisis. They focused on the question of whether euro entry was good for structural reforms and found that belonging to the eurozone accelerated the reform process in the product market—particularly in the transportation and telecommunication sectors—but had no effect on the labor market. The logic was that countries became unable to use their monetary policy to accommodate negative shocks. This created incentives to liberalize product markets in order to rely more heavily on market-based adjustments. Also, the euro increased price transparency and therefore facilitated trade. A larger European market increased competition and made it more difficult for domestic monopolists to protect their rents. Labor reforms, on the other hand, were blocked by all-European labor unions.

An important feature of this book is that it tells the story of my involvement in policy reforms in Bulgaria prior to the main story of wrestling with the euro crisis. I chose to tell this story because the euro crisis significantly affected my work as finance minister in a noneurozone country, just as it affected the work of my fellow ministers from other noneurozone countries. And although the focus of scholars of the eurozone will no doubt be the political decisions that took place in Frankfurt, Brussels, Athens, Dublin, and Lisbon, all of us in the European Union were victims of the same crisis and faced similar problems. Moreover, noneurozone policymakers had an important voice in many decisions about the future of the eurozone—for example, in the set-up of the fiscal and banking unions. If scholars want to know how decisions on the eurozone were made, they can benefit from knowledge of how noneurozone countries acted during this difficult period.

This book is organized chronologically, highlighting the main events in the unfolding of the euro crisis. A list of these events also appears in the chronology at the end of the book, along with a glossary that describes many of the institutions and terms used. Chapter 2 focuses on my work in Bulgaria, including some of the reforms undertaken to keep the public finances in order and not succumb to large deficit spending as did most of our neighbors in Europe. Chapter 3 describes the onset of the euro crisis with Icelandic banking troubles, and the origins of the euro, both in Robert Mundell's economic theory and in practice. Chapter 4 details past attempts to form a fiscal union in Europe, and also analyzes the beginning of banking troubles in Ireland. Chapter 5 documents the first Greek bailout, and describes the first tipping point in the euro crisis, Prime Minister Papandreou's admission that Greece had consistently manipulated national statistics to meet the Maastricht criteria. It also reflects on the pros and cons of a proposed solution to the euro—letting troubled countries take euro holidays. Chapter 6 covers the second tipping point in the euro crisis: the Sarkozy-Merkel introduction of "private sector participation" in bailout packages. Doing so publicly in the midst of a volatile market and without detailing how it would work was a mistake. It rattled investors and undermined confidence in the ability of European institutions to undertake crisis management. The chapter also presents the theoretical basis for creating a northern euro as a way to eliminate the long-term weaknesses in the design of the eurozone.

Chapter 7 presents the crisis developments that led to Portugal's request for a bailout package. In doing so, it describes the third tipping point in the crisis—approval of the expansion of the European Financial Stability Facility at the cost of the fall of the government in Slovakia. The chapter also goes into the notion of issuing eurobonds as a way to support failing economies.

Chapter 8 documents the events surrounding Prime Minister Papandreou's announcement on October 31, 2011, of a surprise referendum on the second bailout package. This was the fourth tipping point in the euro crisis: Greece decided to test the resolve of eurozone leaders. On November 2, 2011, EU leaders cut off aid payments to Greece and said it must decide whether it wanted to stay with the euro. The chapter also describes Italian prime minister Silvio Berlusconi's decision to resign, as well as the popular debate about euro devaluation that took place among economic theorists in late 2011.

As described in chapter 9, by July 26, 2012, the euro crisis was getting out of control. In response, ECB president Mario Draghi announced that the ECB would do "whatever it takes" to keep the eurozone together. This was the fifth tipping point in the crisis—and this one was for the better. Following on this resolute ECB action, Ecofin advanced significantly in working out the details of both a banking union and a fiscal union.

Chapter 10 documents the steps taken toward creating the single banking supervisor in the eurozone, as agreed at the Ecofin gathering on December 14, 2012, and confirmed by the heads of state immediately. The sixth tipping point in the euro crisis, it wiped out any remaining doubts that European politicians were united in strengthening the euro. The reform required governments to yield control over the supervision of national banks to the ECB in October 2014.

Chapter 11 focuses on the seventh and final tipping point in the euro crisis. As noted, it came on March 25, 2013, when the Eurogroup, European Commission, ECB, and IMF agreed on a €10 billion bailout ($14 billion) for Cyprus. Slovenia soon ran into troubles of its own. The troubles of Cyprus and Slovenia prompted Leszek Balcerowicz, the most accomplished European economic reformer, to call for structural reforms in the eurozone of the same magnitude as the ones taken in some East European countries during their transition from communism.

The concluding chapter enumerates the successes and failures in decision making and how my views evolved on some key issues.

Disclaimer

Bulgaria is not yet a eurozone country, but it is not a bailout country either. As noted earlier, during my tenure as finance minister Bulgaria was actively pursuing the notion of entering the eurozone, and therefore I was quite engaged in the euro crisis because it affected Bulgaria's path to entry. But the finance ministers from eurozone bailout countries would likely have a very different read on the events and decisions described here. In fact, several of these ministers are academic economists, such as former Portuguese finance minister Vítor Gaspar, and so they are likely at some point to pick up their pens.

During my tenure as deputy prime minister and finance minister, I worked alongside integration believers such as the prime minister of Luxembourg and head of the eurozone Jean-Claude Juncker, Italian prime minister Mario Monti, and German finance minister Wolfgang Schäuble. I also had many thought-provoking discussions with the doubters such as British chancellor of the exchequer George Osborne, Swedish finance minister Anders Borg, German deputy finance minister and later member of the ECB's Executive Board Jörg Asmussen, and Thomas Wieser, head of the Eurogroup Working Group. The interactions with them generated some of the ideas presented in this book.

Praise for INSIDE THE EURO CRISIS

"In his book *Inside the Euro Crisis*, Simeon Djankov goes a long way toward deepening our understanding of the recent troubles in the eurozone and contributes greatly to the discussion of Europe's path toward reform."
—**ANDERS BORG**, finance minister of Sweden

"Simeon Djankov has written an extremely interesting book on the eurozone and on the reforms in his native Bulgaria. The book reflects Djankov's unique combination of superb analytical skills and the experience of successful policymakers."
—**LESZEK BALCEROWICZ**, former deputy prime minister and finance minister of Poland and former president of the National Bank of Poland

"This book is essential reading for students of European institutions and for everyone who wants to understand the difficulties European politicians encountered in the dealing with the eurozone crisis. What makes it unique is the Eastern European perspective on the euro area."
—**JÖRG ASMUSSEN**, deputy social minister of Germany, former member of the Executive Board, European Central Bank, and former deputy finance minister of Germany

"Simeon Djankov was uniquely placed to observe the crisis in Europe. His background as an economist at the World Bank and his function as finance minister in a member state of the European Union outside the euro area gave him the opportunity to observe from the inside and the outside simultaneously. His account is meticulous and analytically sound and has profound insights into the strengths and weaknesses of the European architecture. The book is to be recommended to academics and readers interested in policy issues of a currency union that is still evolving rapidly."
—**THOMAS WIESER**, president of the Economic and Financial Committee of the European Union and of the Eurogroup Working Group

SIMEON DJANKOV, visiting fellow at the Peterson Institute for International Economics, was deputy prime minister and minister of finance of Bulgaria from 2009 to 2013. In this capacity, he represented his country at the Ecofin meetings of finance ministers in Brussels. Prior to his cabinet appointment, Djankov was chief economist of the finance and private sector vice presidency of the World Bank. In his 14 years at the Bank, he worked on regional trade agreements in North Africa, enterprise restructuring and privatization in transition economies, corporate governance in East Asia, and regulatory reforms around the world. He is the founder of the World Bank's Doing Business project. He was also principal author of the *World Development Report 2002*.

Djankov is rector of the New Economic School in Russia and a visiting lecturer at Harvard University's Kennedy School of Government. He was associate editor of the *Journal of Comparative Economics* from 2004 to 2009 and chairman of the Board of the European Bank for Reconstruction and Development in 2012–13. He is also a member of the Knowledge and Advisory Council at the World Bank. He has published over 70 articles in professional journals. He obtained his doctorate in economics in 1997 from the University of Michigan at Ann Arbor.

Peterson Institute for International Economics
1750 Massachusetts Avenue, NW
Washington, DC 20036–1903
(202) 328-9000 Fax (202) 659-3225
www.piie.com

ISBN 978-0-88132-685-7
52595
9 780881 326857