The possible ending of the Eurozone because of the Financial Crisis

In the year 2008 the world recognized the global financial crisis with the insolvency of the American investment bank Lehman Brothers. The crisis had already started with the breakdown of the American Subprime Market one year earlier. In addition, the bank's insolvency made the local crisis become a global financial crisis. In nearly all states, governments and parliaments asked central banks to undertake anything to stop the financial crisis. Therefore, a shift of power from democratic states to financial institutions and economy took place in the following years.

The state of Island apparently turned out to be nearly insolvent, which was the first result of the transmission of the financial economy crisis to sovereign states. Moreover, this type of risk threatens some states of the Eurozone which suffer enormous burden of debts. Currently, the European States develop a new approach to each other and this differs from the balance of powers in the past. As the developments in the past brought wars between nations and suffering to the civil population, so these new changes -which started with the European Coal and Steal Community after World War II- have transformed into a community of states with its own constitution. However, in this community the member states governments continue to have powerful positions and they are able to block initiatives of the European Parliament or Commission.

The actual financial crisis - which has developed into an economic and a sovereign crisis -is threatening the continuity of the single currency Euro and the European Union. The latter is characterized by many different interests, different nations, populations and economies.

This thesis examines the cohesion of the European Union in the actual financial crisis which has prevented wars between the predominant states of Europe for more than half a century. To acquire a fundamental and comprehensive result and to improve the understanding of the reader I have splitted this crisis - which affects nearly all people around the globe - in different parts.

Firstly, the text explains theoretical basics, then it continues with single business, economic, political events and developments which caused the crisis in the end. Secondly,

the text analyzes the structure of the Eurozone and the developments of the crisis in the European Union. Finally, the results out of these analyses and developments are moved together to receive the consequences for the Eurozone. This means the linking points from positions and attitudes are summoned to obtain a better understanding and to get a better conclusion.

Chapter 1 analyses market risks for capital market participants. They consist of diversely positions of which some are nearly not detectable and cannot further be reduced. A big risk for the continued functioning of the capital results in the time horizon of market risks. In actual risk management systems they last at most ten days and in few cases of at most one year. Banks can handle credit risks much better. However, these methods are used in some cases as basis for market risk management and this is not always correct. Furthermore, the separate recognition of market and credit risks is wrong because they overlap in financial markets.

Legal regulations and overall the recommendations from Basel are too weak. After some time capital markets participants are able to go round them and even governments are late in introducing or they do not see any necessity to introduce them. For instance, Basel II was introduced by many governments into legislation either after the start of the earliest global financial crisis or it was not at all introduced. Another point to consider before the beginning of the crisis was the predominant school of thought of New Institutionalism. Some theories of this school of thought are built on each other. However, in the original theories some variables are assumed as fixed whereas in the theories built above the former ones, it is a mistake to assume some variables as fix. Most theories of New Institutionalism assume a perfect market which is not existing in reality. Furthermore, this has led to a reduction of any national regulations at the financial markets.

The final point which is discussed in Chapter 1 are the different types of financial crises. This part comes to the conclusion that in present time one type of financial crisis which is caused by financial market participants and then evolves to sovereign debt crisis remains a major threat. These financial crises generally end with debt restructuring and currency reforms.

Chapter 2 describes developments of financial markets since the Great Depression of the 1930ies. It explores the international and global functioning and analyses the involved actors, factors and developments which caused the earliest global financial and economic crisis.

After the Great Depression financial markets were regulated very strictly and Keynesianism was the predominant way of thinking. Since the introduction of the system of Bretton Woods with fixed exchange rates and the end of World War II, a war which had indebted many states, the USA started to play a dominant role in the financial markets. Their dominant role started with the world's reserve currency US Dollar at many central banks around the globe and continued in the financial markets of private actors, institutions and banks.

In addition to that, the rising power of the financial markets and their lobbyism combined with the dominant mindset of New Institutionalism have reduced any finance regulations and made the USA the center of the financial world, not to mention the continue development of different types of Securitizations, derivatives and globalization of financial markets which were heavily influenced from the USA as the biggest financial center. By showing the functioning of the financial markets, the thesis refers back to earlier financial crisis and shows similar developments to today's acting.

Another point is the technical progress which still continues to accelerate financial transactions and markets. Technical progress - combined with the shift to financial capitalism – made longtime corporate planning nearly impossible.

Next issue of discussion is the ignorance of the systemic risk which is extensively ignored by financial market participants.

Firstly, systemic risk is explained with the introduction of Basel I. Under this regulation all credits must be backed with eight percent of own capital. This means credits with low default probability have too low interests in comparison to high default probability. Therefore, banks securitized credits with low default risks and sold them at the capital markets. They kept those credits with high interest rates and high default probabilities in their own portfolios with the objective to rise profits. By doing so, banks move into

dangerous positions, yet these actions were ignored by governments. They did not introduce stricter regulations, because big financial actors would have left the country and moved to other states with fewer regulations. If these actors left the country this would have led to a capital shortage and put economy into recessions. As people make governments responsible for the economic development, stricter regulations for finance markets are nearly impossible in democratic states.

Today, in the accelerated and more anonymous capital markets with a global derivative markets with the size of more than 600 trillion US Dollars, which consists of capital products and securitized credits and enables global trade for all institutions and banks, systemic risk has risen but it is not sufficiently recognized. Another reason for the financial crisis is the actual use of the rating system of the three big rating agencies. This is not a sufficient risk management used by most capital market participants and is discussed in a separate subchapter. Even after this detection, financial markets still continue to use these ratings. Even today there exist much better risk management methods.

Since the introduction of Basel III which is defined as a weak new regulation, banks transferred parts of their portfolios into the shadow banking system. The shadow banking system is nontransparent, very instable and bigger than the ordinary banking system. For instance one part of it is the asset manager Black Rock with a balance sheet sum of more than US Dollars 4.6.

A reduction in liability and a narrowed feeling for responsibility of the involved people were decisive for these developments. The business, economic and political analyses of the financial crisis and the time before it lead to the next point of this thesis the European Union.

In Chapter 3 are analyzed the problems of the highly indebted states of the Eurozone. It appears that these problems cannot be solved by capital markets against the opinion of different politicians. However, the finance conducted capitalism, as it is described in the book Capitalism Vs. Capitalism from Michel Albert has spread to many

other countries since the book was written and now it is worsening the situation of the indebted states of the Eurozone. As it is concluded in this part of the thesis, the indebtedness will continue to rise in the already highly indebted states. However this will also happen in other states around the world and the people cannot protect themselves against it, because otherwise the international companies will move to other states. This will worsen the economy of any state that reduces state expenditures and it reduces the welfare of the population. To conclude, this means that a state has to get into debt itself because its economy will not be competitive in international markets anymore and the nation welfare will decrease.

The European Union is an example of a hidden undemocratic way of governance. In the past, the founders of its precursor associations like the European Coal and the Steal Community wanted to get a gearing of this community from economy. They also built a structure in which the parliament does not have complete legislative power because it receives proposed legislation from the executive power. The Executive is the European Commission and it makes the proposals for the laws and guidelines which can only be accepted or refused by the parliament. The European council consists of the head of governments of the member states and it has more power than the European Commission. However, it just meets few times a year in comparison to the European Commission, which is working with thousands employees throughout the whole year. This means that the European Commission indeed has more decisive influence on the European Union and its different peoples due to the continued work and the quantity of law proposals.

The European Council introduced the Euro single currency to the European countries, under the regulations of the Maastricht Criteria. However after some years it changed them into recommendations because the European Council was not able to enforce them against the member states. The reason was that the Euro is a political project and cannot comply the economic requirements. In fact, it never did, because even the first member states before the introduction of the currency fouled their data of the Maastricht Criteria. In the end, this means that the Euro remains a political project which does not fit the economic conditions of the member states which have different economic development levels. Therefore, the Euro has become a weak currency which can easily

and strongly be influenced by external factors and actors than if it was a currency of just one country.

The European Council did open different rescue packages for the highly indebted Eurozone member states. However, these packages did spread the government debts to other states and have led to a risen control of the capital markets participants above the governments, as it is shown with the European Stability Mechanism. The disunity of the European Council is a weakness of the European Union, because at this highest point of power of the European Union the intergovernmental issue stands above the super-national point and puts a continued threat to the break apart of the community.

As a comparison, in Chapter 3 the USA and its dollar crisis are investigated. In the USA the policy of the Fed under the command of Alain Greenspan has introduced the methods of reducing the central bank's base rate of interest and increase the money supply to get the economy into a boom again. However, today this method remains only partly successful. It still does work in the USA, as the US Dollar still remains a form of global reserve and major currency. By having this advantage, the USA are able to pilot the capital markets in a hidden way, as it is proven in the text. The USA are able to continue to use the methods of reducing base rate and increase the money supply because other central banks use the same methods - like the Fed - to get the economies into booms again and because the global financial sector has become too big in comparison to the real economy.

After taking these separate analysis in Chapter 4, the results are brought together. There is influence on the legislation of governments done by economy lobbyists and the financial sector implements its participants in governments. There is no introduction of any global limitations on the capital markets companies and institutions and this will let the systemic risk be continuously ignored. There is also the shadow banking system which is far bigger than the banking system and in the end it can influence governments instead of the other way round how it generally works.

In the end, the analysis demonstrates that the debts of any financial crisis are paid by people and not by those who caused the crisis. On the contrary, the text shows that Japan does policy to increase risks for new crisis and Island has managed the crisis as a good example because here in Island the financial economy meets people's expectations again.

In the summary, the autarchy of the capitalism which has developed to the form of the finance conducted capitalism since the breakdown of the Soviet Union rises the risk of the disunity of the European Council and its breaking apart. The finance conducted capitalism bears so many internal contradictions especially in terms of social positions. It rejects the Marxist analysis as a completely wrong system even this is not correct because the Marxist analysis reveals the issues of finance conducted capitalism. Finance conducted capitalism does not accept new ideas and solutions -like the Economy for the Common Good of Christian Felber – and it bases his principles on New Institutionalism. The New Institutionalism - which is apparently not completely correct - and the grown power of the financial markets include a constant rise of debts all over the world.

These developments will lead to a rise in the debts of the member states of the European Union and the Eurozone. Additionally, the risen government debts of most Eurozone states cannot be reduced by taxes but will continue to grow as it can be observed, for instance, for the USA. Even years after the insolvency of Lehman Brothers and the global finance crisis, the European economies remain weak and many governments have high debts. Even just a little crisis can put the focus of the media and the capital markets on the European Union again, which might lead to a break apart of the European Council - whose members feel themselves obliged to keep closer to their own people than to the other member states. However, as shown in the analysis, there exist different structural problems in the Eurozone which cannot be solved by monetary measures of lowering interest rates, increasing money supply and financing state debts by the European Central Bank. They cannot even be solved by the state governments that have to fight strong interest groups and with the develoing domination of the financial world with its internal mistakes, the risk remains for the single Euro currency.

Chapter 5 concludes the analysis describing how the crisis is highly complex to understand. The crisis has its origins in different sciences and the involved groups are dependent on each other. There are real people and institutions that have huger power in comparison than those that rule over ordinary people. Furthermore, the increased money supply - together with a reduced real economy growth - will lead to the next financial crisis.

Another issue is a nearly unlegislated area for capital market participants together with the mistakes of the system itself, as it is, for instance, in the use of ratings of only three rating agencies which have proven not to be trustworthy in the case of subprime ratings. Furthermore, there is a mix between the understanding of freedom of the individual and the freedom for any enterprise which harms peoples, as thoroughly discussed.

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