

# Economics of EU Integration

## Problem Set 2

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### Instructions

- This problem set is worth 15% of your final grade.
- Work in groups, but hand in your own work.
- Submit your work in hardcopy at the start of class on Tuesday, 17 November. Late assignments need to be accompanied by a doctor's cert.
- Label the hardcopy of your work with your name and student number.

### Question 1

In the Euro area, fiscal transfers between countries are a very small fraction of GDP.

1. Explain the possible economic rationale for the Maastricht convergence criteria.
2. Describe 4 elements of the stability and growth pact. What effects did the stability and growth pact have in the run up to monetary union in 1999 in the Euro-area?
3. Explain how fiscal transfers help a country facing an adverse macroeconomic shock. Given an example of such a transfer.
4. Would the absence of substantial transfers matter if there were no restrictions on national governments' budgets, i.e., there was no stability and growth pact?

### Question 2

Of the countries that entered the EU in 2004: Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, and Slovakia, so far only Slovenia and Slovakia have fully joined the Euro. But a number of the others are eager to join, and eventual acceptance of the Euro is supposed to be a requirement of EU membership.

1. What advantages are these countries likely to derive from adopting the Euro?
2. Will an expanded Eurozone including as many as 20 or 25 countries be an Optimal Currency Area? How would you judge this?
3. What criteria will determine when these countries are permitted to join the Euro, and are these criteria appropriate for them?

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