

# Causes of the euro debt crisis, its impact on international financial markets, in...

[Finance](#)



The paper " Causes and Salient Events Leading to the Euro Debt Crisis" is an excellent example of an assignment on finance and accounting. The euro debt crisis is a financial situation facing the eurozone comprising of 17 member states that use the euro currency where some member countries have worsening sovereign debts borrowed from financial institutions. These countries pose a credit risk if they default on their obligations to the detriment of the monetary union. The case is more severe for member countries like Greece, Italy, Ireland, and Spain. Various causes and events have been pointed as leading to the present crisis. For example, according to the Alliance of Liberals and Democrats for Europe- ALDE (2008, 11) structural factors that encouraged free market, deregulation of markets, self-regulating market virtues and increased use of new global financial instruments as a major cause. Extensive leverage on a large scale by market participants and enhanced systemic risk due to reduced transparency and contagion effects. The extensive sovereign borrowing, slow or stagnant economic growth rates by Greece and Italy and lowering of credit rating for Greece from A- to Triple B plus are some of the events that have worsened the crisis (VoA news, 2011). How does the debt crisis in some countries within the Eurozone, such as Greece, Italy, etc. impact on the international financial markets, including the US, Eurozone and Asia?

As indicated in the figure on nytimes. com, the world has become a global village and is much interconnected. Severe debt crisis shocks in Greece and Italy are likely to result in continental contagion because financial institutions holding their sovereign debts have origins and investments in different continents (New York Times, 2011). Both US and Asia heavily trade with

<https://assignbuster.com/causes-of-the-euro-debt-crisis-its-impact-on-international-financial-markets-including-the-us-the-eurozone-and-asia-and-ways-to-resolve-it/>

Europe and the euro debt crisis are likely to slow down their economic growth and possible down-grading of financial institutions that hold sovereign debt instruments. Due to the possibility of high credit risk, interest rates are also likely to go up for both the private and public sector complicating the case further. High sovereign debts among Greece, Italy, and Spain could force financial institutions to write off some debts or a bailout plan by able countries like Germany and France. The possible collapse of the euro would result in a financial loss for among banks (Yahoo news, 2011).

How does the crisis impact the valuation of the Euro as against other major currencies in the world?

Worsening debt crisis would mean slow economic growth among member states and high credit risk associated with holding the Euro resulting to low demand. This makes the euro to depreciate among the major currencies and players prefer to hold safer currencies like the US dollar and Swiss franc. For example, the euro lost 25% of its value against the U. S. dollar since November 2009 to June 2010 (Kolb, 2011, 389)

How, in your opinion, would the crisis be resolved?

First, the countries have to embrace better fiscal management to avoid unnecessary national expenditures among. Rationalization of fiscal income, better tax collection and cuts in civil servants salaries among member states to avoid higher heterogeneity should be embraced (Kolb, 2011, 390).

Member states should also allow the central European authority to have some control over their sovereign budgets in order to create better fiscal and monetary policies. Currently, the monetary policy is joint while fiscal policy is

<https://assignbuster.com/causes-of-the-euro-debt-crisis-its-impact-on-international-financial-markets-including-the-us-the-eurozone-and-asia-and-ways-to-resolve-it/>

not creating a mismatch. Allowing the European Central Bank (ECB) to have control over spending taxation would help the union to monitor and influence recovery among debt-ridden countries (Yahoo news, 2011). High political goodwill and financial transparency among member states to support each other would help to reduce the global fear of a possible collapse. Initiating policies that boost economic growth in countries where its slow or stagnant would also ease the crisis. Finally, issuance of a single euro bond where member states co-guarantees their debt would lower borrowing as strong economies like Germany and France would reduce default risk.