Drown and Out: Is the Eurozone Doomed to Failure?

Sustained deflation in the Eurozone, along with the resurgence of anti-austerity politics and fears of a 'Grexit' could bring Europe to its knees once again - and destroy the Euro in the process, write ***Joe Phillips*** *and* ***Rishi Kakkad****.*

THE EUROZONE has been relatively troubled as of late – the currency union of EU member states that have adopted the Euro – with predicaments building economically, politically and socially across Europe.

Deflation has been on the rise in the Eurozone, reaching 0.8% (-0.8% inflation) as of January 2015 on the HICP, and this could have huge ramifications for all member states. The constituent economies, such as Germany, France and Italy – three G7 powerhouses – could fall into a vicious cycle of underinvestment in the long-run, as firms lack confidence and fear for an economic future of continually lower prices and thus reduced revenue over time, yielding smaller profits and driving many to shut down or contract, giving rise to cyclical unemployment and reduced national income – undoing much of the progress achieved in the recovery from the Global Recession thus far. What's more, offset consumption will multiply this effect – falling prices will strengthen the purchasing power of the Euro for consumers, and households may 'hold off' on spending until prices fall to a level they desire. With Germany having only just avoided recession – two consecutive quarters of negative economic growth – in the third quarter of 2014, and both France and Italy in economic stagnation, it is clear to see that this scenario could be realised.

Economic issues are only being further intensified by the changing political climate in Europe. Most notably, the landslide victory of the anti-austerity party 'Syriza' in the snap Greek election in January, and the new Prime Minister's patriotic ambition to cut the gargantuan £177bn national debt of the country – 175% greater than the Eurozone average. With the austerity enforced in Greece from tight fiscal policy, such as in reduced public spending and greater taxation of both the Greek people and its corporations so as to begin to cut the colossal national debt, incomes have fallen and living standards have thus suffered. The Greeks have reached boiling point, and have voted in their thousands for Alexis Tsipras and his left-wing party to take government in the country, promising an end to progressive tax rises and spending cuts in the country.

So, how does this impact upon the Eurozone? The threat of a 'Grexit' – the potential exit of Greece from the currency union – is considerable, especially as current negotiations with Germany, France, the IMF and the ECB to write off part of Greece's seemingly unpayable debt are stalling and show no signs of progress. A 'Grexit' would have great ramifications for the value of the Euro, the European economy and thus the balance of trade for almost every European country – even those outside of the Eurozone, such as the UK, which is at the forefront of economic recovery in Europe, with 3% GDP growth in 2013.

We are all prisoners of the economy in Europe, and with the sustained rise of the BRICs and falling investment in the Eurozone, the currency union may well be doomed to long-term failure.