

Can the remorseless logic of economics and the confused dilemmas of politics be reconciled?

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In this presentation

- **Assess** the far-reaching reform process of the last two years
- Identify **three main strategies** out of the crisis
- Highlight the main **political dilemmas** faced by EU leaders

An unexpected record of institutional innovation

- **Stronger firewalls** : ECB activism, EFSF/ESM
- **Tighter fiscal surveillance**: Six-Pack, Stability treaty (Fiscal Compact)
- **Financial supervision**: ESRB, supervision agencies, ‘banking union’
- **Reinforced macroeconomic coordination**: macroeconomic imbalance procedure, Euro + Pact, Europe 2020
- **European Semester** as integrated coordination framework

Assessment

- **Markets not yet convinced**, despite a major departure from Maastricht: creation of the ESM
- **Continuation with decentralised, rule-based governance**: flawed regime of ‘non-credible’ sanctions and targets
- Macroeconomic coordination biased towards **collective austerity** and privileging **rules over discretion**
- Long-term ‘social investment’ (Europe2020) downplayed

Unanswered questions

- **Shift towards intergovernmentalism?** New role of European Council under Lisbon Treaty strengthened in crisis; but also long-term institutional innovations (ESM)
 - **Uncertain future of EU-27** : who is out? who is in?
- ⇒ Though unimaginable a few years ago, these developments are deemed insufficient. The Euro is not yet seen as an “irreversible project”.

3 main strategies put forward in economic literature

1. Insurance-adjustment strategy (reinforce the current direction)
2. Smaller Eurozone
3. Fiscal (and political?) union

1. A beefed-up insurance-adjustment strategy

- A **more credible insurance pillar**: larger ESM (with banking licence), debt redemption fund, ECB as “lender of last resort”
- **More time for peripheral countries** to adjust, more EU incentives (but continuation with conditionality)
- **Two-sided adjustment**: higher inflation rate in the core (wage-bargaining coordination)
- Need for **stronger growth strategy**: greater room for manoeuvre at EU level

2. A smaller Eurozone

- **OCA theory:** monetary union works only if sufficient cycle convergence and market flexibility
- Contrary to expectations, **EMU did not get closer to an OCA** during the last decade
- **One-size-fits-all monetary policy** widens divergences

3. Fiscal union

- **Eurobonds**
- **Banking union:** EU resolution mechanism, central supervisor
- **Finance ministry** : could overrule national budgetary decisions
- Optional: counter-cyclical insurance scheme (automatic transfers)

The politics of the Eurozone crisis

- **Confusing picture of public opinion:** preference for keeping the euro... but reluctance to pay the financial and/or political price
- **3 overarching political dilemmas:**
 - Diversity and cohesion
 - Institutional consistency
 - Democratic legitimacy

Diversity and cohesion: what kind of convergence?

- Diversity considered a founding principle of EU. EU historical success as ‘growth and cohesion’ machine
- **EMU, and the Eurozone debt crisis, unravel the equilibrium:** preference for (downward) market-based restoration of competitiveness over (upward) harmonisation of socio-economic settings

Institutional dilemma: how to preserve the Community framework?

- Emergence of a **multi-speed Europe** with uncertain common direction
- **Which institution is in the driver's seat? Who speaks for Europe?**

Democratic dilemma

- **Integration “by default”** rather than by choice
 - Rising **anti-EU feelings**, but politically diverse
 - Strong rationale for political union (strengthening input legitimacy), but **absence of European demos**
- ⇒ **Conclusion: Urgent to realign competing economic and political objectives**