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“The State of the European Economic Union”

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When we talk about the state of the European Economic Union, there is some ambition; we have to look beyond the technicalities beyond the literally hundreds of initiatives and specific measures that are taken in the quite extraordinary context in which we are finding ourselves. In fact we are looking, if we want to address these themes for some kind of benchmarks of success of public policy. It is not enough to take measures; the question is how to measure the effectiveness and the relevance of what we are doing from the point of view of public policy. We could take a starting point to that by looking at the overall picture.

1) Our Democracies clearly need to provide answers to the angry American voters or the angry European demonstrators complaining about austerity, the risks for their jobs and the risks for their living standards that are ambitions that we can not escape. Linked to that, the other profoundly important benchmark is that we need to respond to short term challenges in a way that is compatible with the long term interests of our citizens and long-term values of the EU. It is clear that we need to find answers that do not just respond with some sort of populist short term reactions to the expectations and anxieties of our citizens but we need to respond in a way that corresponds to a coherent vision of where we want to go.

There are two things that have dominated the debate and sometimes they are being mixed up.

1. The challenges that existed before the crisis started
2. The crisis itself.

The challenges that existed before the crisis started

- i) The process of globalization that creates all this interdependence that is unique in human history.
- ii) The geopolitical shift that is taking place through the emergence of the emerging countries.
- iii) A whole group of issues having to do with the limits of Mother Nature: Our civilization and the technological level of our civilization, brings us close to the ability of our planet in many respects. This is true for issues like climate change, competition of access to limited resources, biodiversity and overall the need to end the carbon economy and move toward a future that is really sustainable.

Sustainability is a key concept in the 21st Century both in terms of the environment but also fiscal sustainability and social sustainability.

All these evolutions (globalization, the emerging players, the limits of Mother Nature) are in terms of International Relations increasing the global interdependence in a spectacular way.

And then the crisis came.

What did the crisis do?

The crisis itself

1) It accelerated the changes (three headings before).

2) It demonstrated how difficult it becomes to manage the challenges of the interdependence if you are in a situation of crisis. When you have angry citizens, you cannot really make trade negotiations or climate change initiatives. The crisis in fact undermines our global ability to deal with the challenges that we are facing. The crisis itself was so powerful that it created a sense of urgency both in the direction of coping with the consequences that we have in our hands but also on the need to prevent the next one. So in

these extraordinary circumstances, in terms of public policy there are **three ideas** that are extremely pertinent.

i) The global challenges have become much more significant: At the beginning of this crisis we had all these discussions about decoupling, the US was going to suffer from the crisis but not Europe. Then we had the fiscal crisis and the US saying is there really going to be contagion. These discussions now look like a joke two years down the road. We discovered, with some degree of astonishment (from some public commentators) what a cliché the governor of the European Central Bank (ECB) said:

"In fact we discovered through the crisis that we live in one global integrated economy with all the interdependence that this means".

ii) In a context where the global challenges become very important for each State and even for each individual, the ability of public policy to deal with them, is becoming more difficult.

You have seen as a result of the economic crisis the G20 getting together. The G20 Leaders was created as a result of the need to act coherently because nobody can face the consequences of the crisis alone. As we feel this need to react together we see globally on all issues on each one of the big challenges that the ability of the States to get together and produce a coherent public policy response to the global challenges of our time is not up to the task that we are having. We are improving, but the world is moving ahead, the interdependence is moving again quicker. You can see that in all specific aspects of each one of the core challenges.

iii) A lot of what we have seen as a result of the crisis concerns primarily the developed world. This is a profound evident truth. On the top of that list has to be fiscal sustainability, it is the whole of the developed world that is really facing a profound challenge of historical proportion of fiscal sustainability and managing public debt (not only public by the way but debt in general). Fiscal sustainability, sluggish growth, high levels of unemployment, risks of relative loss of standards of living. We are facing the same challenges among developed countries and particularly in the United States and Europe.

So that is the kind of context within which we should look at the state of the Economic Union. Without defining a little bit this context, we cannot look for the benchmarks because the state

of the Economic Union depends on how much we are able to respond to the challenges that we are facing.

There are three questions that we cannot avoid if we really want to answer the question what is the state of the Economic Union?

- 1) How the existence of the EU protected our citizens from the consequence of the crisis?
- 2) How the EU reacted to the crisis itself, the crisis management?
- 3) How can the EU face the challenges of the future?

How the existence of the EU protected our citizens from the consequence of the crisis

There are two main aspects of this; the internal market and the Euro. The internal market, worked in a visible way as a huge barrier to the protectionist that appeared all around the world. To a very big extend, this is due to the EU governance, the rules of our Internal Market and the legal framework that they created. Also the Internal Market together with the Euro has been a formidable engine for growth at least for the 10 years before the crisis that made the EU much more able to face the crisis. That is something that is often not understood, how successful from the Economic Policy point of view, the EU has been the 10 years before the crisis. During these 10 years the GDP per capita in Europe increased roughly as in the United States. The EU created in the 10 years before the crisis around 60 million new jobs which is a bigger number than the corresponding number in the US. The currency itself in the international markets won much more space and importance than the currency that it replaced. Certainly the Euro and the internal market where a very important defense they made the EU much more able to face the crisis than it would have been possible otherwise. Think of this crisis with 16 Central Banks, think in terms of the instability, the exchange rate recreation that we would have and the impact that this would have on the real economy. There is no doubt on the importance that the existence of the EU and the economic governance and instruments of the EU had in the ability of the Europeans to face the crisis.

How the EU reacted to the crisis itself, the crisis management

The EU as other big players in the world scene had all kinds of initiatives in the direction of creating a stimulus to start with. It supported the banks and the financial stability, it created some kind of financial regulatory initiative to respond to the weaknesses of the system as they appeared from the crisis and it managed the exit strategies. There is a big set of reactions and measures that should not be underestimated.

Most importantly, during the extraordinary period of the pressure of the economic crisis the EU took the measures in support of Greece with more than 100 billion Euros, which is an extraordinary initiative of solidarity that was taken outside of the institutional framework, with each member state helping Greece individually. Then we created the stability mechanism for the Euro, with the IMF for 750 billion euro capability, which are initiatives that have to be appreciated to their right value. These were measures of an enormous scale that had to be decided, in some cases "over the weekend" in a coherent way among 27 democratic governments that are sovereign and it happened.

There were huge discussions about whether the Germans hesitated too much or whether it took too long. Of course there will be difficulties and of course there will be different legitimate views. What really counts is where the ability to act is? What has this process demonstrated in terms of the ability of the EU to act? The outcome was beyond the wildest expectations of the most convinced Europeans before the crisis. Both the mechanisms and the level of solidarity, go far beyond the institutional framework and the rules that exist in the Treaties.

How the EU can face the challenges of the future

A starting point has to be the Euro and the fiscal discipline because this is where the core crisis of the EU emerged during the process of the wider economic crisis. Making a long story short, we knew from the beginning of the Euro, that there are 3 fundamental conditions for the sustainability of the Euro without a political Union that you can find in all the Reports of the Commission particularly through the "decade" of existence of the Euro.

These are:

i) Fiscal discipline: You have 27 sovereign players, on who the system cannot impose what their fiscal attitude will be. The EU needs to succeed to find a way to reach States of guaranteed fiscal discipline.

ii) Convergence of competitiveness: You cannot politically have the Greek economy moving the opposite direction than all other Member States for too long because it becomes politically unsustainable. This is traditionally seen as a fundamental weakness of the EU system. It could however also be seen as a fundamental strength. If the EU manages to develop mechanisms that can bring convergence of competitiveness on the long term and to lead an economy where we have crisis, like Greece back to a positive evolution of its competitiveness, it will have created a system where for each Member State, the participation to the Eurozone make it a political and economic imperative to.....

iii) A mechanism to manage Crisis

These are the three conditions of the sustainability of the Euro. What we are seeing now in terms of reaction, the two conditions, fiscal discipline and convergence of competitiveness, were supposed in the growth and stability pact, to be taken care of by the process of surveillance and the peer review process. Obviously this did not work out in a sufficient way and this is why we had the crisis. Europe would not have suffered from the fiscal crisis if the surveillance and coordination mechanisms had worked to the extend that was required for the crisis. However that's how the modern world works; Public policy fixes a framework and then the world evolves so quickly that the crisis emerges because it escapes the framework that was established.

Now we are seeing an effort to improve and to deepen the surveillance, the peer review mechanisms and the sanctions in order to achieve these key objectives that we know are conditions for the sustainability of the Euro. This is linked to the whole debate on how to manage crisis. We had the temporary mechanism for stability of the Euro dimension before, this needs to become Permanent. So you have the proposals of the task force, the proposals of the Commission, the ideas of Germany and others on how to make this mechanism permanent and you have this whole debate about the possible change of the Treaty. So what we are seeing as a result of the crisis is a reinforcement of the mechanism of crisis management that was missing. We knew it was missing from the Euro setup. The crisis created the conditions

so that we can do something about it. The heads of state of government accepted that we need to see whether we need to change our Treaties to consolidate this mechanism.

Coming back to the idea to reinforce the surveillance which is another key concept. The whole effort has to be to create a surveillance that deals with the discipline that is needed but also a surveillance that is wider in two ways.

- 1) Create a kind of macroeconomic surveillance that anticipates the difficulties.** We felt that we should have some warning indicators before we get into the fiscal crisis.
- 2) Concentrate in this surveillance and policy coordination on the structural changes that serve growth jobs that means the objectives of 2020.**

Europe 2020 is the long term vision of the EU, where we want our society to go. There are three main orientations of Europe 2020

- i) Improving productivity through knowledge and innovation.**
- ii) Create an inclusive high employment society**
- iii) Tackle climate change, so the green economy of the future becomes a real sustainable economy**

The governance that is emerging from the crisis is a governance that aims both to improve the fiscal discipline thus making us more able to deal with fiscal instability and to deal with the competitiveness/convergence that we need. Furthermore it aims help us move in a coherent way towards the Green economy of the future. That is the deep essence of the European semester which is the idea that during in fact the six first months of the year, the European Governments will get involved deeply with the EU Institutions in a kind of step by step interaction that should resolve into much deeper coordination of national economic policies in order to insure that we become more able to guarantee the stability and the sustainability of the Euro. However, we also give full attention to the convergence of competitiveness and the need to move towards more innovative and competitive Economies in the long term.

In terms of the Economic governance that is emerging in Europe we have seen the Commission proposals for boosting the single market, together with the proposals for the citizens' rights (issued as a package).

The economic governance is not only about growth, it is about growth focused on the needs of EU citizens. There is a fundamental debate concerning the way we deal with the financial institutions, the moral hazard of having tax payers bailing out private capital to the financial institutions, the need to find mechanisms for the future that do not allow our societies to get into the situation that we found ourselves in the last crisis. In fact the European tax payer committed almost $\frac{1}{4}$ of the total GDP of the EU to support private capital/financial institutions. That raises fundamental questions about the future and it's important that we have this whole debate about the economic governance focused on the needs of EU citizens as this is the essence of our Democracy.

There is another dimension namely that the EU is focused on the individual citizen in respects that often even our own citizens do not understand. Being a citizen of the EU means that the individual has additional rights such as the right to work, to live, to buy a house, to start a business in wider space. That means a more coherent space and more rights for the individual. That is what the EU has been doing for the last decades. In fact the wellbeing, the freedom of choice the personal development of every individual citizen is not only about the individual himself, it is about the society. These are powerful engines for social and economic progress and it's an integral part of the challenge of growth and prosperity for the future and this is what we want to achieve for the future.

Final Point: The link between domestic policy and international policies. There again there is an incredible amount of misunderstandings. Today, International Relations is because of this exploding interdependence not so much about relations among states it's to a great extent about how able we are to coordinate domestic policies in a coherent way with the other so that we serve the common purpose. In other words if you have a situation where you cannot deliver domestically, you cannot lead internationally. The only way to lead internationally is by example and in a world of interdependence, where each one has to develop domestically the policies that serve the common purpose and the actors are fundamentally sovereign the real measurement of the leadership is how much we can adapt our domestic policy in terms the fundamental challenges that we are facing. As we all depend

upon each other in this extraordinary interdependence there is no possibility for one to lead the others. In fact the concept of leadership that we must have is more and more "each one does his part in a relation of interdependence".

From that point of view it is important to think on those terms about what is happening in Europe and what Europe is producing. Many EU governance processes can appear complex therefore it is important to keep both dimensions in mind.

- 1) What the EU is doing in terms of managing the interest of its citizens and its economic governance internally and
- 2) What is it able to project on the key issues of our times in terms of global challenges as a contribution to the global effort that we need to do (trade, climate change).

In fact Europe through the crisis has demonstrated a fantastic ability to adapt, to move forward beyond its own rules and treaties when it is necessary in a positive direction building on the spirit of what the EU is. The EU has been able to project a quite astonishing sense of responsibility and leading by example the world scene (Kyoto treaty Trade, g20).