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Economic governance: ending the creative ideas fair

Discussion based on recent papers by EIN experts Michael Wohlgemut, Walter Euken Institute, Freiburg (Avoiding the Debt Trap, CES) and Fernando Navarette, FAES, Madrid (see his presentation at the Europe 2020 hearing on the EIN website)

The present European ideas fair over the best economic governance possible **ends playing against the Euro**. One should first seek seriousness in **the implementation of the existing mechanisms**.

To a large extend, **the current Euro crisis is the consequence of the failure in the implementation of two instruments designed to work together**: **the Lisbon Agenda** supposed to provide more flexible markets and constant structural reforms (micro-economic agenda) and **the Euro** supposed to secure a prudent fiscal behaviour in the framework of the close economic coordination organized by the Stability Pact (macro-economic agenda). Instead, we had a total failure in the implementation of the Lisbon Agenda because of the open method of coordination and **the inability to enforce the Stability Pact** to core countries, with **no real discipline enforced since 2004 and no binding fiscal rules**. The time is to **reinvent, to rejuvenate existing mechanisms and reintegrate them in one agenda.** The EPP Group in the EP is the only European political force paving the way for a comprehensive and realistic agenda for stability.

1) European economic governance is enough.

One does not need to establish an economic government in the form of a national government. What would be its legal basis? Already "committee like decisions" - as those of the Eurogroup since 2004 - have proven less effective that just fulfilled commitments, according to many economists.

By contrast, the **European economic governance may be defined as increased convergence on good economic practices (with incentives and sanctions**).

Such economic governance **should be discussed in the framework of the Europe 2020 Strategy**, which is **the** comprehensive strategy for long-term competitiveness following the Lisbon Agenda. Why?

a) **Boosting economic growth** is the best way to overcome growing levels of public debt. Growth-enhancing structural reforms are the focus of the Europe 2020

b) No (new) budgetary rule, even necessary, will be enough to restart productivity gains in countries where global competitiveness has declined (France, Spain, Italy,...) with a mid-term risk for the Eurozone as a whole.

c) **Creating a more resilient monetary union** means according to the theory a union in which every country is better able to resist an asymmetric choc, because it has a diversified economy, easy access to export markets (ie.global competitiveness) and access to a large foreign employment market. Therefore **the regional policies and the Single market policies** - whose next steps are outlined by the Monti Report - **should be fully integrated in the Europe 2020 Agenda**.

d) The Europe 2020 initiative provides a unique opportunity to review rapidly, in the framework of existing mechanisms, **national plans for structural reforms** and investments, and then to back them with the appropriate European funding (or suspend such funding if those plans are not convincing).

e) The Lamassoure's working document (May 2010) proposed to **address immediately the issue of the funding of the Europe 2020**.

2) **The Eurozone governance: back to the bases**

Crisis management mechanisms should not be transformed into permanent safety nets. Over the long-run, the Eurozone economic governance should respect key principles on which the Euro was built:

- **independence of the ECB** ;
- close economic coordination in the framework of a **revitalized Stability and Growth Pact;**
- no automatic participation in the Euro.keping Euro as a currency should remain a demanding and selective venture;
- the cost of non-prudent fiscal behaviour should be assumed by infringers.

3) **Against the debt trap: the subsidiary principle should applies.**

There is not a single European model.
As the major risk for the long-term stability of the Euro is the debt trap, **national strategies** to avoid it have to be designed according to the **specific situation** of each member state:

- for most of EU States, higher taxes should not be a sustainable path to consolidation, since over-taxation is already quite near with a risk to go on slippery slope of the Laffer curve, where tax increase ends up in tax evasion and reduced growth ;
- lower public expenditures should be associated with a strategic shift from consumptive spending (welfare, defence and redistribution) to public investment (training, research) for the benefit of future generations
- reforms of social security system ; health care and pension reform should be a priority.

Those decisive moves should come together also with additional long-term **"debt brakes"** also decided at national level. **Far from demagogical reasons, well founded reasons should support important decisions about public debt** :

- super-majority in legislatures in order to authorize increase of public debt ;
- 'golden rule' according to which the share of government outlay financed by the debt is equal to the share of investment in public capital;
- constitutional amendments that require balanced budgets, as in Germany, those rules taking full effect in the future and after a transition phase.

The management of this major crisis requires an increased flexibility in terms of intellectual approach, decision making and structural reforms. It has been proven that some recently integrated members with experience of permanent adjustment and change over the last twenty years have resisted better and recovered faster.

Boosting growth is the basic of economic recovery, monetary stability and convergence. The present brain-storming at European level may come out with very positive results if it remains focused on:

- the content of **further economic convergence** required to achieve that objective;
- the governance of the **Europe 2020 process** and its relation with existing European policies, including the budget ;
- the final **completion of a true Single market : the excessive fragmentation of the EU has proved to be an obstacle to recovery and deepens stagnation ;**
- the future governance of the **Stability and Growth Pact.**

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