Joint Action versus Free Ride: EU Financial Crisis Management Based on a Common Good?

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> We must all hang together, gentlemen...
> Else, we shall most assuredly hang separately.
> Benjamin Franklin

> The common weal of the peoples of Europe must be our maxim.
> Helmut Schmidt

I Introduction

'The situation is hopeless, people are helpless, markets are relentless and politicians are clueless'. This seems to characterise the general mood in Europe in 2012, as pundits and serious analysts hold alike.

Anti-Europeanism abounds, combined with mistrust in the political elites who are considered incapable of solving the multiple crises Europe has been facing ever since 2008.The alleged decline of Europe and notably the European Union (EU) is the subject of a whole legion of books,[2] articles, and newspaper headlines, which pinpoint this 'deplorable development' almost every single day. This is not an isolated phenomenon in individual member states of the EU, but rather a kind of generic characteristic all across the Union. Annoyance with Europe has become *à la mode* and is growing rapidly.

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2 For an excellent overview of the arguments see Paul Taylor (2008), The End of European Integration. Anti-Europeanism examined. London: Routledge.

Over the past two years, EU heads of state and government have met 20 (!!) consecutive times at summits to deal with the fallout of financial crises without any convincing result in spite of the high hopes they had held to impress the markets. Numerous meetings of eurozone finance ministers, task forces, and preparatory bodies (such as the well-known EFC[3]) have been called again and again in order to suggest and to shape the right emergency measures – most of them in vain! It has thus been proved that in European politics, more so than in national politics, the shortest distance between two points is never a straight line.

Scholars and students of European integration keep reminding us that crises and the determination of Europe's political elites to find common solutions have both been at the cradle of the European Communities and have often preceded the leapfrogging which has characterised the development of Europe over the past six decades.[4]

The choreography of EU development over time may be described as a swinging pendulum: alternating periods of europhoria and over-integration, and phases of stagnation and under-integration. The point of equilibrium has always been the 'locus' that marks the common good for both the member states and the Union as such.

In Section II we will search for this 'European common good'. We will try to determine what the common weal of Europe and the combined well being and shared values and interests of the member states might mean and imply, and answer the questions of whether such a European common good exists at all and if so, how it might be captured and defined.

In Section III we will investigate the multiple rationales of Europe and its approach towards ever closer integration, and we will question whether there is enough 'convergence of beliefs, values and interests' to build upon – notably in times of economic crises. On the one hand, Europe has indeed managed to create a common and free realm of mobility, communication, interaction, liberty, etc. without boundaries; on the other hand, it may have degenerated into what Ha-

3 The Economic and Financial Committee (EFC) is a committee of the EU set up to promote policy coordination among the member states. It provides opinions to and works for the Council of the EU including assessments of the economic and financial situation, the coordination of economic and fiscal policies, contributions on financial market matters, exchange rate polices, and relations with third countries and international institutions.

4 Desmond Dinan (2004), Europe Recast: A History of European Union. London: Palgrave Macmillan; Tony Judt (2005), Postwar: A History of Europe after 1945. NY: Penguin Press.

bermas[5] recently criticised as a ‘post-democratic threat of executive federalism’, i.e. the heads of state and government decide whilst ignoring and blindsiding the will of the peoples and the citizens of Europe.

The upshot of Section III will be further analysed in Section IV, which will discuss the possibilities and limits to economic policy coordination within the European Union.

Section V is devoted to the actions and reactions of major European players trying to fight the two financial crises since 2008. The tension between a common good approach and the prevalence of partial and national interests makes for interesting conclusions regarding where Europe and the EU presently stand and where they might be heading when the crisis is over.

Section VI will examine the feasibility of turning the eurozone into a fully-fledged fiscal union, concluding that there are both structural difficulties to make such a reform ‘tick’ and notional uncertainties about what a fiscal union might actually be and possibly entail.

This leads to some concluding remarks in Section VII and the crucial questions of what kind of Europe we want to strive for and which Europe mirrors the common good: a Europe of bureaucrats and the Brussels institutional machinery, a Europe of economic interests and enterprises in an unregulated free-market setting, a Europe of intellectuals and academics (widely neglected and side-lined so far), or a renewed and refreshed Europe beyond the alternative of ‘deals versus ideals’ and based on the will, preferences, and discourse of the normal citizen of Europe holding a national, regional, and European identity atz the same time. Today the European *citoyen*, the sovereign of last resort, has become alienated and appears no longer aware of the spirit and purpose of the European Union, nor of its common good. The Brussels institutional apparatus has managed to create a distance between citizen and elites, which needs to be rapidly and drastically narrowed if Europe is to be revived.

5 Jürgen Habermas (2011), Zur Verfassung Europas (‘On Europe’s Constitution’). Berlin: Suhrkamp Verlag.. Habermas criticises the European Council, which was given a central role in the Lisbon Treaty. He views the Council as a *‘governmental body that engages in politics without being authorized to do so.’*

II In Search of the Common Good

The notion of 'common good'[6] encapsulates a deep-seated yet subjectivist politico-philosophical concept encompassing a juridical, sociological, political and, last but not least, economic dimension.[7]

When talking about a common good from a medieval *Aquinian* perspective,[8] philosophers used to refer to the ***bonum commune*** as a natural quality – something which is a given and for which all humans strive. However, such a transcendental, abstract and *a priori* definition runs the danger of quickly turning totalitarian:[9] an idea, ideology or higher objective or purpose may be hijacked by a ruler or dictator and may be used to coerce his people and citizens into following what he defines as the common good. Whereas Rousseau[10] differentiated between the '*volonté de tous*' (the will of all individuals in a community) and the '*volonté génerale*', (the will of the community as a higher entity), the utilitarians in the Bentham tradition[11] defined the common good as the 'greatest happiness of the largest number principle'. Utilitarians claimed that the best course of action – and consequently the common good – is the one that maximises the overall 'happiness' of all. Similarly and in the same vein, classical philosophy considered the common good identical to the *res publica*![12] Modern theorists[13] believe that the common good may only be identified in a 'deliberative discourse', i.e. in an autonomous, non-hierarchical communicative situation undistorted by any

6 The German Max Plank Society established an entire institute in Bonn for the 'Research on Collective Goods' and published a whole series of articles and papers under the heading *Common Goods: Law, Politics and Economics.*

7 Theories in the Social Sciences involve related concepts such as Social Goods, Collective Goods, Public Goods, and Club Goods, etc.

8 Thomas v. Aquin, Summa Theologiae I-II; Herfried Münkler, Harald Bluhm (2002) Gemeinwohl und Gemeinsinn. Historische Semantiken politischer Leitbegriffe. Berlin: Akademie Verlag.

9 Ernst Fraenkel (1941), The Dual State. New York: Octagon Books.

10 Jean Jacques Rousseau (1762), Du Contrat Social, Paris 1992, p. 40.

11 Philip Schofield (2006), Utility and Democracy. The Political Thought of Jeremy Bentham. Oxford: Oxford University Press.

12 *Res Publica***,** meaning 'public affairs' or matters important to a community of individuals or groupings, dates back to classical philosophy and has accompanied political thinking ever since. Cf. Robert. E. Goodin, Philip Pettit. (eds.) (1995), A Companion to Contemporary Political Philosophy. Cambridge: Blackwell.

13 Dietmar von der Pfordten (2004), Normativer Individualismus, Zeitschrift für philosophische Forschung 58, pp. 321-346.

kind of asymmetrical power relation in which all members of a community act as equals.[14] Other students of common good and a general (economic) interest at the European level[15] have pointed out that common good theory conceives of individual acting units – be they persons, citizens, families, clubs, communities, countries, peoples or states, and nations – as always having to take into account the interests and preferences of other such units, with whom they interact, live, or relate. In this vein, it goes without saying that the more homogeneous the various units, the easier it is to jointly define a common good and vice versa!

This points our reflections to the concept of spill-overs and externalities,[16] as developed and applied in public economics. The ubiquity of externalities was notably emphasised in the writings of Egon Matzner.[17] In addition, welfare economics in the Paretian and Kaldor-Hicksian tradition contributes to the thinking about the common good: according to the famous *Pareto criterium*, an initial allocation or distribution among individuals or units of action which may be changed and can make at least one individual better off without making any other one worse off is an improvement to strive for. An optimal allocation is reached when no further improvements are possible. This is a kind of steady state that defines an optimum in the sense of a common good. This theoretical approach was later complemented by Kaldor and Hicks, who argued that even if one individual (A) may suffer a loss by getting another individual (B) into a gainful position, such a reallocation may be efficient if and only if the gains of (B) will be sufficient to compensate for the pain (losses) of (A) and yielding an overall gain on top.[18]

Common goods can thus be defined as the action of individuals or units of action in any community with the aim of achieving cooperative, non-conflictual and pleasant 'togetherness', taking into account the (unintended) results of any

14 Jürgen Habermas (1986), The Theory of Communicative Action: Reason and the Rationalization of Society (original: Die Theorie des kommunikativen Handelns). Cambridge: Polity Press.

15 Gunnar Folke Schuppert, Friedrich Neidhardt (eds.) (2002), Gemeinwohl – auf der Suche nach Substanz, WZB Jahrbuch, Berlin.. 'Les services d'intérêt économique général' have been part and parcel of the Roman Treaty of 1957: Art 86/2.

16 Concepts of externalities and spill-overs are best described in the seminal book of Richard Cornes and Todd Sandler (1996), The Theory of Externalities, Public Goods, and Club Goods. Cambridge: Cambridge University Press (2nd edition).

17 Egon Matzner (1982), Der Wohlfahrtsstaat von morgen, Entwurf eines zeitgemässen Musters staatlicher Interventionen. Wien: Österreichischer Bundesverlag.

18 Tibor Scitovsky (1941). A Note on Welfare Propositions in Economics. Review of Economic Studies 9 (1), pp. 77–88.

individual action on the welfare of all other parties involved and concerned. This implies Subsidiarity,[19] Solidarity,[20] and Solidity,[21] and is the counter-model to private goods and individual interests.

Against this backdrop, our analysis will be based on a consequentialist notion of the common good that cannot be defined *a priori*, but is determined by its resulting outcome, i.e. *a posteriori*. This dovetails with the fact that Europe does not traditionally or historically have a *bonum commune*; rather we were – throughout the largest part of our history – a continent of fierce conflicts and wars. Therefore, no pre-defined *bonum commune* can serve as a precondition or prerequisite, i.e. a sound basis for developing a coherent European political framework in its own right; rather it is Europe's history and tragedy that a common good will have to be the fateful *result of pooling sovereignty and hammering out previous joint action among member states of the Union*. Therefore, the European common good can only be identified knowing all the ultimate consequences of individual and common action at the EU level.

At this point, a related concept may come into play: public finance theory has developed the 'Theory of Public Goods', and ever since has differentiated between (pure) public goods and so-called 'club goods'. Whereas pure public goods imply unity in production and non-excludability in their use, i.e. consumption, club goods, in contrast, allow for partial excludability of non-club members. Both kinds of goods may constitute collective action problems[22] at the EU level: mutually beneficial outcomes (or public goods) can only be secured if member states have no incentives to 'free ride'[23] and if special interest groups are prevented from obtaining benefits to the detriment of the 'public interest'.

19 Klaus Gretschmann (1991), Le Principe de subsidiarité: Quelles responsabilités à quelle niveau de pouvoir dans une Europe intégré? Subsidiarité: défi du changement, Maastricht: EIPA, pp 49-70.

20 Klaus Gretschmann (1986), Solidarity and Markets, in Franz-Xaver Kaufrnann, Giandomenico Majone, Vincent Ostrorn (eds.), Guidance, Control and Evaluation in the Public Sector. Berlin/New York: Walter de Gruyter, pp. 387.

21 This pinpoints economising on scarce resources and the absence of a free-rider attitude on the good will and cooperative spirit of others. See further, the argument relating to the framework of a fiscal union below.

22 Elinor Ostrom (1990), Governing the Commons: The Evolution of Institutions for Collective Action. Cambridge: Cambridge University Press.

23 Mancur Olson (1965), The Logic of Collective Action: Public Goods and the Theory of Groups. Cambridge, Mass.: Harvard University Press; a critical view can be found in Robert Axelrod (2006), The Evolution of Cooperation (Revised ed.). New York: Perseus Books Group.

One final remark seems to be in order with regard to the European level: a good that is common between actor (A) and actor (B) may not necessarily be the same common good for actors (C) and (D). What may be considered in a local community as a common good, may turn into a particularistic interest at a higher – say, national – level. What may be considered a common good at the level of a nation or nation-state may easily change into a particular national interest not conducive to a common cause or concern at the European level.[24] Therefore, some scholars consider the European common good a result of mediation and compromise among competing and differing preferences, interests, and national priorities. Albeit partially true, this interpretation might end up in a smallest-common-denominator approach not apt to bring clarification to the matter.[25]

III Europe's Multiple Rationale: Common Interests and Divergent Beliefs

Fundamentally, states seek to increase their power in international economic relations in order to create conditions that minimise the costs of pursuing their domestic economic priorities in an interdependent world economy. Their policy choices are conditioned by the constraints and opportunities they face in the international environment.

International interdependence provides both costs and opportunities for all actors involved. The main benefit of interdependence is the welfare gain that results from a more efficient allocation of resources. The foremost price of interdependence is a relative loss in national decision-making autonomy. Under the conditions of interdependence, the ability of a government to pursue its own domestic priorities is constrained by external forces over which it has little or no control. These costs of interdependence, however, are asymmetrical among the various participants. In other words, states possess different degrees of power to

24 Therefore, European solidarity among citizens of the Union may be much less resilient and more abstract than national or local solidarity and communality among peers. In respect to the European Union, Alessandra Casella and Bruno S. Frey (1992), Federalism and Clubs: Towards an Economic Theory of Overlapping Political Jurisdictions, European Economic Review 36, pp. 639-46 advocate a structure of 'functional federalism' that allows for a system of overlapping political jurisdictions.

25 Paul Taylor (p.124) asserts that too much emphasis on 'the logic differentiation' and too little on 'the logic of synthesis' may attenuate the sense of common values and destiny in a community such as the EU.

adjust to external pressures or to change the international environment under which they operate. The preferred option of states would be to push the costs of adjustment onto other actors in the system and to reduce domestic costs.

Governments can control domestic conditions only if they can influence the decisions taken in other countries. Thus, states want to avoid or constrain negative externalities of other governments' pursuits of domestic economic priorities. What is the rationale behind these developments? It is the growing interconnectedness of the global world that makes us feel the often unintended effects of the actions of others more directly and immediately. Such 'externalities' are changing the boundaries between domestic and international politics and are eroding the traditional modes of governance. This has profound implications: national decision makers must refocus on international cooperation; new institutional arrangements are needed to take up the new challenges; existing organisations must adapt their working methods; economic policy coordination both in the area of macroeconomics and at the level of micro-policies is badly needed.

Therefore, Moravcsik[26] argues convincingly that both the demand and the willingness to integrate and coordinate are determined by the extent to which it is necessary to manage international interdependence. It seems to be a kind of generic law in integration that, whenever a nation's ability to control its economy is constrained by either market forces, the most prominent of which is international capital mobility, or by spill-over from economic policy measures abroad, integration provides a tool for regaining control and material sovereignty at a supranational level, through the pooling of resources, cooperative governance, and institutionalisation of rules for policymaking. Therefore, it will be necessary to reconcile conflicting national preferences, perceptions, interests, and 'beliefs'. This is particularly relevant since EU policymaking is only rarely built upon a shared, consistent, and coherent concept of policymaking for Europe as a whole.

Essentially, there are two major forces at work: ***deals and ideals.*** As we know from economic psychology, ideals tend to dominate in periods of economic well being, high growth rates, and stable political situations, in which certainty and security prevail, whereas interests and deals become the predominant force in situations of instability, economic slow-down, unemployment crises, etc. The advantage of ideals over deals is, as Thomas Shelling has put it, their self-binding function: in the pursuit of ideals, agents (be they governments or people)

26 Andrew Moravcsik (1993), Preferences and Power in the European Community: A Liberal Intergovernmentalist Approach, Journal of Common Market Studies 31 (4), pp. 473-524.

are inclined to act even beyond their narrow self-interest. When it comes to deals and interests playing the major role, there seems to be less leeway for selfless visions: only if there is interest mediation and positive gains for those involved, will agents stick to treaties and contracts. If interests cannot be made compatible, agents will start to defect. It seems to be quite obvious that due to the many elements of instability and uncertainty currently arising, which result from lower expected growth rates in the coming years, interests may dominate over ideals. This affects both citizens, voters, and taxpayers on the one hand, and institutional actors such as public authorities, administrations, and Eu member states on the other hand.

When we search for the European common good in such a complex setting as described above, laden and interwoven with national interests, the question arises as to what brings nation-states to cooperate and integrate.

Non-conventional theory[27] holds that in the case of the EU the following elements are constitutive:

The fact that in view of a growing number of ***externalities*** in an interconnected world, isolated national policies will no longer be able to work efficiently and effectively. Traditional deficit spending to stimulate the national economy of a country has become inefficient by leading to higher demand for imports; national tax policy has failed in the face of the high international mobility of tax bases; national anti-pollution policy has been rendered useless in the face of emissions carried by wind across borders.

Economies of scale allow for economising resources in a larger Union – in an unrestricted single market, a wider range of goods can be produced at lower costs and sold at lower prices, compared to a smaller national market.

The ***pooling of resources and influence*** contributes to increasing the influence and power in wider settings. A small country like Luxembourg may not be able to promote its interest at the negotiation table of the World Trade Organization or elsewhere, but may possess greater bargaining weight by being an integral part of the EU as a negotiating party.

The well-known '***prisoner's dilemma***'[28] can be avoided between countries which cooperate and integrate closely.

27 For a more traditionally theoretical approach, see*:* Antje Wiener (2009), European Integration Theory. Oxford: Oxford University Press.

28 Anatol Rapoport, Albert M. Chammah (1965). Prisoner's Dilemma. Ann Arbor: University of Michigan Press.

Indeed, in an interdependent world and notably in an integrated area such as the EU, problems and solutions stretch across national borders, resulting in a growing need for collective action. Clean environment, health, knowledge, property rights, economic, and monetary policy are all examples of common and public goods. The main properties and distinguishing features of such international public goods are usually characterised by the fact that their benefits have strong qualities of '*publicness'* – i.e. they are marked by non-rivalry in consumption and non-excludability. This means, respectively, that when provided to one party, the public good is available to all, and consumption of the public good by one party does not reduce the beneficial effect to the others.

Regional public goods[29] are those whose benefits could in principle be consumed by the governments and peoples of all member states. Examples include mechanisms for ensuring financial stability, the creation of a common market, the promotion of research and scientific knowledge, and international regulations for aviation and telecommunications. European energy policy (security of energy supply to all members of the Union), a European patent (with equal legal rights and costs), European public service obligations (valid in all countries), free movement of labour, capital, goods and services with no discrimination, overcoming the financial and economic crisis, a European budget of its own right: these are all examples of European common goods in a wider sense.

If all member states of a Union can benefit from the provision of such common goods they should be easy to supply. However, literature argues convincingly that the public nature of common goods means that this is not always the case, due to problems of:

1. *Sovereignty*: Governments are often unwilling to limit or constrain sovereign decision making, for example by accepting binding rules or international monitoring of their own compliance with agreements.

29 "In the 1990s, it was noted that international public goods fall into the two categories of global and regional public goods, the latter differing from the former on account of the more limited geographical reach of the benefits conveyed. RPGs benefit spillover communities that can range from a couple of neighbouring countries to a continent or hemisphere. Their production typically requires cross border collective action that engages all (or most) of the members of the spillover group."See Marco Ferroni, Regional Public Goods: The Comparative Edge of Regional Development Banks, Paper prepared for the Conference on Financing for Development at the Institute for International Economics, February 19, 2002.

2. *Heterogeneous preferences*: Governments often have divergent interests and priorities as regards specific solutions, even where they share general long-term goals. Energy policy or CO_2 reduction policies may impact differently on individual EU member states. What might be a highly desirable public good for one country or group of countries may not be so for another.
3. *The 'free-rider' problem*: Once a common or collective good is produced and made available to one party, it is hard to exclude others from benefiting. Consequently, there is an incentive for every party to wait until somebody else provides and pays for that good.
4. *The 'weakest link' problem*. Some goods can only be produced when every government fully complies with a common approach, such as the reduction of CO_2 or banking regulation. Success can be eroded by a single act of non-compliance, sometimes due to a country that cannot – at a reasonable cost – carry the burden.

IV Common Good and Policy Coordination

Nonetheless, despite the fact that the EU is often considered an 'unfinished union on the way to an unknown destination',[30] and in spite of being criticised as a 'soft power', it is moving ahead steadily: while undergoing major changes over the last 50 years from a 'trade-driven' (customs union) via a 'factor-driven' (single market) and a 'money-driven' (EMU) to an 'innovation-driven' undertaking – the EU has acquired both political and economic influence and reputation. Its model of regional integration incorporates unprecedented economic progress, new modes of international governance and new forms of collective leadership.

In a world of growing interconnectedness which makes us feel the often unintended effects of the actions of others more directly and immediately, such 'externalities' are changing the boundaries between domestic and international politics and are eroding traditional modes of governance. This has profound implications: national decision makers must refocus on international cooperation, new institutional arrangements are needed to face the new challenges, and existing organisations must adapt their working methods and (economic) policy coordination both in the area of macroeconomics and at the level of micro-policies.

30 Joseph H.H. Weiler (1999), The Constitution of Europe. Cambridge, Mass.: Harvard University Press.

These observations lead us to what Le Cacheux[31] called

> 'the generic idea that the need for coordination arises in contexts characterized by interdependencies…(and the fact that) decentralized decision-making in the absence of coordination devices will lead to sub-optimal, non-cooperative, Nash equilibria'.

However, there seems to be an absence of substantial economic policy coordination in Europe. While Article 121 of the *Treaty on the Functioning of the European Union* requires member states to consider their economic policies as a matter of common interest, the reality is that policy coordination is still rather weak. Whereas *euroland* is characterised by a single currency and a single monetary authority, fiscal policy in Europe is still the domain of national governments. This raises questions of policy consistency and compatibility of decisions and instruments, as well as the timing and extent of policy changes.

There is no reason, Korkman[32] argues convincingly, to expect that the sum of the fiscal policies of 17 individual member states of the eurozone is always appropriate for the euro area. There seems to be general agreement that a genuine European economic policy in its own right is necessary, and that it should not be modelled on a single member state's approach. The problem, however, is that there is as yet no clear vision of where we are heading, nor is it evident which of the features from different national systems should be adopted.

Against this backdrop, there is a need to reconcile conflicting national preferences, perceptions, interests, and 'beliefs'. This is particularly relevant since the monetary union did not start out with a shared, consistent and coherent concept of economic policymaking for Europe as a whole; rather, it was built on the insulated introduction and management of a single currency. Its founders expected the necessary macroeconomic and fiscal institutions, instruments, and policy content to flow from monetary policy pressure.

Indeed, coordination is particularly difficult if policymakers do not agree on the 'true model' that is an accurate characterisation of how the economy functions. As discussed above, a common good requires the existence of both common perceptions and interpretations of what can be influenced as well as a sufficient degree of homogeneity among the relevant actors. Unfortunately, as ana-

31 Jacques Le Cacheux (2010), How to Herd Cats: Economic Policy Coordination in the Eurozone in Tough Times, Journal of European Integration 32 (1), pp. 41-58 at 43.

32 Sixten Korkman (2002), Fiscal Policy Coordination in EMU, Anne Brunilla et al. (eds.), The Stability and Growth Pact – the architecture of fiscal policy in EMU. Basingstoke: Palgrave Macmillan, p. 269.

lysed in the literature on policy coordination in the late 1980s[33] difficulties can be attributed to four main factors:

1. There are different national constraints on the policy instruments available *(limited domain);*
2. There is disagreement about the effects (both of their scale and nature) of specific policy changes on policy targets *(differences in beliefs);*
3. There are cross-country differences in the degree of (inter-)dependence *(differences in spill-over effects);*
4. There are different models of how national economies and the global economy work *(model uncertainties).*

Decision makers tend to have only limited knowledge about the functioning of their national economies. They know even less about the working of the European economy in its entirety. This means they are faced with the problem of having to decide between competing models, the properties and premises of which are only partially understood. This is already an intractable problem at the national level. It will be even harder to solve and even more complicated at the international level. Feldstein and Frenkel and Rockett[34] have proven conclusively that if policymakers do not agree on the true model, coordination may well entail welfare losses. In any international setting like the EU, the probability that there is model certainty and consensus is pretty low. The more uncertain and less consensual a policy model is, the less aggressively policymakers will use their policy instruments.

Siebert[35] pointed out that the conduct of a joint optimal economic policy would require near-perfect agreement on the model and the philosophy on which an economic policy is to be founded. In the same vein, he argues that a coherent and jointly acceptable paradigm of economic explanation and analysis is an indispensable prerequisite.

33 For an instructive overview, see Ralph C. Bryant (1995). International Coordination of National Stabilization Policies (Integrating National Economies: Promise & Pitfalls). Washington: Brookings Institution Press.

34 Martin S. Feldstein (1988), International Economic Cooperation. Chicago: University Press; Jacob A. Frenkel, Katherine E. Rockett (1988), International Macroeconomic Policy Co-ordination when Policymakers do not Agree on the True Model, American Economic Review 78 (3), pp. 318-340.

35 Horst Siebert (1997), Zu den Voraussetzungen der Europäischen Währungsunion, Kiel, Discussion Paper 289, Institut für Weltwirtschaft.

In principle, governments can coordinate either through *inter-governmental arrangements* or through *a transfer of sovereignty to a common institution.*[36] The more binding arrangement is, of course, the latter. The main problem is multidimensional and is confronted by the following dilemmas:

1. As long as there is no consensus on economic models and measures, self-binding arrangements are difficult to achieve;
2. As long as it is not clear which interests prevail in the common, supranational institution and whether it can be trusted to pursue the common goal, the transfer of sovereignty is risky; and
3. As long as spending and taxation are about the level and composition of *national* public goods and *at the same time* about European macroeconomic policy, a sacrifice of the former for the sake of the latter – in the face of varying national preferences – is very improbable.

Therefore, loose forms of coordination are to be preferred and a clear majority of eurozone member states seem to agree with former Commissioner Solbes[37] that economic policy coordination 'should not be seen to pursue a centralised economic governance with a uniform policy response to economic challenges, national policy should continue to have sufficient latitude to formulate and implement policies tailored to their needs.'

Economic policy coordination, as it is understood in the Brussels context, by no means dovetails with the conception of it in academic economics. In principle, economic coordination may have a narrow or a broad meaning.[38] The former implies a 'simple' surveillance and monitoring of the national policies of EU member states in order to veto those national policies that are expected to violate the European common good; i.e. that may produce – Paretian – welfare losses for the EU as a whole. Under this *regime-related coordination* come the Excessive Deficit Procedure and the Stability and Growth Pact, as well as – to a somewhat lesser extent – the Broad Economic Policy Guidelines. The coordination task is

36 Jürgen von Hagen, Susanne Mundschenk (2001), The Functioning of Economic Policy Coordination, mimeo, Bonn: ZEI Working Paper.
37 Pedro Solbes (2002), Economic Policy Co-ordination - the Way Forward, Brussels Economic Forum, 2 May 2002, mimeo, p.5.
38 Jürgen von Hagen, Susanne Mundschenk (2001), The Functioning of Economic Policy Coordination, mimeo, Bonn, ZEI Working Paper.

to identify and measure policies that might affect the EU's welfare position adversely and, in response, to push member states to refrain from adopting such policies. The broader notion of *strategic policy coordination* aims at developing cooperative policies in order to maximise welfare gains and positive externalities from policies adopted by one country that could affect economic variables in other countries. In this sense, the aim is not harmonisation of policy, but ensuring that it evolves in a coordinated manner maximising the common weal.

The above argument about model uncertainties and disparate beliefs demonstrates that in fact (economic and monetary) integration has not yet sufficiently overcome national interests and is still embedded in and constrained by disparate (economic) beliefs and ideas of what kind of Europe we should envisage. A fully-fledged and well-functioning Economic and Monetary Union would require the political will to steer (fiscal and monetary) politics and policies in line with a still to be defined common interest and a generally accepted common model. Considering the lack of these conditions and taking into account the challenges that the Union faces, the conceptual, theoretical, and political foundations on which the monetary union has been erected still appear rather shaky.

V Common Good and Partial Interests: Europe fighting the crises of 2007-08 and 2010-11

At first glance, the movement towards *European Monetary Union* was built on an economic rationale: as a logical corollary of the *Single European Act* which was broadly about the removal of (non-tariff) barriers to intra-European trade. As an upshot, the single market in goods and services called for a commensurate liberalisation of cross-border movements of capital and labour. The creation of a single European currency and control of Union-wide monetary policy by a Union Central Bank was the capping stone of the whole venture. It was considered indispensable that one market operates on the basis of one currency. From this standpoint, an Economic and Monetary Union is principally a macroeconomic project, its target being essentially to shield the internal European market from the vagaries of fluctuating exchange rates and the perceived threats of *competitive devaluations*.

Some players in all of this, to be sure, have always entertained much more ambitious hopes. In their eyes, monetary union has always been the cornerstone of a far-reaching political strategy of integration yet to be consummated. The hope of the integrationists was to create a quasi-automatism in which the single market was to be followed by a monetary union, which might lead to a fiscal union and therefrom to a fully-fledged political union. Moreover, the idea to 'sell' was that the euro's economic mechanics might make everybody better off: if the poorer countries at the periphery shared a common currency with the strong core – like Germany and France – they could count on borrowing money at cheaper rates. The 'core' at the same time was able to export more of their products if the periphery was able to deficit-finance their imports at lower costs.[39] Some analysts called this a 'marriage of convenience'.

Against this backdrop, the original idea to 'sell' the euro to its critics and the general public as by and large compatible with a series of divergent national fiscal policies and on-going national economic sovereignty was attenuated over time. Economists had argued that the EU was no 'optimal currency area', and therefore so-called asymmetric shocks which in a monetary union could no longer be cushioned by exchange-rate adjustments had to be absorbed by means of wage and labour-market flexibility or through a system of transfers and fiscal federalism and a new 'unionised' fiscal policy. These arguments mirror the tension between those who advocate the 'unitary principle' and those who wish to maintain differentiation and diversity in European economic policymaking. Indeed, the risks for the EU as a whole and for any single member state depend on the policies and tools chosen by other member states.[40]

After ten years, during which time the euro worked perfectly and gained a strong reputation and position on the global financial markets due to its high internal stability (measured by inflation rates) and external stability (exchange rate vis-à-vis the US dollar), it was the financial and sovereign debt crises of 2008 and 2011 which laid bare its insufficient economic base and raised doubts about the economic 'principles' of EU integration.

Like the rest of the world, Europe has been going through major financial and economic crises and these are far from over. The crises have led to a search for solutions incorporating the European common good! This has involved a flurry of activity at various levels, including at member state and Union level. Yet the public perception of Europe's response has been rather mixed, with criticism focusing on the lack of decisive action and on the absence of a 'unitary response'.

At first glance, the EU response to the fall-out of crisis 1.0 – i.e. the so-called subprime crisis leading to a banking, financial market, and export crisis followed by a deep global recession – has been rather impressive: central banks cut inter-

39 This argument has forcefully been put forward by Hans-Werner Sinn, President of the German Ifo-Institute in Munich.

40 If too many go for a restrictive fiscal policy, demand in the Union itself may decline and the result may be a negative economic dynamic for all.

est rates to historically low levels, and provided huge amounts of liquidity to the financial system. Some of them embarked on unorthodox measures to provide credit to the economy. European governments channelled massive support to their banking systems through guarantees and recapitalisation. This was done in a well-coordinated fashion. The European Recovery Plan, which was proposed in November 2008, eventually received full endorsement from the European Council and included a significant and coordinated fiscal stimulus.

This response has avoided a financial meltdown involving bank runs and a loss of confidence on the part of European citizens and has prevented an overall collapse of economic activity. Moreover, (1) the mere existence of the euro has prevented member states from choosing 'competitive devaluations' as a national way out of the crisis; (2) the internal market has held up remarkably well, despite all the loose talk about imminent protectionism, and (3) massive sums have been provided directly by the Union and indirectly through the IMF (under pressure from EU member states) to those countries confronted with sudden and drastic balance of payments problems.

The reaction to crisis 2.0 was however quite different:

It all started in October 2009. Trying to hide within the economic turbulence in the wake of crisis 1.0, the Greek government announced that its deficit figure for 2010 was 12.5 per cent, three times the amount officially acknowledged previously. Under market pressure, in February 2010 the Greek government launched a severe austerity package in order to control the fall-out on bond markets. Harsh debates in the European Council followed about the consequences of and solutions to the Greek situation, in particular how to prevent contagion, avoid bail-out discussions, and revise the Stability Mechanism. It soon became obvious that other member state such as Ireland, Portugal, and subsequently Italy and Spain were confronted with similar problems of sovereign debt and refinancing difficulties. In November 2011 the newly created European Financial Stability Facility lent money to Ireland with conditions attached.

It subsequently became evident that in the wake of crisis 1.0 the eurozone was caught in a downward spiral with European leaders left wanting in their approach to crisis management.[41] The sovereign debt crisis inside the eurozone soon laid bare the problems faced by European banks, which were holding government bonds of all types. Struggling banks and stumbling governments under-

41 For a chronological sketch of the developments and decisions since 2008 see Table 1.

mined the confidence of investors, which led to a kind of 'investment strike', deepening fears that governments might be unable to pay back their debts.

Objectively, the eurozone is still strong enough to cope with the crisis. It is less indebted than the United States and its deficit is manageable. It has the financial means to prevent the default of any of its member states. And if not hampered by rules, regulations, and ideologies, the European Central Bank (ECB) could buy out the weak bonds of crisis-stricken countries on the secondary market.

The real problem is that the governments of the eurozone are deeply at odds over what the crisis is really about, and riven by disagreement over what each country must contribute towards solving it. So long as the eurozone's members cannot settle these arguments, or at least agree that their differences matter less than finding a solution, the collective action needed to defend the euro will remain impossible.'[42]

In theoretical terms a coordinated approach by no means implies a harmonisation in which everyone does the same thing, but rather a well-orchestrated coordination, nationally diversified, designed to guarantee a welfare maximum for the whole of Europe. EU member states can *choose from a broad portfolio of measures ('toolkit') the combination that seems to them to be most advantageous*: reducing public spending, increasing the tax burden and revenues, cutting subsidies and the support of specific branches of business, or reducing wages and pensions, often of low-income households. The measures taken to combat the crisis in the short term should be carefully considered as regards their coherence with the mid- to long-term endeavours to accomplish national goals and the Lisbon structural reforms. This means, primarily, intensified investment in infrastructure and innovation, greater support for SMEs and stimulation of employment, innovation, research and development, as well as education and training in order to increase competitiveness. In parallel, the European Council has repeatedly stressed that a strengthened *stability and growth pact continues to be the cornerstone of the fiscal framework of the EU*. However, criticism has been voiced vis-à-vis the 'toolkit approach' since, in addition to a gratifying commitment to flexibility, the approach is characterised by a lack of both conceptual stringency and of a common interpretation of the economic situation and its consequences for the diversity of economic interests in the Union.

42 Economist 12 November 2011: Special report: Europe and its currency. Edward Carr, Staring into the abyss.

In the wake of crisis 1.0 the analysis of the benefits of coordinating fiscal policies (or the lack thereof) was focused on joint stimulus programmes and was based on the notion of spill-overs. If a fiscal stimulus programme in one country also stimulates economic activity in other countries and if that country does not coordinate its actions with the other countries, we are faced with a free ride. The reason is that the other countries benefit from that country's stimulus and thus may decide to reduce their own stimulus effort. This way they can profit from the externally generated expansion without having to run costly budget deficits. This free-riding behaviour creates a problem for the first country – the benefits of its stimulus programme spill over (partially) to the other countries, while it alone bears the costs of the budget deficits. The country will therefore have an incentive to reduce its own stimulus programme. If all countries reason in the same way, they will not enact sufficiently ambitious stimulus plans. These very general principles also apply when countries disengage by withdrawing from their stimulus programmes because their leaders feel constrained to do so.

In the debate about crisis 2.0 and the management thereof, the reverse logic is valid: when one country starts a policy of fiscal contraction and debt reduction, this reduces domestic economic activity and also negatively affects economic activity in the other countries. In this case, part of the cost of fiscal restriction spills over to other countries, while the benefit of the restrictive policy (which is the reduction of the budget deficit) is enjoyed solely by the first country. As a result, the other countries find themselves in a worse situation – economic activity declines and this in turn tends to increase their budget deficits. They are likely to respond by following restrictive budgetary policies thereby reducing economic activity both domestically and in the other countries. This process triggers a further deflationary dynamic that hurts everybody and complicates the task of reducing the budget deficits elsewhere.

Unfortunately, there is not much agreement either within the relevant decision-making bodies, such as the Competitiveness or Economic and Financial Affairs Councils or in academic circles, about how much and what kind of economic coordination is required. Ministers meeting in the Council of the EU collectively exercise many governmental functions, including legislation, but always with the intention, at the same time, of furthering what they consider to be their individual national interests. Jabko[43] (2011) has coined the notion of 'divided sovereignty' to capture this ambivalence.

43 Nicolas Jabko (2011), Which Economic Governance for the European Union**?** Facing up to the Problem of Divided Sovereignty; SIEPS Paper.

Governance of the EU is indeed conceived of as an ***aggregation* of national interests rather than a *disaggregation* of a European common good.** EU economic policy is not driven by an operative conception of its own common interest. **So far, there is no clear-cut conception of *the common good of a European economy*,** because there is no consciousness of a European communality and no joint model of European economics and how such an economy should and could work.

VI On the Way to a Fiscal Union?

The discussion about how best to fight the sovereign debt crisis has rolled out into two tracks: a short-term dimension to calm and soothe the financial markets and so put their unease to rest, and a longer-term reform of the economic governance structure of the eurozone and ultimately the EU as such.

Whereas the discussion of tools such as Eurobonds, the ECB 'bazooka', or other instruments belonging to the first category represents one pillar of the political debate, the second pillar deals with the creation of a fiscal union and essentially, finally, a European Ministry of Finance[44] that will steer the economic policy of the Union towards its best common interest.

What is a fiscal union?[45] According to the textbooks of public economics, a fiscal union comprises the joint determination of public activities in a market economy, i.e. public spending and public expenditures, as well as revenues, primarily. taxes and loan financing. This may include strict rules to limit sovereign debt.[46]

However, measures to streamline, coordinate, or harmonise such elements carry the risk of producing externalities and unwanted policy results.

In this respect several summits, including the one in December 2011, tried hard to find agreement on the ways and means to close the institutional gaps in the Union. Quite simply, they failed. As Simon Tilford put it so aptly: 'What has been agreed falls far short of a «fiscal union". There will be no joint debt is-

44 Jean-Claude Trichet (2011), Building Europe – building institutions, speech on occasion of receiving the Karlspreis, in Olaf Müller, BerndVincken (eds.), Challenges in Times of Crises, Aachen, pp 41-75.

45 Benedicta Marzinotto, André Sapir, Guntram B. Wolff, (2011) What kind of fiscal union? Bruegel Policy Brief No 6/2011.

46 Donatella Gatti, Christa van Wijnbergen (2002), Coordinating Fiscal Authorities, Oxford Economic Papers 54 (1), pp. 56-71.

suance, no shared budget, and no mechanism to transfer monies between the participating countries. Essentially, the agreement hard-wires pro-cyclical fiscal austerity into the institutional framework of the Eurozone, with no *quid quo pro* in terms of a commitment to move gradually to debt mutualisation. It is little more than a revamped version of the EU's existing Stability and Growth Pact.[47]

The reproach is that the heads of state and government under German-French leadership have exclusively concentrated their efforts on austerity measures. Such a strategy cannot solve the crisis but may actually pose part of the problem. As *Standard and Poor's*, the world's largest rating-agency, have voiced in their sharp criticism in the week running up to the December 2011 summit, markets may become even more unsettled when taking into account the deflationary and contractive effects from austere public savings in an already-threatening recession.

While, as Annunziata puts it, 'Requiring countries to amend their constitution sets the bar high – but it is the kind of step that would demonstrate an irrevocable commitment to fiscal discipline, and the dividends in terms of credibility would be enormous',[48] it remains to be seen whether and by how much market expectations will be impacted by this kind of approach, which may well change the risk structure, the expectations, and calculations of market participants. However, what remains dubious is the hope it might help in returning government bonds back to the realm of confidence and zero risk weight.

Admittedly, 'there is no easy way to prevent the decisions of national governments from becoming an unsatisfactory aggregate for the European Union as a whole. This could arise in various circumstances: too many governments pursuing fiscal policies that are restrictive and thus exert a collective squeeze on demand or, vice-versa that are lax, fuelling inflationary pressures; over-reliance on net exports as the principal source of growth; or a reluctance to implement politically difficult supply-side reforms.'[49]

47 Tilford Simon, EU Summit: Enough to save the euro? Friday, December 09, 2011 CER Paper.

48 Marco Annunziata (2010), Moral Hazard in the Eurozone: A Proposed Solution'. UniCredit, Economic Special.

49 Iain Begg (2011), Prevent or Cure, in: Iain Begg et. al. (2011), European Economic Governance. Gütersloh: Bertelsmann Stiftung, p. 24

VII By Way of Conclusion

The dominance of both financial and asset markets over goods markets and labour markets during the past two decades has created **a house of cards of 'overleveraged', i.e. super-credit-based national economies**. The saying, '*This house of cards has gone down – we'll bring it back'*, seems to be the order of the day in many quarters. But rebuilding this house of cards will simply not do. New business models for banks and companies and new regulatory considerations in business and society appear absolutely indispensable. *The undisputed growth model of an overleveraged, credit-based and borrowing economy will have to be revised substantially and replaced by a sound alternative.* Over the past 20 years the financial sector has boomed with hitherto unknown intensity and has become too powerful. The dominance of the financial markets spawned the *Masters of the Universe* (previously mere investment bankers) and lured policymakers into excessive public loan financing.[50] The wealth that the financial sector created and concentrated in the banking system allowed bankers to influence the political system to a degree that had never before been achieved.

Therefore, mastering the crisis means recasting the Common Good and 'reconstructing responsibility', which means transparency, control, and setting incentives correctly. Runaway speculative financial capitalism must be reshaped to become a reliable and servient means of support for business and the real economy. The traditional, old European virtues of the respectable businessman, such as reliability, honesty, dependability, long-term business relations, trust, considerateness, and continuity have been lost. This is what we will have to bring back!

The era of excessive liberalism, deregulation and privatisation – which was accompanied by the destruction of social and collective values and a development towards ignoring common goods – obviously contained the seed of its own decay. The philosophy of minimal state intervention has turned out to be a mere illusion. Massive growth and artificial profitability of the financial sector, financial innovations, economic imbalances, etc. have led to speculative bubbles on the housing, asset, and securities markets, to insolvency of households and com-

50 Between 1973 and 1985 the share of the financial sector never amounted to more than 16 per cent of US corporate profits. In 1986 it rose to 19 per cent and in the 1990s it oscillated between 21 and 30 per cent. Since 2000, this share has been about 35 per cent. This figure carries enormous weight considering that the total contribution of the financial sector to US GDP is only about 7 per cent.

panies, to undercapitalised banks, and to fragile financial markets. Eventually the saviours – i.e. the public and political agents – fell into the abyss, since the loan-financed rescue packages turned out to destroy the credibility of the bond markets. In a globalised world marked by ubiquitous *spill-overs*, Europe could not remain completely unscathed by these developments. The role of the state will have to be redefined and revised in the process. To master the crisis we *do* need a convergence of *economic beliefs around fresh ideas of a European common good.*

The crises have demonstrated the importance of a common coordinated crisis-management framework; joint action rather than free rides. What is required is:

1. *Crisis prevention* to avoid future repetition. This should be mapped onto a collective judgment as to what the principal causes of the crisis were and how changes in macroeconomic, regulatory, and supervisory policy frameworks could help prevent their recurrence. Policies to boost potential growth and competitiveness would also bolster the resilience to future crises.
2. *Crisis control and mitigation* to minimise the damage by preventing systemic defaults or by containing the output loss and easing the social hardship stemming from recession. Its main objective is thus to stabilise the financial system and economic activity in the short run. To strike the right balance between national preoccupations and spill-over effects affecting other member states, it must be coordinated across the EU.
3. *Crisis resolution* to bring crises to a definitive end, at the lowest possible cost for the taxpayer, while containing systemic risk and securing consumer protection. This requires reversing the temporary support measures and action to restore economies to sustainable growth and fiscal paths. This includes policies to restore banks' balance sheets, restructure the banking sector, and bring about an orderly policy ‘exit’, especially from expansionary macroeconomic policies.

In generic terms, we will have to strike new balances between risks and security, rewards and sanctions, consolidation and dynamics, wealth and distribution, the state and markets, finance and production, global and local, hope and resignation, equity and efficiency, macro and micro, rhetoric and practice, competition and competitiveness, trust and control, regulation and de-regulation, and euro-phoria and euro-scepticism, to name just a few.

Against this backdrop, Europe today needs a new economic strategy, a new vision for the future.[51] Its representatives must explain how they intend to foster creativity, to promote science and technology, and enhance human capital, and how they will reinvigorate entrepreneurial spirit in order to transform and modernise the European economy to create more jobs, growth and welfare. Unless Europe's leaders can come up with convincing and compelling answers, the EU is bound to lose credibility, confidence, and trust. However, it goes without saying that the vision of a renewed European economy based on an agreed common economic policy for the Union in its entirety is a tall order. It is in this very realm that Europe's common good will emerge and take shape. What is required are the three I's: ***intellectual*** rigor, ***innovative,*** out-of-the-box thinking, and ***inspiring*** visions for the future. These I's will be indispensable in the process of (re-)constructing the European common good.

ANNEX: The Ten Commandments for the Eurozone

1. **Thou shalt not live beyond your means –** no member state may exceed its deficit-to-GDP ratio of 3 per cent.
2. Thou shalt not prevent punishment – *automatic sanctions must be accepted.*
3. Thou shalt consider the interest of future generations – *introduce a national 'debt brake'*.
4. **Thou shalt honour the European Court of Justice –** which is supposed to ensure good fiscal governance and prosecute any violation of the treaty.
5. **Thou shalt not unsettle financial investors –** refrain from inflicting losses on private sector creditors (no involvement of the private banking sector).
6. **Thou shalt procure economic growth –** by means of the Euro Plus Pact and the creation of a European economic government.
7. **Thou shalt respect the independence of the European Central Bank –** don't give unwanted advice or demand bond market interventions or liquidity provision.

51 The German Daily Handelsblatt put together (in December 2011) – by way of irony – the 10 Commandments for the Eurozone which the author has attached in this Annex. He is sure, however, that these Commandments do not represent what may be considered the European Common Good!

8. Thou shalt not seek your neighbour’s money – *no Eurobonds.*
9. **Thou shalt listen to what the large national economies demand –** the leadership role (directorate) of Germany and France has to be acknowledged.
10. **Thou shalt serve the new ‘core Europe' –** the eurozone is the exclusive new frame of reference.

Table 1: Chronological Order of the Crisis

2007	United States/World financial crisis: the collapse of the US housing bubble had dramatic consequences on financial institutions on a global scale. Economies worldwide slowed during this period as credit supply tightened and international trade declined.
2008 September	Lehman brothers filed for Chapter 11 bankruptcy protection on 15 September 2008. This bankruptcy is considered to be the trigger point of the global financial and economic crisis. It sparked ‘contagion’ and a massive liquidity shortfall in the US and EU banking systems.
2008 -2009	The EU was hit hard by the fall-out of the banking crisis, and as a consequence almost all member states suffer from severe economic recession.
2008 November	On 26 November 2008 the European Commission proposed a European Stimulus Plan amounting to €200 billion to cope with the effects of the global financial crisis on the economies of the member states.
2009 February	Publication of the De Larosière report. A high level working group chaired by former managing director of the International Monetary Fund and former governor of the Bank of France, Jacques De Larosière, produced its findings on how to reform financial supervision in Europe.
2009 September	The European Commission suggested measures for a new European financial supervisory architecture.
2009 October	Trying to hide within the economic turbulence in the wake of the

	crisis, the Greek government announced that its deficit figure for 2010 was 12.5 per cent, three times the amount officially acknowledged previously.
February 2010	Under market pressure, the Greek government launched a severe austerity package in order to control the fall-out on bond markets.
11 February 2010	Harsh debates occurred in the European Council about the consequences of the Greek situation: prevent contagion, avoid bail-out discussion, and revise the Stability Mechanism. Heads of state and government declared their willingness to support Greece if it so desired.
25/26 March 2010	European Council Conclusions called for the establishment of a Van Rompuy Task Force to draw up measures to improve economic governance in the eurozone. The Task Force held its first meeting on 21 May 2010.
2010 May	Peak of Greek sovereign debt crisis, and the Council decision to 'save' Greece by adopting the European Financial Stability Facility (EFSF) and the European Financial Stability Mechanism (EFSM).
29 September 2010	The European Commission submitted six legislative proposals – the so-called 'Six-Pack' – to strengthen economic governance: broader macroeconomic surveillance and greater fiscal discipline.
18/19 October 2010	At the Deauville Summit a Franco-German deal was hammered out. Germany accepted less automated sanctions in exchange for a French concession to support the eventual changing of the EU treaties to create a new, permanent mechanism to manage future (Greek-style) bail-outs.

21 October 2010	The final report of the Van Rompuy Task Force was submitted to the European Council involving: (1) broader macroeconomic surveillance, (2) greater fiscal discipline in the form of a stronger and more efficient Stability and Growth Pact, (3) deeper and broader policy coordination, e.g. the European Semester, (4) a more robust framework for (financial) crisis management, i.e. the temporary European Financial Stability Facility (EFSF) and the European Financial Stability Mechanism (EFSM) to be turned into the permanent European Stability Mechanism (ESM), and (5) stronger institutions such as the European System of Financial Supervision (ESFS).
28 October 2010	Heads of state and government agreed upon the setting up of a permanent crisis mechanism (ESM), supposed to replace the EFSF. Merkel declared: We have taken the necessary decision and can, from this moment on, guarantee the stability of the euro in perpetuity!
21 November 2010	Irish crisis due to unlimited bank guarantees through public money forced Ireland under the rescue umbrella. The European Financial Stability Facility lent money to Ireland with conditions attached. Van Rompuy issued caution regarding exaggeration of the fiscal fragility of Portugal.
1 January 2011	The European System of Financial Supervision (ESFS) was set up, comprising: the European Systemic Risk Board (ESRB), and the three European Supervisory Authorities (ESAs), namely the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA), the European Securities and Markets Authority (ESMA) and the Joint Committee of the European Supervisory Authorities (ESAs).
12 January 2011	The European Commission presented its first Annual Growth Survey, marking the start of the first European Semester, a procedure by which the Commission can monitor and control the budget planning of individual member states.

4 February 2011	European Council Summit adopts the Franco-German Competitiveness Pact – later called the Euro Plus Pact – signed-up by 17 eurozone members + 6 EU member states.
11 March 2011	Extraordinary eurozone summit to identify priorities for structural reforms and fiscal consolidation.
24/25 March 2011	Final decision on the limited treaty change and the setting up of the European Stability Mechanism by the heads of state and government
8 April 2011	Further to a call for help from Portugal, the EU establishes a €80 billion rescue package.
20 June 2011	Finance ministers agree on an enlargement of the EFSF: in order to enable the facility to hand out loans up to €440 billion, guarantees have to be increased to €750 billion. Germany considers this move indispensable: 'If the euro fails, Europe fails!'
21 July 2011	Heads of state and government decided to increase the financial support to Greece by up to €109 billion. The private sector creditors joined in with a 'voluntary' contribution of €37 billion.
26 October 2011	After hefty discussions among both the heads of state and government of the eurozone and the EU, Greece received a debt relief of 50 per cent. The private investors realised losses of 50 per cent vis-à-vis the nominal value of Greek bonds. European banks were forced to increase their core capital share to 9 per cent and the EFSF was supposed to be 'leveraged' up to €1000 billion. France claimed: There was a risk of implosion; this is our credible and compelling answer!
8/9 December 2011	Heads of state and government endorsed a series of rules tightening budget surveillance and setting limits to public spending: the 'fiscal compact'. The key element is a 'golden rule' enforcing balanced budgets defined as deficits not exceeding 0.5 per cent of GDP to be inscribed in domestic constitutions. The European Court of Justice has been tasked with monitoring the transposition into national law. Countries breaching deficit rules would be subject to 'automatic consequences' unless a qualified majority of states decided other-

wise. Members of the eurozone are obliged to submit their budgets to the EU Commission before they are discussed in national parliaments. The whole package is supposed to be the launching pad of a fiscal union and a means to regain the confidence of financial markets and investors.

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