REFORM PROPOSALS FOR THE EURO ZONE

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This Tribune by Jacques Delors and Henrik Enderlein is based on the main findings of the report of the Tommaso Padoa-Schioppa's group. It is inspired by an article published in the German newspaper *Die Zeit*.

Within the European Monetary Union, what were once long-term challenges have suddenly become urgent. After the allocation of urgent aid in return for reforms, the issue of the euro zone's structure has finally taken the front seat. But this begs another question: to just what degree are political union, fiscal union and solidarity necessary in order to ensure that the common currency is successful?

This crisis is not about the euro; its origin does not lie in the single currency. It is a crisis that has been triggered by differences over the economic policy to be pursued in the effort to get different national economic systems to coexist with a single currency. There are two ways of causing those differences to disappear: either Europe returns to a series of different currencies, which would threaten the future of the European single market and, with it, the future of the common project for political integration; or else it succeeds in blending the different national economic systems to a degree sufficient to allow the euro to function properly as a single currency.

This second option is often confused with some kind of blueprint for a European "superstate". That is not the object at all. It would be far more beneficial for us to ask ourselves, in pragmatic terms, what supplementary measures on the path to integration need to be adopted in order for the euro to function properly.

That is precisely the question that a report just published in German, but already available in English and French, seeks to answer. Entitled "Completing the euro", it was put together by a group of which we are members, the "Tommaso Padoa-Schioppa Group" which is named after one of the founding fathers of the Monetary Union. We do not argue in the report for some kind of dogmatic solution to overcome the euro crisis. If we want to drum up broad support for the next stages in the integration process, what we need is political pragmatism rather than any dogmatic solution: we need to build as much additional "Europe" as necessary, to tackle the emergency, but as little as possible.

The first challenge lies in the tension between a key factor in European integration – the internal market – and the major structural differences within Europe. The single market is not compatible with fluctuating exchange rates because that would still make it possible for countries to recover their competitive advantage in the short term through devaluation. Thus the blueprint for a common currency was the practical and logical answer for the single market. Unfortunately, the first decade of monetary union has clearly demonstrated that, contrary to initial expectations, the common currency has not led to stronger convergence among its member countries. Price differences within the euro zone have increased rather than decreased. Thus the key interest rates set by the European Central Bank have never actually been suited to any of the member states. Those interest rates have had damaging and even pro-cyclical effects, which have even tended, in most of the member states, to be self-reinforcing. This situation has led to excessive imbalances and to cyclical divergence within the euro zone. The ECB has been pursuing and implementing a policy for a country that does not exist.

To meet this challenge, it is necessary first and foremost for us to continue to pursue the completion of the internal market. A totally integrated commercial area is necessary in order to implement a more effective common monetary policy and to strangle any hint of cyclical divergence in the cradle. Not only is the service industry still rooted in the national sphere to the tune of 80%, but the free movement of people across borders also encounters a number of obstacles: pension rights, for example, are very difficult to transfer from one country to another.

In parallel with these measures designed to strengthen the internal market, it is also necessary to compensate for a part of the cyclical disparity existing within the euro zone. This has been achieved in the United States, and even in Germany, thanks to a common taxation system or to a common form of unemployment insurance. Such advances may appear desirable to convinced pro-Europeans, but they are not at all urgent. In our report, what we propose to set up is a stabilisation fund designed to counter excessive cyclical fluctuation. Countries enjoying a boom would contribute to the fund while those in a recession would benefit from it. In a system of this kind, over the longer term, transfers do not occur in a one-way direction only. For instance, if the system had existed over the past ten years, Germany would have benefited from it in the years in which its growth rate slowed down at the start of the last decade, and while Ireland and Spain were both enjoying a boom, they would have contributed to the fund and prevented their national economies from spinning out of control. Today the situation would be in reverse. Such a system would reduce cyclical divergence within the euro zone and it would thus ensure that the ECB's monetary policy would become more effective.

The second major challenge lies in the tension between independence in the field of fiscal policy and coordination within a monetary union. How far does a country's national sovereignty in deciding its own budget policy extend if all of the other member states in the currency zone are going to be impacted by those decisions? We are not advocating the total transfer of fiscal policy to the European level, simply a temporary arrangement.

Under normal circumstances, each country would be independent in forging its budget policy, in accordance with the established regulations in the sphere of fiscal policy within the euro zone. However, if a country's debt were to spin out of control, another mechanism would have to be adopted. In this connection, the report suggests that in a monetary union, a member state's sovereignty ends when its solvency ends.

In practical terms, that would mean that when a country no longer has access to a financial market, it would gradually transfer its sovereignty in the field of fiscal policy to Europe in return for financial aid: the greater its financial dependence on Europe, the broader would be Europe's scope for intervention.

We also propose the establishment of a European Debt Agency (EDA). Unlike the ESM, such an agency would facilitate the gradual relinquishing of sovereignty, while simultaneously creating incentives designed to foster the return to a responsible fiscal policy. This agency would be guaranteed at the Community level and it would issue common bonds in perfectly measurable proportions. The figure we mention in the report entails funding to the tune of 10% of each euro zone member country's GDP. That would allow Germany, for instance, to continue to maintain over 80% of its public debt in the form of state-issued bonds. But at the same time, the European bond market would become far more liquid. The advantage of the EDA would be that a country which no longer has access to the short-term financial market could obtain funding rapidly and flexibly through European bonds. As an offset, it would have to agree to the gradual transfer of its sovereignty. In extreme cases, countries that have a debt exceeding 60% of their GDP, as the Maastricht Treaty rightly stipulates, could adopt their budget only with the agency's agreement. A process of this kind requires a strong democratic base. We believe that parliamentary supervision of the agency should fall to a mixed committee comprising representatives of both the national parliaments and the European Parliament.

We consider it important to improve the interplay between Community responsibility, shared sovereignty and democratic supervision. Our proposals, which should be seen as supplementing the establishment of the banking union currently under way, could form the basis for a political compromise between those who are opposed to any kind of Community responsibility and those who are opposed to the transfer of sovereignty. In our view, these proposals represent "federalism by exception". Community responsibility would not be the rule, it would be an exception in return for the relinquishing of sovereignty.

There have always been political motivations behind the euro. The common currency is rooted in the belief that trade generates greater wealth and greater exchange among the countries taking part in it. That is why, at this juncture, it would be beneficial to complete the euro through rapid-impact reforms and through a political compromise regulating shared sovereignty in the euro zone.

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