European Union: From relaunch to stagnation
The role of States in European Economic and Monetary Integration

by

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Summary

The aim of this study is two-fold: First it seeks to carry out a critical analysis of the creative imbalance model which underpinned the European Monetary Unification project (EMU). The second aim of the present study is to highlight the role of states as a driving force in the process of European integration, with respect to macro-economic policy. Our study shows that the European monetary unification is by no means the product of institutional dynamics—initiated by the European Commission and propelled forward by liberalization of capital flows—as conceived by the creative imbalance model. As a matter of fact, the attitude of European states – in particular the most powerful – explains both the ebb and flow of the integration process. The current blockage in integration is due to the reluctance of states to assume the costs of deeper coordination of the European policy mix. The attitude of European states is due to the close connections between fiscal policy and the political make-up of nation states. Such close links make it very difficult to achieve significant coordination of the European policy mix without first progressing towards political union in Europe. Financial globalization and its corollary – the rise in neo-liberalism – contribute holding back the integration process notably by encouraging a divergence of interests between Europe’s multinational capital and greater European integration.
The relaunching of the European integration process, which paved the way for monetary unification, started with the Single European Act (SEA) of 1986 (Lelart, 1994). The new departure came after 10 years of inertia largely encouraged by the downturn in the European economy following the first oil crisis. “Europessimism” and “Eurostagnation” had undermined the spirit of solidarity – essential to the original ethos of European integration – and prompted new forms of protectionism, sidelining supranational Community bodies, in particular the Commission. The signature of the SEA treaty marked the start of an upward surge culminating in the establishment of the European Central Bank (ECB) and the single currency. However, since the launch of the euro the process of European integration has lost momentum, particularly in economic policy.

The Treaty of the Single European Act relaunches dynamics of European integration by abolishing all barriers relevant to the movements of products (Single market) and financial services and by providing freedom for the establishment of credit institutions (European financial area). The Treaty of the Single European Act also stipulates complete liberalization of capital movements. The liberalization of capital flows not only concerned the residents of the European Union, but also non-European capital.

According to the advocates of the reforms enshrined in the SEA the new impetus was inspired by the creative imbalance theory (or the engrenage concept). This model assumed that SEA reforms – in particular complete deregulation of capital movements – would act as a driving force toward European monetary union. According to this theory unfettered movement of capital, as “conceived” by the European Commission would – by virtue of Mundell’s incompatibility triangle – make the European Monetary System (EMS) obsolete and the single currency a necessity. Unifying monetary policy would in turn lead to unification of other aspects of economic policy, on account of the costs involved in a policy mix under which only monetary matters were centralized. European states would find themselves mechanically drawn into a dynamic that was beyond their control resulting in a gradual reduction of their powers. Thus, by “entrapping” participating states, increased European integration would be gradually encouraged through successive stages thereby allowing – in the final phase of the process – substantial progress towards political integration as well.

The aim of the present study is two-fold. First it seeks to carry out a critical analysis of the creative imbalance model which underpinned the stimulus measures of the1980-90s, touching on the process of European economic integration itself. Our study shows that the European monetary unification is by no means the product of institutional dynamics—initiated by the European Commission and propelled forward by liberalization of capital flows—as conceived by the creative imbalance model. On the contrary deregulation of capital flows contributed to integrating the European space in the process of financial globalization, a factor which ultimately contributed to sapping the process. As the process of Europe’s economic integration advanced, it also emerged that harmonising monetary policy had not produced the results predicted by the creative imbalance model, with respect to greater coordination and/or harmonization of other branches of economic policy.

The second aim of the present study is to highlight the role of states as a driving force in the process of European integration, with respect to macro-economic policy. Our analysis shows that the attitude of European states – in particular the most powerful – explains both the ebb and flow of the integration process. The new impetus of the 1980s and 1990s was the result of a geo-economic compromise between the two most powerful European states: recognition of
German reunification by France as a trade-off for Germany’s acceptance of the single currency project supported by France. The stimulus also served the interests of European investors.

The current blockage in integration is due to the reluctance of states to assume the costs of deeper coordination of the European policy mix. The attitude of European states is due to the close connections between fiscal policy and the political make-up of nation states. Such close links make it very difficult to achieve significant coordination of the European policy mix without first progressing towards political union in Europe. Financial globalization and its corollary – the rise in neo-liberalism – contribute holding back the integration process in two ways: first by encouraging a divergence of interests between Europe’s multinational capital and greater European integration; secondly by helping to turn – under pressure from European states – European institutions into vectors driving neo-liberal reform in Europe. This trend has fuelled public opinion’s growing estrangement with European integration.

The dynamics of the project for European Monetary Union according to the creative imbalance theory: the driving role of supranational institutions and of spillover effects

There are two major approaches as regards the European integration model: the creative imbalance model and the intergovernmental approach (Van Apeldoorn, 2002; Nollert and Fielder, 2000; Grieco, 1995; Corbey, 1995; Sandholtz and Zysman, 1989).

The creative imbalance model, which inspired the re-launching of the European integration process, derives from neo-functionalist theory. This theory, connected with the liberal tradition, confers fundamental value on supra- and trans-national players, which are considered the driving forces of the project.

The creative imbalance theory considers that the European integration process consists of successive stages: the Common market, the Single market, the European financial area, the single currency, etc.. The completion of each stage implies substantial transformations of the European economies. As a result, this would make any retreat from the integration process very costly. Coherence and consolidation at each stage are subordinate to the achievement of additional advances involved in the following stage. If at some point the dynamics are broken, previous achievements are weakened. Accomplishment of successive stages implies national states increasingly renouncing their sovereignty.

The creative imbalance model perceives the European Monetary Unification (EMU) project as a self-sustaining process with a federal rationale. This process is initiated by reforms of the SEA “conceived” by trans-national institutions, especially the European Commission, and European trans-national capital—with its driving force technocratic rationality.

Thus, the liberalization of capital movements and financial services by the European Commission in 1986 is instrumental for the Single market. In a context of free capital flows, the autonomy of monetary policies becomes incompatible with the stability of exchange rates (“incompatibility triangle”). According to the creative imbalance model, this entails the following two choices for the member states, both of which are unacceptable: accept a loss of control over national monetary policies, should priority be given to the preservation of the EMS; or take the risk of “competitive” devaluations, if preference is given to the control over national monetary policies. “Competitive” devaluations would destabilise the EMS and
jeopardise the Single market, by creating distortions in international competition. The imminent deadlock would quite naturally lead to monetary unification.

Centralization, focused only on monetary policy, would ultimately imply economic costs. These could threaten the single currency, unless European states decide to make substantial progress in harmonizing or even centralizing the other components of economic policy (Sifakis, 1998). The costs are relevant particularly to asymmetric shocks occurring in the context of a monetary union. Centralization of monetary policy should result in a loss of capacity for member states to employ demand-side stabilization policies. Both the well-regulated functioning and the viability of the monetary union make collective cost sharing necessary. The participating states would thus be led to take additional steps toward fiscal federalism and coordination (even centralization) of budgetary policy. Thus, by “entrapping” the states, the deepening of European integration would be favoured with substantial progress in political integration as well.

The creative imbalance model considers spillover effects fundamental. To provide some insight regarding their creation, three categories of these effects can be distinguished:

° Spillover effects on the monetary policy level, resulting from liberalization/deregulation measures relevant to the application of the SEA (from the Single market and European financial area to the single currency);
° Spillover effects affecting the European policy mix (from the unification of monetary policies to the coordination/centralization of other components of economic policy); and
° Spillover effects on a political level (from coordination/centralization of economic policies to political integration).

These categories of spillover effects do not imply the same difficulties, stakes, or institutions for their implementation.

Within the first category of spillover effects the liberalization of capital movements plays a key role. Indeed, the pressure of international capital flows imposes constraints on national economic policies, by weakening their stabilizing capacity. These constraints make European monetary unification “necessary”. The “external constraint” thus becomes more than a major argument for the necessity of monetary unification; it becomes a “self-realising” prophecy. In this way, the presumed inability of Europe to resist the globalization process (Delors, 2004: 203) is used as an argument to accelerate the impact of globalization through complete liberalization of capital movements. By producing the anticipated effects on national economic policies, this impact favours the project of European monetary unification, which would pave the way for coordination/centralization of the weakened national economic policies. This is well articulated in Michel Aglietta (1990). He analyses the reasons for which perfect capital mobility is a sine qua non condition for the establishment of a supranational central bank. He then discloses how the monetary union allows European states to regain fiscal autonomy, otherwise lost at a national level, due to constraints on the balance of payments. In concluding, he emphasizes dangers associated with financial liberalization already in process, if this is not accompanied by monetary unification.

Contrary to the theory of creative imbalance which posits the key role of the Commission and spillover effects in the process of stimulating European integration, our analysis highlights the essential role played by members states as a driving force in this process.
The actual dynamics of the EMU process (1986-1992): the crucial role of states and of the balance of power

The project of the European monetary unification emerged for the first time in the Werner Report in the early 1970s. The Werner Report suggested that the accomplishment of the monetary unification be achieved by the end of the 1970s. This report however did not reflect any consensus among the European states. On the contrary, the negotiations following the report publication revealed the extent of disagreements over the opportunity of a single currency. They reflected contradictory positions defended by countries with a “strong” currency (Germany and the Netherlands), and countries with a “weak” currency (France). The former considered structural convergence and convergence in levels of development among member states a precondition for the monetary unification of Europe, thus postponing it far into the future. On the other hand, countries with a “weak” currency supported a monetary “big bang” supposedly leading to convergence. This opposition among European countries—concerning the conditions and timing necessary for the European monetary unification—persisted until the elaboration of the Maastricht Treaty.

Monetary union became a real European project when Jacques Delors was appointed to chair the Commission in 1984. This appointment reflected France’s determination to give new impetus to the process of European monetary integration.¹ It is worth noting that Jacques Delors, supporter of the federalist conception of the European integration, was François Mitterrand’s first Minister of Economics and Finance. After his appointment, Jacques Delors took monetary affairs in hand, dissociating them from economic affairs “for the first and only time in the history of the European Commission” (Delors, 2004:193). Furthermore, the single currency project was one of three proposals for relaunching European integration then presented—in a context of advanced crisis of the Soviet bloc—to the heads of European governments. The lack of consensus on this project led him to propose for realization of the large internal market (ibid, 185). “This [large internal market] was a fulfilment operation, but Delors connected it with a broader objective of being a stepping stone to an economic and monetary union” (Hoffmeyer, 2000: 61).

For France, the single currency was the monetary system compatible with the smooth operation of large internal market (contrary to the floating of currencies) and one that also coped with the asymmetric functioning of the EMS to the benefit of Germany. Mitterrand is reported to have said to German Chancellor Helmut Kohl in December 1985: “The internal market without currency makes no sense” (Attali, Verbatim T. 2, 1995, quoted in Hoffmeyer, 2000: 61). On the contrary, the Germans were not ready to share their economic and monetary supremacy and were in favour of a common defence policy—a project hidden behind their demand for “political” unification of Europe, with which France did not agree. (Attali, Verbatim, T. 2, 1995: 365; and T. 3, 1997: 454)

Given France and Germany’s divergent positions, French acceptance of full deregulation of capital transfers represented a concession. In exchange France hoped to obtain concessions on the single currency. Prior to Delors’ appointment, liberalization of capital flows, supported by Germany, was rejected by France along with other European countries with weak currencies, in particular those of Southern Europe. The single currency project substantially contributed to altering the French position, and, subsequently, the position of less developed countries, thus rendering the liberalization of capital movements feasible. The French reversal was crucial to the liberalization process, since France represented one of the two driving forces of European integration. Moreover, France had always been the rampart of the
intergovernmental conception for European integration, opposed to the federalist conception—the latter being the "preferred habitat" of the defenders of economic liberalization mechanisms, Germany in particular.

Delors himself initiated this reform. “I mean that the advance of the project for an “economic Europe” could not be realized without accepting the risk of imbalance. This measure [complete liberalization of capital movements] gave both great momentum and credibility to the overall project. It was one of the major building blocks [.....]. Considering what was going to happen after the European Monetary System, it was important to set up this essential pillar of the borderless market” (Delors, 2004: 203).

The threat of disputing the liberalization of capital movements was used, by France, in order to obtain concessions regarding monetary unification from 1987, when the SEA was enforced until 1992, which was the deadline for reform completion (Hoffmeyer, 2000: 77). However, this threat was not sufficient to reach a consensus about the EMU project. It was the upheaval of the European geopolitical context, in the late 1980s, that led Germany to accept the single currency project in exchange for the recognition of its reunification by France in particular. Indeed, to appreciate the real chances of success of this project without the impact of this true “revolution”, one should not consider the formal position of European countries, especially that of Germany, which has always stood in favour of European monetary unification. It is important to determine whether there existed a consensus at the time about the prerequisites and the time limits necessary to implement the project. This consensus does not seem to have emerged prior to the European geopolitical upheavals in the late 1980s (especially 1989).

Contrary to the neo-functionalist conception (Sandholz and Zysman, 1989), supranational players—European Commission and the transnational elite of major European companies—did not play a decisive role in the re-launching of the European integration.

The true decision-maker with regard to new policies in Europe, is the Council of the Heads of State or Government (European Council) and not the European Commission. The Commission cannot submit formal proposals to the European Council, but only communications and reports (Bertrand, 2002: 33). The Delors Report (1989) proposing the creation of the European economic and monetary union was mandated by the European Council. It was also the European Council that convened the intergovernmental conferences that culminated in the Single European Act and the Maastricht Treaty. The analysis of the decision-making process within the European Community’s governing bodies also reveals that the members of the Commission have no real independence from the governments of the member states (Quermonne, 2005: 34).

Furthermore, the relaunching of European integration was not primarily the outcome of pressures deriving from European industrial capital—though its most internationalized components benefited from this re-launching and, consequently, obtained increasing influence on European governance. The supposed crucial influence of various lobbies in the re-launching process—especially the one exercised by the European Round Table of Industrialists, referred to by many studies (Nollert and Fielder, 2000; Van Apeldoorn, 2002) —is exaggerated. Indeed, corporate CEOs from non-member countries took part in this Round Table (Turkey, Switzerland and Norway), and companies from the smaller countries were overrepresented. Additionally, consumer goods companies, mainly targeting the internal market, were over-represented (Nollert and Fielder, 2000). Finally, players other than major European community industrialists seem to have played a crucial role in setting up this Round
Table, which was in fact initiated by both the Belgian Etienne Davignon, European Internal Market Commissioner at the time, and Gyllenhammar, the CEO of Volvo.

The European monetary unification project is the outcome of a strong political will from some European states and of an interstate geo-economic bargaining. However, contrary to the majority of the analyses based on the intergovernmental approach, inspired by the neoclassical model, we consider that states have a class nature. This should be taken into account, to understand their choices in international relations. For instance, defending the interests of German and Dutch industrial capital motivated the strong support of Germany and the Netherlands to the Common market project. Nevertheless, states also defend geo-economic and geo-political interests that transcend economic interests of dominant social classes and strata. Thus, the asymmetric operation of the EMS to the profit of Germany, which transferred the burden of parity adjustment to the weak currencies, was not only costly for France as “an economic and social formation”. It also weakened the French position in relation to Germany. It actually affected its great power image, and its capacity to draw benefit from such a status. The objective of disputing this asymmetric operation generated French proposals toward a stronger “communitarization” of the monetary policy in Europe during the 1980s. Germany accepted introduction of the single currency because it needed France to recognize German reunification.

Monetary union was the last major decision taken by European states to further integration of economic policy. Since introduction of the single currency the integration model has lost its impetus, which relied on states acting as a driving force. It was this force that underpinned European integration from the Treaty of Rome onwards.

**Backtracking by states and exhaustion of the policy mix centralization process**

In a context of financial globalization monetary policy plays a key role. Among the various branches of macro-economic policy monetary policy is the easiest to centralize. Its implementation opened the way for monetary union in the 1990s.

Since the single currency was introduced the process of economic integration in Europe has been running out of steam, a trend reflected, in particular, in the inability to harmonize at a higher, Community level, the national policy mixes, contrary to what was predicted by the creative imbalance model. This inconsistency explains the hybrid nature of the eurozone policy mix. Monetary policy is centralized in the hands of an independent central bank. National budgetary policies are preserved but subject to severe restrictions under the 3% limit set by the Stability and Growth Pact, in the framework of a very limited development of budgetary federalism. European states remain free to deploy the fiscal policy of their choice.

The hybrid nature of the European policy mix is a factor driving differentiation and even increased heterogeneity in macro-economic policy across Europe, particularly with respect to fiscal policy. Centralizing monetary policy in the hands of an independent central bank deprives member states of the use of two key instruments – interest rates and exchange rates. Centralizing only monetary policy – given the low mobility of the labour factor, the resistance to downward pressure on wages and the 3% limit set by the Stability Pact – restricts any form of leverage to fiscal policy. This trend encourages “beggar-my-neighbour” behaviour, with European states attempting to make their national space more attractive by lowering fiscal pressure, which in turn benefits the most mobile production factors, in particular the capital
factor. The upward tendency of the euro against the dollar since 2002 encourages this trend too. Fiscal competition also poses the problem of the sustainability of taxes on the least mobile factors and involves the risk of reducing the fiscal attractiveness of all European countries (snowball effect). Lastly it damages the political unity of the EU.

Setting up a consistent European policy mix requires greater coordination of budgetary policy, the development of budgetary federalism and substantial harmonization of national fiscal policy (Van der Ploeg, 1993; Walsh, 1993; Walsh, Reichenbach et alii, 1993). Federalist theory posits that of the three recognized functions of economic policy – allocation of goods and services, redistribution of income, and stabilization policies – the last two should be controlled by the central power. In the case of the European Union this would mean centralizing redistribution and stabilization functions. Regarding fiscal policy many studies have concluded that the optimal level – between federalism and devolution – is achieved when certain taxes are centralized. Given the externalities related to national economic policy, in the absence of actual centralization, at least some coordination seems necessary.

In the least centralized OECD countries expenditure by central government represents at least 30% of GNP. In the United States the federal budget exceeds the total budget of states and local authorities. Expenditure on goods and services by federal government accounts for about 40% of such expenditure by public bodies. Looking more specifically at expenditure linked to the stabilization function, Sachs and Sala-i-Martin observe that in the United States when a fiscal region suffers a real drop in its GNP following a downturn, federal transfers compensate 40% of the loss, mainly thanks to the progressive nature of income tax. In contrast Europe’s Community budget is minute (Wyplosz, 1990:170). It does not exceed 2% of the GNP of member states.

Obviously greater coordination of economic policy in Europe would involve major difficulties (Sterdyniak and Villa, 1993: 312). The first relates to the large number of jurisdictions concerned by the coordination process, namely the ECB and the many national budgetary authorities. The second is due to the risk of asymmetry in the perception of the nature of economic shocks by the various authorities involved in the process. The risk may be considerable given the diversity of the shocks with which European countries can cope.

The increased budgetary federalism would require a transfer of resources from member states to the European budget. This would enable, in particular, stabilization policies to be deployed at a European level or indeed transfers to be made in the event of asymmetric shocks.

A large part of the cost of transferring resources from member states to the Community budget would be borne by the most highly developed EU countries, given the current structure of resources and budget expenditure. A large share (about 70%) of the EU’s budget resources come from contributions by member states proportionate to GDP. In turn most of the expenditure by the EU budget consists of expenditure related to the Common Agricultural Policy and Regional Policy – respectively 46% and 40% of the total. This expenditure mainly benefits countries with the least well developed economies. The share of developed countries in budget resources being larger than their share of expenditure they are net contributors to the EU budget. The structure of resources and budget expenditure is the result of compromises reached among European states during the negotiations leading up to the start of the Common market and subsequently the Single market. The position of the richest EU countries, which are net contributors, explains their negative attitude regarding increased coordination of budgetary policy. Setting up the Stability Pact was an expedient, resulting from these
countries’ reluctance to move towards greater coordination of EU budgetary policy. In the absence of a transfer system, the lack of any framework for budgetary policy could act as an incentive for cross-the-board “excessive” budget deficits.

Intermediate levels of budgetary federalism are possible – halfway between the current EU system and federal states. In particular it has been proposed to set up – in the absence of a significant federal budget – automatic stabilization mechanisms paid for by member states to compensate asymmetric shocks. Such mechanisms would not be costly – less than 1% of contributing countries’ GDP – and though wielding less stabilizing power than in federal states, they would nevertheless be significant (Muet, 1995). Other, more recent proposals advocate better organization of eurozone economic policy, with for instance the setting up of an Economic Policy Council bringing together eurozone finance ministers. This council would enjoy decision-making powers over budgetary policy orientations and the overall thrust of economic policy in the eurozone. Council decisions would not be legally binding, given the treaties currently in force. But non-compliance would nevertheless carry “on account of the transparent, official nature of decisions, high political costs in terms of reputation and credibility” (Jacquet, and Pisani-Ferry, 2000: 31).

Contrary to the costs of greater coordination of budgetary policy, the cost of harmonizing fiscal policy would be borne mainly by the least developed EU countries. In their struggle to catch up, the smallest nations resort to fiscal competition, often followed by their more powerful neighbours. The smaller countries are therefore hostile to any significant attempt to harmonize fiscal rules, particularly with respect to capital taxation.

The blockage in the process of integrating macro-economic policies coincides with many other signs that European integration is running out of steam. First the size of the European budget is rather in decline, whereas the perimeter of the Union and the eurozone is spreading with the arrival of new members, in particular from central and eastern European countries, which to make matters worse have a far lower level of development than the European average. Secondly supranational European institutions are growing weaker, particularly the Commission. Successive waves of enlargement have almost doubled the number of Commissioners, making collegial government increasingly difficult, despite the fact that the Commission’s legitimacy is based on precisely this form of government. Its political prerogatives, primarily the monopoly over political initiatives, is being steadily reduced. The Commission is becoming increasingly renationalized, gradually turning into a committee consisting of the Permanent Representatives of the Member States responsible for preparing the work of the Council (Dehove, 2001: 71). Beside these changes there is a lack of vision for a common future, despite Europe continuing to suffer sluggish growth compared with other major centres of the global economy. Lastly the financial crisis is accentuating the drift in the integration process, encouraging an increasingly domestic outlook, and even protectionism which threatens the basis of the Single market itself.

The obstacles in the way of better coordinated organization of the European policy mix

Until now it has been the European states that have provided the impetus driving European integration. All the major advances in the process of economic integration reflect strong political determination. The current blockage in the process of integration through the policy mix reflects the lack of willpower among member states to bear the costs associated with such integration. For the most part these costs relate to the development of budgetary federalism.
European monetary union has also involved substantial costs for nations with a strong currency, in particular Germany, obliging it to abandon the Deutschmark, the flagship currency in the EMS, and its overall control of monetary policy. However the geopolitical concessions it obtained in exchange largely compensated such costs, which would not be the case now with greater coordination of the European policy mix.

One of the obstacles holding back the development of budgetary federalism is the fact that such development impinges on key attributes of the nation state. It would require EU states to abandon a substantial amount of sovereignty. The nature of political power itself and the main issues at stake hinge on raising and allocating taxation. “Taxation expresses and nurtures political sovereignty; it has gradually imposed parliamentary representation, making parliament the place where budgetary and fiscal policies are framed” (Delessy, Fourmann, Harasty, Lerais, Sterdyniak, 1994: 21). Nations states constitute a space in which various forms of solidarity are deployed. Such solidarity, which has taken time to develop, is the result of social struggle and is rooted in a community of language, culture and history. The first obstacle in the way of any transfer of sovereignty, as part of greater budgetary federalism, is the resistance of competent national bodies – national parliaments and governments – determined to protect their powers. The second hurdle is the as yet limited legitimacy of European institutions in the eyes of European public opinion. This shortfall in legitimacy is due to inadequate control exerted by the European Parliament over the executive (the Commission), on the one hand and on the other, over the EU budget. The Parliament only has an advisory role in a large number of fields. Furthermore, mandatory expenditure, on which Parliament is not consulted, represents the lion’s share of expenditure.

The obstacles in the way of greater coordination of the policy mix lead to the conclusion that there is little chance of achieving a satisfactory organization of Europe’s budgetary and fiscal policy in the foreseeable future.

Several factors may be cited to explain the almost complete lack of progress towards this goal. First the powerful redistributive bias, which benefits less developed countries, makes it difficult for the most prosperous countries to accept the introduction of stabilization mechanisms. Secondly, there is a widespread fear that, through some ratchet effect, any attempt to rationalize the European policy mix will lead the richest countries to increase their solidarity contributions beyond an acceptable level. The engrenage concept, which was supposed to reflect the positive dynamic driving European integration in 1986-92, could, if turned on its head, prove to be a useful tool for analysing the current deadlock in integration!

Lastly globalization and the growing control over European states exerted by multinational capital is contributing to the current blockage in the process of integrating the European policy mix. In addition to geopolitical considerations, the attitude of states to key decisions on the regional integration process is guided by the will to defend the interests of the dominant social classes. But states also enjoy a degree of autonomy with regard to these interests, depending on the balance of power between capital and labour, and between factions within the dominant social classes.

During the prosperous post-war years managerial capitalism was based on a vast compromise between the owners of the means of production, on one hand, and the working class and managers, on the other (Stockhammer, 2004). This configuration of the power structure enabled the state to broaden the scope of its action. General de Gaulle agreed to the Common
market despite the misgivings, even hostility, of French industrialists at the time. He did so, not only because he had obtained concessions in exchange, in particular on the Common Agricultural Policy, but also because he was convinced that European integration would serve the long-term interests of French business.

The current period has witnessed a relative decline in the power of European states, primarily due to monetary union, which has deprived states of substantial economic policy leverage. Europe’s integration in the process of financial globalization – made possible by the deregulation of capital transfers enshrined in the SEA – is an additional factor in European states’ decline. Deregulation does not only concern residents but also foreign (non-European) capital, without any form of reciprocity being demanded, whereas in fact only the deregulation of European capital transfers was needed to establish the European financial space. Financial globalization also substantially reduces the relative autonomy of states with regard to the interests of dominant social classes. Freedom of capital movements enhances the mobility of capital and its ability to arbitrate at any given point in time between markets and stocks. This profoundly changes the balance of power between the owners of the means of production and employees, and between shareholders and managers, to the advantage of shareholders. It greatly increases the power shareholders may wield to sanction business strategies or policies deemed contrary to their interests, thus consolidating the control of capital over European states.

Capital’s growing control over states has accentuated the neo-liberal bias of public policy: continued tax relief for business, privatization of banks and public corporations, rethinking of pay-as-you-go retirement systems, reforms to “flexibilize” labour markets. The discourse of European governments seeks, aided and abetted by the opaque workings of EU institutions, to give credence to the idea that Brussels is behind these policies. Admittedly the influence of corporate lobbies on the Commission is not only a well established fact, it has become a part of the institution itself. Responsibility for the neo-liberal bias of European policy should however be mainly borne by member states, given their weight in the decision-making process. The discourse of European governments fuels public disaffection towards the European project, whereas the reforms needed to “rationalize” the policy mix can only be implemented with the largest possible support among European peoples.

Financial globalization thus contributes to establishing market forces and capital, particularly its most international segments, in the place of states at the heart of the European integration process (Sifakis, 2007). These segments are supposed to henceforth become the driving force of the process. However, the perimeter of the interests of capital is set by the constraint of its valorization. The aim of the capital, being the maximization of profit, limits its horizon to the direct determinants of its valorization. Capital cannot not be the driving force of projects bearing a strong political, almost visionary dimension, such as the deepening of European integration. Financial globalization even leads to a divergence of interests between the globalized segments of European capital and greater European integration. Deregulation of capital transfers in Europe encourages a process of delocalization and globalization of European firms. During the 1986-99 period acquisitions by European firms mainly targeted international rather than European companies (Sachwald, 2004: 55). Furthermore the vast majority – about 70% – of strategic alliances involving European firms in the 1990s concerned partners outside Europe (OCDE, 2001). This suggests that the dominant trend for firms is towards greater globalization, rather than European. As a result the whole planet, not Europe, becomes the relevant space for the reproduction of European capital. Europe’s multinational firms also derive considerable benefit from a situation in which the tax systems
of individual nations are forced to compete, due to the lack of fiscal harmonization in the EU. European capital also benefits from the decline in labour’s bargaining power and the advance of neo-liberal policies in Europe, made possible by financial globalization. Lastly, globalization of finance and production encourage fiscal competition, by consolidating the position of European countries that oppose any attempt to question this trend. Harmonization of taxes on capital would only have a limited effect as long as capital can still move freely all over the world.

The shift in the interests of European capital and the considerable increase in its control over EU states contribute to blocking the process of coordinating the European policy mix.

Conclusion

This study shows that the conception of the creative imbalance model concerning the dynamics of the process of European economic and monetary integration is not relevant. The re-launching of the European economic integration of the 1980s and the 90s is not the outcome of liberalizing capital flows supposedly initiated by the European Commission and European industrialists, but rather the result of a compromise between the two most powerful European states, France and Germany. What was at stake in this compromise was the organisation of post-Soviet Europe in accordance with the interests of both countries. Furthermore, European monetary unification has not had the integrating effects on European policy mix predicted by the creative imbalance theory. Finally, the arguments underpinning this theory made it easier to put through the reforms needed for a liberalization of economic mechanisms in Europe, a liberalization that was meant to be the first step towards setting up a federal Europe. The re-launching of European integration and financial globalization are two interdependent processes with shared dynamics. Full capital mobility is the very essence of financial globalization (Helleiner, 1994). It was also necessary for the implementation of the EMU project. Freedom of capital flows was used as an argument to reinforce the credibility of the project and to justify economic policies of austerity.

This study also shows that the European states that initiated the relaunching process are also responsible for the current loss of momentum in the process of European integration. The organization of the European policy mix is unusual. Monetary and exchange policies are centralized, while budgetary and fiscal policies are decided at the national level—the former highly constrained, the latter autonomous—while political integration is deadlocked. The European policy mix encourages member states to set up non-cooperative strategies: fiscal competition but also social dumping and wage restraint packages (Fitoussi, Le Cacheux, 2007:123). Such strategies are a follow-up to the “competitive” devaluations that occurred in Europe before monetary union. However, unlike the devaluations which were used by countries with weak currencies, today’s non-cooperative policies are deployed by all the countries in the eurozone. This trend accentuates disparities and harms the sense of unity between EU member states.

The model on which European integration has been based until now is rooted in the idea that the political integration of Europe must be achieved through economic integration. But in view of the close interlocking between these policies and the political structure of states, greater centralization and/or coordination of Europe’s budgetary and fiscal policy can only be achieved if comparable progress towards Europe’s political union is made at the same time.
Financial globalization is contributing to the loss of impetus in the process of European economic integration. It has weakened the European states that acted as a driving force in the integration process. It also enables European capital to force different national spaces to compete among themselves. This does not foster the development of a spirit of cooperation nor to mutual concessions, without which the European policy mix cannot be rationalized.

With integration of the European policy mix at a standstill, the rules of economic policy instituted by the Maastricht Treaty and the Stability Pact are perpetuated. These rules, bringing with them inter-temporal inconsistencies, are conducive to a technocratic drift in institutional operation and to less effective state intervention that dents confidence in the public authority. Thus, by “entrapping” the Member States, the initiators of the European monetary unification project seem to have achieved their goals. Nevertheless, in the absence of a European social contract, the market and the capital are progressively occupying the space left empty due to the weakening of public players.

Notes

1. Several studies emphasize the influence of the French vision and French officials within the European Commission during the seventies. I. Maes (1998) notes that the commissioner responsible for the Directorate-General II, Economic and Financial Affairs, has always been French, except during periods of French presidency of the Commission.

References


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