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FOUR SCENARIOS FOR THE REINVENTION OF EUROPE

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SUMMARY

Europe's leaders see the need for "more Europe" to deal with the euro crisis but do not know how to persuade their citizens, markets, parliaments or courts to accept it. This is the root of Europe's political crisis: the necessity and impossibility of integration. European integration has been defined by two contradictory but mutually reinforcing forces that operate on both the European and national level: technocracy and populism. But the more technocratic the EU has become, the more it has provoked a populist backlash. European leaders are now unable to solve the euro crisis because they can only force inadequate solutions through loopholes in the Lisbon Treaty.

Four routes towards solving Europe's institutional crisis are now emerging: asymmetric integration by working around the existing treaties; a smaller, more integrated eurozone based on the existing treaties; political union through treaty change; and a deal among a new vanguard through a Schengen-style treaty. There are also calls to strengthen each of the three traditional channels for democratic participation in order to restore legitimacy: European elections, referendums and national opt-outs. Whichever of these options Europe ultimately chooses, the challenge will be to solve the acute euro crisis without at the same time exacerbating the chronic crisis of declining European power.

Looming behind the euro crisis is a larger and more fundamental challenge: the near-collapse of the EU's political system. The markets have now forced Silvio Berlusconi and George Papandreou out of office, and their impatience with the slow pace of decision-making has moved the crisis from the periphery to the core economies of the eurozone. While the traders rage, European leaders have been inching towards agreement on the steps that are needed to save the euro. But while they see the need for "more Europe", they do not know how to persuade their citizens, markets, parliaments or courts to accept it. This is the root of Europe's political crisis: the necessity and impossibility of integration.

The economic necessity is easy to grasp. In order to deal with the imbalances in the eurozone that led to insolvent banks, excessive sovereign debt and real estate bubbles, there is a growing consensus that the single currency area needs greater integration. Many people are now calling for fiscal union to be complemented by economic and even political union. There is still disagreement among member states about the details, but most economists point to five key elements: a quasi-finance ministry to set and enforce fiscal rules; the ability to raise its own resources; common banking supervision, regulation and deposit insurance; common representation in international institutions; and a mechanism for ensuring the democratic legitimacy of these processes.

However, what is economically necessary is politically impossible. The steps needed to save the euro could be blocked by any one of a number of forces: a taxpayers' revolt in creditor

nations such as Germany, Finland, the Netherlands and Slovakia; a revolt against austerity in debtor countries such as Greece and Spain; the threat of referendums in countries such as Ireland or even France; the rulings of judiciaries such as the German Constitutional Court; or the collapse of markets or re-grading of ratings agencies. Meanwhile, a weakened David Cameron has promised his Eurosceptic backbenchers that he will make British support for any treaty change contingent on a renegotiation of British membership of the EU.

While elites across Europe are aware of these dangers and are generally committed to finding a European-level solution, they continue to see the root causes of the crisis differently in different countries. Because leaders have been slow to accept the legitimacy of other countries' concerns and positions, the EU still lacks a deep-seated consensus on what needs to be done that both creditor and debtor countries can support. The lack of a common understanding of the causes and responsibility for the crisis has made it harder for the eurozone countries and the EU to get ahead of the crisis and persuade markets that they are really prepared to do what it will take to stop the contagion.¹

In fact, the crisis is driving European countries even further apart and creating a perception of a "European 'clash of civilizations'".² In particular, three blocs are emerging within Europe: a Germanic bloc that wants austerity and rules, a Latin bloc that wants growth, and an Anglo-Saxon tendency that wants to loosen ties with the EU altogether. Of course, these blocs are based on hypocrisy and misinformation: for example, the country that broke the Stability and Growth Pact most dramatically was Germany; Spain met all of the Maastricht criteria well into the crisis; and Italians have very low levels of personal debt. Nevertheless, based on these perceptions, northern creditors are resisting a "transfer union"; Eastern Europeans are insisting that others should accept painful reforms as they did; and debtors are resisting the austerity measures that are being imposed on them.

Thus European leaders find themselves caught between global markets that have lost patience with multilateral decision-making on the one hand and voters who have lost patience with globalisation on the other. As they explore various different scenarios to integrate the eurozone, they are struggling to find a zone of the possible between these two extremes. Europe must develop institutional arrangements for a two-speed Europe that will strengthen rather than weaken Europe's ability to play a role in the world and to rethink Europe's political agenda to win back the consent of its citizens. Former British Foreign Secretary David Miliband has distinguished between two crises that Europe faces: an acute euro crisis, which requires Europe to strengthen its core; and a chronic crisis of a power transition to the east, which requires Europe to integrate its periphery. In solving the acute crisis, Europe must also avoid exacerbating the chronic crisis.

Jean Monnet vs. Marine Le Pen: technocracy and populism

If the eurozone's core economic problem boils down to the creation of a common currency without a common treasury, its political dilemma lies in the development of common policymaking without a common politics. The EU was built at a time when citizens were deferential and relations between states were seen as being above politics. Thus shielded from the cut and thrust of political debate, national leaders had the space to pursue visionary foreign policies. But this "permissive consensus" began to erode with the signature of the Maastricht Treaty 20 years ago when the EU entered domestic politics. Since then, rather than developing a continental politics, European integration has been defined by two contradictory but mutually reinforcing forces that operate on both the European and national level: technocracy and populism.

On the one hand, the EU has been the ultimate technocratic sphere. It is true that European integration has been driven by larger-than-life politicians such as Schuman, Adenauer and De Gasperi at the beginning of the European project and Giscard and Schmidt and Kohl and Mitterrand later on. But the EU's day-to-day agenda has always been driven by practical steps rather than grand political visions. The "Monnet method" – named after the key architect of European integration, the French official Jean Monnet – was designed to generate a consensus among European diplomats for limited projects of practical cross-border integration. The idea was that each of these projects would lead to the integration of further policy areas – from Europe's single market to its foreign policy.

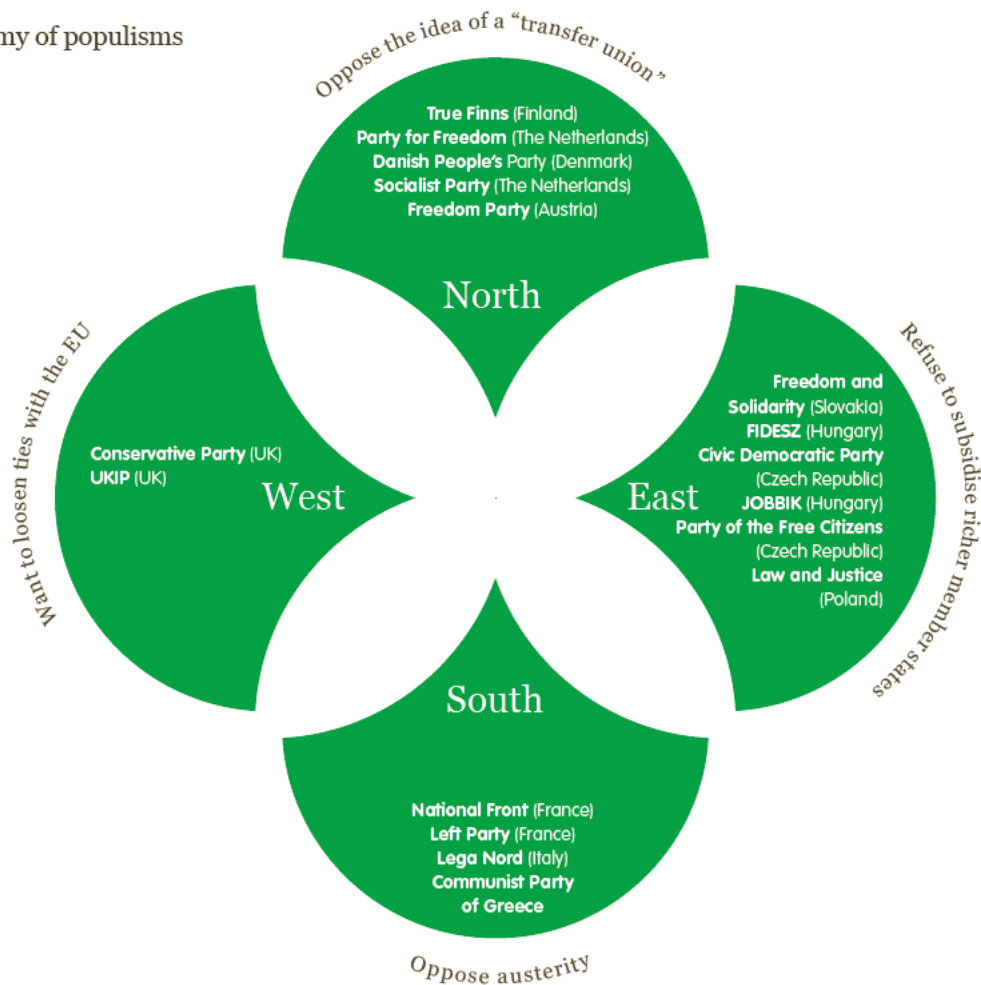
By building the EU in an incremental way, the technocrats managed to lower political temperatures in national capitals and find agreement among bureaucrats who were more interested in negotiating deals than grandstanding for the national media. They first created a coal and steel community, then a customs union, then a single market and finally a single currency. But, as the EU matured as a political project, its very success as a bureaucratic phenomenon fuelled a populist backlash at a national level.

It started in Britain in the 1980s when Margaret Thatcher famously wielded her handbag around Europe. But what began as a localised phenomenon gradually grew following Maastricht into a pan-European force embodied today by such disparate forces as Geert Wilders, the True Finns, Umberto Bossi and Marine Le Pen. There are now populists from the north, south, east and west as well as from the left and right (see figure 1 opposite). But although they have different ideologies, they all share a sense that politics has become the preserve of elites who are serving themselves rather than common people. In particular, they portray the EU as a conspiracy to build "Europe against the people". In its place, the populists aim to mobilise the "people against Europe" – leading, in the words of one senior Dutch diplomat, to the "democratic destruction of the EU".

¹ George Soros, "Does the Euro Have a Future", the *New York Review of Books*, 15 September 2011, available at <http://www.nybooks.com/articles/archives/2011/oct/13/does-euro-have-future/>.

² Hans Kundnani, "The European 'clash of civilizations'", ECFR Blog, 22 August 2011, available at http://ecfr.eu/blog/entry/the_european_clash_of_civilisations.

Figure 1
An anatomy of populisms



For many populists, the EU looks after the welfare of big business and banks; removes border controls and protects minorities at home; while promoting globalisation abroad. According to Le Pen, this is leading to a new split between so-called mainstream parties and the new populist movements: "Both left and right are for the EU, the euro, free trade and immigration," she has said. "For 30 years, [they] have been the same; the real fracture is now between those who support globalisation and nationalists."³

Technocracy and populism are mirror images: one is managerial, the other charismatic; one seeks incremental change, the other is attracted by grandiose rhetoric; one is about problem solving, the other about the politics of identity. They also have different models of legitimacy. The technocrats have sought to build legitimacy for the EU by trying to deliver positive outcomes for different interest groups – businesses, farmers, students, etc. Populism, on the other hand, has emerged during a period in which politics is organised not in factories or party meetings but on the internet. Its claims about distribution centre around identity.

However, although European technocracy and national populism are opposites, they are also mutually reinforcing. At a European level we can see this in the saga of the Lisbon Treaty. In 2005, the people of France and the Netherlands rejected the European constitution; Europe's leaders responded with a technocratic solution that sidestepped public opinion. Thus, on the one hand, as EU leaders try to remove European integration from national politics, the EU's legitimacy becomes more brittle, which in turn means that policymakers want to evade public opinion even more. On the other hand, as the EU becomes even more technocratic, the calls for democracy and referendums become stronger, which in turn creates a space for populist parties to emerge.

The situation in Italy and Greece shows the reverse: that national populism can lead to a technocratic backlash. Here, European markets, following a signal from Angela Merkel and Nicolas Sarkozy, forced Berlusconi and Papandreou out of office. Berlusconi was being punished for his populism and Papandreou for failing to develop the power to govern. As Tony Barber has argued: "In the name of saving their currency union, European policymakers prefer the suspension of politics as usual in Greece and Italy and its replacement with non-partisan, managerial expertise. Government policies will be supervised, not to say crafted in the first place, by Brussels

³ Charles Grant, "Marine Le Pen and the rise of populism", Centre for European Reform, 20 July 2011, available at <http://centreforeuropeanreform.blogspot.com/2011/07/marine-le-pen-and-rise-of-populism.html>.

and Frankfurt, the headquarters of the European Central Bank (ECB), and will be implemented by Greek and Italian experts of identical pan-European outlook.”⁴

This may slightly overstate the case, as both of the new governments have started not just with the blessing of European authorities but also with large majorities of public opinion who have shown a strong preference for transitional governments over renewed elections. Nevertheless, the result is that, rather than delivering democracy at the European level, the crisis has brought technocracy to the national level. The worry is what will happen if technocrats fail. The populists are already circling around the new governments in Greece and Italy.

Thus, from Athens to Helsinki, besieged elites are now caught between the destructive power of feral markets and Eurosceptic populists. Germany seems to be bucking the trend as its political class rediscovers its traditional pro-European rhetoric while its technocrats in the ECB and the Constitutional Court make common cause with the tabloids to set a Eurosceptic agenda. Across the rest of Europe the populists define the political options for all parties. In Slovakia, the ultimate cosmopolitan, European-minded government found itself opposing the bailout of Greece (although it claimed that it was anti-European to expect a poor country like Slovakia to bail out the richer debtor-nations). In Finland, a coalition of passionate pro-European politicians signed a deal on collateral that nearly sank the EU’s entire plan to save the euro. “We are scared shitless”, said one passionately pro-European cabinet minister. “The only way we can take on the populists is to clone them.”⁵

As a result, there is a gulf between what many pro-European mainstream politicians think they should do and what they think they can sell to the public. Consequently, they have hastily roped together inadequate solutions: stress tests lacking credibility; a credit facility hampered by stringent rules; and the emission of bonds that aren’t quite Eurobonds. These solutions fell far short of what was needed to provide a solution to the crisis, but because they were the most that could be forced through loopholes in the Lisbon Treaty, they were all that was politically possible.

The efficiency problem: four Europe’s or a funeral

Given the political constraints they face at home, European leaders have focused on fixing the institutional crisis that lies behind the euro’s travails rather than grasping the political challenges. Four routes towards a solution are emerging, based on four distinct procedural approaches: asymmetric integration by working around the existing treaties; a smaller, more integrated eurozone based on the existing treaties; political union through treaty change; and a deal among a new vanguard through a Schengen-style treaty. All four will fundamentally change the political and institutional settlement that today’s Europe has inherited from Maastricht. Each has advantages and disadvantages. But whichever of the four options Europe ultimately chooses, the challenge will be to solve the acute euro crisis without at the same time exacerbating the chronic crisis of declining European power.

Asymmetric integration

The first option is to continue the current system of incremental solutions without treaty change by relying on the European Council – that is, national leaders – to set the agenda (as opposed to the European Commission), creating new intergovernmental funding arrangements such as the European Financial Stability Facility (EFSF) and its successor the European Stability Mechanism (ESM) (to avoid breaking the “no bailout” clause); encouraging the ECB to buy bonds (to get around the challenge of asking for approval for each tranche of support to debtor governments); creating arrangements such as the so-called six pack of legislative proposals to scrutinise member states’ public finances and take action before imbalances develop; and using the International Monetary Fund (IMF) to police austerity measures.

It is not clear exactly what form this model of incremental change will take, but it is already apparent that it represents a break with the traditional approach to European integration in two ways. First, this mosaic of measures, some taken within and some outside the framework of the EU treaties, is in practice sidelining the European Commission and the European Parliament. The fact that the EFSF was established outside the treaties has allowed member states to get around the “no bailout” clause in the European treaties. But it also means that every legal decision has to be ratified by all national parliaments and every executive decision to deploy the funds for their intended purpose has to be agreed unanimously by every state government. This provides an opportunity for Eurosceptic populists to rally every time a new crisis emerges.

Second, it places much greater burdens on the deficit countries than the creditors (the memorandums of understanding signed by debtors go right into the nooks and crannies of national sovereignty – everything from retirement age and taxation levels to the size of shops and the level of pensions). As Joschka Fischer has argued, it creates the danger of a shift from a rules-based Europe to a power-based Europe. The

⁴ Tony Barber, “Europeans clutch at technocratic fixes”, *Financial Times*, 9 November 2011, available at <http://www.ft.com/cms/s/0/abccdedc-0ae3-11e1-b9f6-00144feabdc0.html>.

⁵ Unless otherwise stated, quotes are from interviews with the author.

MEP Andrew Duff even argues that this pattern is in danger of turning peripheral countries into “German satellites”: “There is a real risk of excessive centralisation of national policies along German lines with punitive consequences for the recovery of the weaker eurozone economies. [...] The fact is that mere economic policy co-ordination is not a federal solution and will hardly generate the necessarily tough and inevitably unpopular measures which the deteriorating situation requires.”⁶

These dynamics reflect a change in Germany, which is renegotiating its traditional approach to European integration. Against the background of the euro crisis, the Franco-German tandem has become unbalanced in Germany’s favour. Meanwhile, Germany has fallen out of love with the European Commission, shifting its preferred dynamic for integration from the “community method” to a new intergovernmental “Union method”. Above all, Germany has gradually become less willing to pay more for Europe than other member states while restricting its formal representation to the same level as that of other large member states. In these new intergovernmental mechanisms, which have been designed outside the formal EU institutions, voting power is linked to financial contributions, which gives Germany greater weight.

As well as being inefficient, the muddling-through approach is seen in many quarters as illegitimate. Some member states, particularly the smaller ones, worry that the European Commission is being sidelined, while citizens do not understand the arrangements or feel their voice is heard. In fact, many voices within Germany are also nervous about such an inefficient and overtly German Europe – which is why they are calling for a European convention on the future of Europe.

A smaller eurozone

In September, according to *Spiegel*, the German Finance Minister Wolfgang Schäuble, who is reportedly doubtful that Greece can be saved from bankruptcy, asked his officials to begin preparing for the scenario of a Greek exit from the common currency and the reintroduction of the drachma.⁷ A month later, at the G20 summit in Cannes, Angela Merkel and Nicolas Sarkozy broke the taboo on talking publicly about a Greek exit when they said it might be necessary to maintain the eurozone’s long-term stability. Following this meeting, French and German officials revealed that they had been working on plans to prune the eurozone to make it stronger. “You’ll still call it the euro, but it will be fewer countries”, an official said anonymously without identifying who might have to drop out.⁸ The members of this smaller eurozone could rapidly integrate in sensitive areas such as corporate

and personal taxation, leaving the remainder of the EU as a “confederation” that could possibly expand from 27 to 35 in the coming decade.

There is a legal obstacle to this idea of creating a smaller, more integrated eurozone: the EU treaties do not have a provision for leaving the euro and it is by no means clear how it would be possible to do so.⁹ But even if this procedural issue could be overcome, it is unlikely that an orderly exit would be possible without causing contagion. An exit would have consequences for the real economy as well as for the financial sector that would be much more severe than those of the Lehman Brothers bankruptcy which pushed the world economy to the brink of a new Great Depression. For example, UBS has estimated that a weak euro country that left the eurozone would incur a cost of around €10,000 per person in the first year, and €3,500 per person thereafter. If Germany were to leave, it would cost around €7,000 and €4,000 per person thereafter. In comparison, the cost of bailing out Greece, Ireland and Portugal entirely following a default would be a little over €1,000 per person.¹⁰

It is not even clear if the EU itself could survive what would amount to a break-up of the euro: some of the countries left out of the new, streamlined eurozone might form a new union of their own. Even if the EU did survive, it would lose much of its political influence in the world. A deep European recession would immediately and dramatically reduce the means available for both military and peacekeeping endeavours as well as for overseas development aid. Perhaps even more importantly, a break-up would greatly undermine European soft power: if Europeans were perceived to be unable to deal with their own internal problems adequately, it would be hard to imagine that the rest of the world would accept them as serious players on pressing global issues.

Political union through treaty change

The third option, which the European Council has now embraced in theory, is to make a bold leap forward to political union through treaty change. There have been calls from various sources for a mini-constitutional convention with representatives from national parliaments, national governments and EU institutions, followed by an intergovernmental conference. The main purpose would be to fold into the European Treaties the integrative moves that have been taken in the last two years. However, there are two different views about how far to go. Some want to focus mainly on creating an institutional and legal basis for enforcing budgetary rules; others want to shift additional economic and fiscal policy powers towards Brussels so that the final institutional set-up would resemble more closely a “fiscal union” with a de facto euro area finance ministry.

⁶ Andrew Duff, *Federal Union Now*, The Federal Trust, August 2011, available at <http://www.fedtrust.co.uk/admin/uploads/federal-union-now-book.pdf>.

⁷ German Finance Minister Prepares for Possible Greek Bankruptcy, *Spiegel Online*, 9 October 2011, available at <http://www.spiegel.de/international/europe/0,1518,785482,00.html>.

⁸ Julien Toyer and Annika Breidhardt, “French and Germans explore idea of smaller euro zone”, *Reuters*, 9 November 2011, available at <http://www.reuters.com/article/2011/11/09/us-eurozone-future-sarkozy-idUSTRE7A85VV20111109>.

⁹ Phoebus Athanassiou, “Withdrawal and Expulsion from the EU and EMU: some reflections”, European Central Bank, Legal Working Paper Series, Number 10, December 2009, available at <http://www.ecb.int/pub/pdf/scplps/ecblwp10.pdf>.

¹⁰ Eurozone: Where next? UBS Investment Research, 26 September 2011, available at <http://www.scribd.com/doc/66461792/xrm45376>

The current German government leans towards the first position, envisioning more of a “stability union” than a fiscal union. Its main priority is to strengthen the Stability and Growth Pact to include “automatic sanctions”. It would also like to appoint a “European Stability Commissioner”, who would be mandated to interfere directly in the affairs of states that violate the pact as well as cutting off payments to these states under the EU’s structural and cohesion funds. In order to make these measures seem less punitive, the German Christian Democrats propose – possibly as a second step – to move towards a political union in which the president of the European Commission would be directly elected and the European Parliament would have the right to initiate legislation. However, in southern Europe and even in France, this would be perceived not so much as a “stability union” but as an “austerity union” with a strong anti-growth bias.

The second option, which might be more acceptable beyond Germany, is a fiscal union that would have power over some of the EU’s expenditure and taxes. The former president of the European Central Bank, Jean-Claude Trichet, suggests that the eurozone should move towards a situation in which “it would be not only possible, but in some cases compulsory, for the European authorities to take direct decisions”.¹¹ In particular, Trichet proposes the creation of a eurozone finance ministry that would supervise financial institutions and represent the euro area. Some, such as French Foreign Minister Alain Juppé and former Belgian Prime Minister Guy Verhofstadt call for a full-blown United States of Europe. Others, such as Emma Bonino, propose a “federation lite” that would not absorb more than 5 percent of GDP, which would currently amount to around €650 billion – more or less the amount of the current rescue fund.¹²

However, whether the eurozone opts for a fiscal union or a political union, there remain big questions about whether a new treaty would include provisions for ejecting eurozone countries and whether to include other policy areas such as foreign policy. This plan is also fraught with risks. In particular, it could run into British demands for the repatriation of powers or be rejected in referendums that some member states would be required to hold. These risks lead some to favour a fourth scenario: an intergovernmental treaty between a new vanguard of eurozone countries that want to press ahead with further integration.

Federalism without the federalists

Joschka Fischer, a long-time champion of the idea of a two-speed Europe, predicts that the EU will divide into a vanguard (the euro group) and a rearguard (the rest of the 27 EU members): “This formalised division will fundamentally change the EU’s internal architecture,” he wrote in July. “Under the umbrella of the enlarged EU, the old dividing lines between a German/French-led European Economic Community and a British/Scandinavian-led European Free Trade Association re-emerge.”¹³ What Fischer envisages is some kind of legally binding intergovernmental agreement signed by members of the eurozone outside the scope of the EU treaties (along the same lines as the Schengen arrangement on border-free travel).

An intergovernmental arrangement of this kind would allow member states to avoid the pain of ratification in the 27 member states and prevent the 17 from being blackmailed by the renegotiation demands of British Eurosceptics. Even some eurozone countries such as Slovakia and Finland could be excluded if their parliaments refused to ratify the agreement. However, the paradox of this idea of a “euro-core” is that it could be a kind of federalism without the federalists: it could exclude EU institutions such as the European Commission, the European Parliament and the European Court of Justice (ECJ). Moreover, many of the most pro-European member states – including Poland (which currently holds the presidency), Latvia and Lithuania – would also be left in the slow lane of European integration.

Thus each of the four routes to fixing Europe’s institutional crisis has advantages and disadvantages. The first is the easiest to achieve but it risks failing to solve the crisis as well as exacerbating the resistance of European citizens. The second solution could be more sustainable and less painful for the citizens of countries such as Greece, but it could unleash a tsunami of panic that results in the unravelling of the euro. The third would be the most complete and durable solution but also has the greatest risk of spectacular failure, as a rejection of the treaty by parliaments or referendums could lead to the rapid disintegration of the EU. The fourth solution could give the eurozone what it needs while sidestepping the resistance of non-euro members, but it could lead to a new gulf within Europe and the slow marginalisation of the EU itself.

¹¹ “Tomorrow and the day after tomorrow: a vision for Europe”, Speech by Jean-Claude Trichet at the Humboldt University, Berlin, 24 October 2011, available at <http://www.ecb.int/press/key/date/2011/html/sp111024.en.html>.

¹² Emma Bonino, “The euro will be saved only if Europe exists”, European Council on Foreign Relations, 9 December 2010, available at http://ecfr.eu/content/entry/commentary_the_euro_will_be_saved_only_if_europe_exists/.

¹³ Joschka Fischer, “Europe’s Sovereignty Crisis”, Project Syndicate, 31 July 2011, available at <http://www.project-syndicate.org/commentary/fischer64/English>.

The danger of a two-speed Europe

Angela Merkel has said that the fragmentation of the euro would lead to the end of the EU. But, as Wolfgang Münchau has argued, saving the euro could also lead to the destruction of the EU. This danger is in part an institutional question: the inner core that is emerging is breaking some of the elements of the consensus that has allowed the EU to function in recent years. It has sidelined the European Commission, empowered and co-opted the European Council by appointing Jean-Claude Juncker as chair of the group, and has acted through a Franco-German core that does not fully reflect the interests of small member states or the deficit countries.

At the same time, the danger of a two-speed Europe is a policy question. It is inevitable that the “euro-core” will increasingly speak with one voice within the EU as well as outside it. For example, in negotiations on the single market in financial services it is quite likely that the “euro-core” would agree a single position and only then negotiate with the 10 states outside the eurozone. If an inner core of European states moves forward, the excluded states will be very nervous about ensuring that control of key policy areas such as the single market, common trade policy and the common budget remain with the 27 rather than being decided by the “euro-core”.

There are also big questions about the effects of a two-speed Europe on the other two big integration projects: the common judicial space and common foreign policy. For example, it will be hard for the EU to rise to its potential on the world stage if geopolitically powerful countries such as Britain and Poland are excluded from the core. The implications for justice and legal affairs could be equally profound. Some of the Schengen countries could be excluded from the “euro-core”, but it is possible that countries that have entered a fiscal union with each other might want to unite their migration policies. As David Miliband has argued, a two-speed Europe would be unbalanced on economic issues such as free trade and the single market and foreign-policy issues such as Russia.¹⁴

This could in turn create a danger of the fragmentation of the EU into informal or even formal alliances and the emergence of geo-economic power struggles within it. There has already been some co-ordination between the Polish presidency, Denmark, Sweden and the UK. Some have suggested that the non-eurozone states should formally organise themselves into a “Non-Eurogroup” (NEG) that would elect its own chair and hold its own summits in order to protect itself from discrimination (in particular, by ensuring that future Council and Commission presidents can still come from non-euro countries).¹⁵ However, unless the eurozone behaves in an aggressive way, it is unlikely that this group – which includes

some states such as Poland that want one day to join the euro, others such as Denmark that haven’t yet decided, and others such as the UK that are unlikely to join for the foreseeable future – will cohere into a coalition with shared interests. As well as a lack of cohesion among the “euro-outs”, there is also a lack of cohesion within the eurozone: one eurozone minister recently said in private that “the countries we want in the eurozone like Sweden and the UK are not there and the ones we do not want are.”

In order to avoid the break-up of the EU, attention should be devoted to the relations between the 17 and the 10, as well as to the governance of the eurozone. It will be important to devise membership criteria that are open so that other countries can join at any time if and when they are willing and able (many Eastern Europeans are keen to make sure they are able to join when they meet the convergence criteria). It will also be important to leave a gateway open for the absorption of the core into the larger union at a later stage.¹⁶ The best outcome would be to develop the two-speed Europe within the existing treaties under the provisions for “enhanced co-operation”. This would make it possible for non-euro countries to stay in the room when discussions take place and to prevent the “euro-core” formally discussing without them issues that fall within the scope of the existing treaties. This would also keep alive the prospect of a messy Europe of variable geometry rather than a two-speed Europe of first- and second-class states.

Above all, European leaders will need to agree an explicit new deal between surplus and deficit countries and between northern and southern, eastern and western member states. As well as reconciling the eurozone with the non-eurozone countries, this deal will need to strike a balance between austerity and budget transfers, liberalisation and social protection, and ways of transferring money from the rest of the world to the eastern *and* southern neighbourhoods. Such a deal will require many national leaders to recognize that it is in their own national interests to reach consensus about how the eurozone and the EU should work in future. They must agree on a vision that is perceived as fair by all member states rather than seeming to penalise any of them.

A break with the one-speed model could create opportunities as well as threats. For example, enlargement has ground to a halt within the current EU. But in a messier multi-speed Europe, there may be new ways to integrate Turkey or Ukraine (although Turkey will not be keen on second-class membership unless it includes visa-free travel). Yet whichever of the institutional options Europe’s leaders choose, they are unlikely to close the gap between Europe and its citizens – in fact, they may exacerbate it – unless they also change the content and form of European integration.

¹⁴ David Miliband, “Don’t split Europe; make it stronger”, *Financial Times*, 14 November 2011, available at <http://blogs.ft.com/the-a-list/2011/11/14/dont-split-europe-make-it-stronger/#>.

¹⁵ David Owen and David Marsh, “It’s time for a radical blueprint for a new Europe”, *Financial Times*, 10 October 2011, available at <http://www.ft.com/cms/s/0/3dbadbda-f32b-11e0-8383-00144feab49a.html#axzz1d1wXsKYm>.

¹⁶ Sebastian Kurpas, Julia De Clerck-Sachsse, José Ignacio Torreblanca and Gaëtane Ricard-Nihoul, “From Threat to Opportunity: Making Flexible Integration Work”, EPIN Working Paper 15, September 2006, available at <http://www.ceps.eu/files/book/1380.pdf>.

The legitimacy problem: how to close the gulf with Europe's citizens

The EU faces a paradox. It has lost legitimacy because its leaders cannot act. But the reason they cannot act is in turn because the EU has so little legitimacy. There has been a debate for three decades about the EU's "democratic deficit". But a more accurate way of describing Europe's legitimacy problems would be to say that the EU has had a surplus of democracy on technocratic issues which fail to engage voters, and an absence of politics on the big issues which might actually engage them. There are already many channels for European citizens to exercise their voice: national elections for the leaders who represent them in the European Council, European elections for representatives in the European Parliament, and even referendums in some countries to ratify new treaties. But most attempts to engage voters have been over procedural issues such as treaty change rather than political choices facing the EU.

As the euro crisis heats up and proposals are made for greater European action, there is a renewed quest for a democratic mandate. People are calling for each of the three traditional channels for democratic participation to be strengthened: European elections, referendums and national opt-outs. But it is not clear that any of these channels will necessarily give the EU the legitimacy it needs to act. And each route could paradoxically make Europe even harder to govern.

Electing European officials

Germany's ruling Christian Democrats recently endorsed a paper calling for direct elections of the president of the European Commission and allowing the European Parliament to share the right of initiative with the European Commission.¹⁷ Others – including Felipe González, chairman of the Reflection Group on the Future of Europe – have called for the next Commission president to be elected from a transnational list in the 2014 European elections.¹⁸ As the EU moves towards having stronger fiscal rule, and monitoring of national budgets – the so-called European Semesters – many are calling for the European Parliament to be given a formal role in signing off on national budgets as well as the Commission and the member states.¹⁹

The rationale for these moves is that they could help the EU overcome institutional gridlock, produce a mandate for reform and increase the legitimacy of the EU by providing a forum for a real contest of European ideas. However, the

European Parliament has stubbornly refused to live up to the expectations of its champions. Although it has established itself as an effective revising chamber that can hold the European executive to account, there is little to suggest that it has the legitimacy or ability to set the European agenda. Turnout has fallen with each successive election, and European elections tend to be referendums on the national governments rather than a real chance to debate the future of Europe.

As a result, the main European issue that comes up at election time is whether people want the EU to exist at all (one in five MEPs elected in 2009 stood on a single issue Eurosceptic platform). The Parliament's supporters have argued that with greater power would come greater legitimacy. In fact the turnout has fallen with each successive election even as its powers have increased. Given this track record, and the general crisis facing representative democracy even at a national level, it is not clear that the dynamics would change if European elections were linked to the selection of Commission president. The real question is whether, in the absence of a common language and a common media, it will ever be possible to have a common debate about the future shape of Europe. This has led some such as Joschka Fischer to call for the involvement of national parliaments rather than the European Parliament.

Referendums

George Papandreou first proposed – and then, under pressure from Paris and Berlin, withdrew – the idea of having a referendum on his national austerity plan. He claimed that this would give him a direct mandate for austerity that would allow him to impose discipline on his fissiparous party and the opposition. However, the counter-argument of the Group of Frankfurt was that a cacophony of national referendums would spook the markets and could prevent the EU from taking any decisions at all. Although the motivation was to avoid further delay, the strong-arming of Papandreou by Paris and Berlin created the impression that the EU is so scared of public opinion that it will suppress it at any cost (and, moreover, that the opinion of creditors weighs more than that of the debtor nations).

However, it will be impossible to avoid referendums in the future. Although Eurozone leaders hope to avoid referendums in the 10 "euro-outs", a number of the eurozone 17 such as Ireland are legally obliged to hold a referendum on transfers of sovereignty (see figure 2). However, it will be politically difficult for the six eurozone members that promised a referendum on the incremental changes in the so-called European constitution in 2005 to deny their voters a similar say on the much more significant steps towards fiscal union. The problem is that referendums on the treaties – complex documents negotiated by European diplomats outside the political process – do not allow European citizens and political parties to air big political disagreements about the future shape of Europe. Consulting people on the future

¹⁷ See the resolution of the CDU party conference, 13–15 November 2011, available at <http://www.leipzig2011.cdu.de/images/stories/docs/111114-beschluss-europa.pdf>.

¹⁸ A Spanish official has portrayed this as a thinly disguised German power-grab: as the biggest member state Germany has one in eight MEPs (compared to one in 27 commissioners).

¹⁹ Benedicta Marzinotto, Guntram B. Wolff and Mark Hallerberg, "How effective and legitimate is the European semester? Increasing role of the European parliament", Bruegel, 22 September 2011, available at <http://www.bruegel.org/publications/publication-detail/publication/612-how-effective-and-legitimate-is-the-european-semester-increasing-role-of-the-european-parliament/>.

Figure 2
Requirements for referendums in EU member states

COUNTRY	POLITICAL PRECEDENT	LEGAL REQUIREMENT
Austria		XC
Belgium		
Bulgaria		
Cyprus		
Czech Republic	●	XC
Denmark	●	X
Estonia		
Finland		
France	●	XC
Germany		
Greece		
Hungary		
Ireland	●	X
Italy		
Latvia		
Lithuania		XF
Luxembourg	●	
Malta		
Netherlands	●	
Poland	●	XF
Portugal	●	
Romania		
Slovakia		
Slovenia		XC
Spain	●	XC
Sweden		XC
United Kingdom	●	X

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Political precedent:

- = Held, or committed to hold, a referendum on the European Constitution

Legal requirement:

- X = Referendum legally required
- XC = Referendum legally required only if treaty changes affect a constitutional amendment
- XF = Referendum legally required only if treaty changes affect the fundamental principles of the constitution

institutional shape of the EU is the technocrats' idea of democracy. It is entirely unsurprising that citizens responded by backing the populists.

National opt-outs

One way that the EU has managed to avoid outright rejection has been to show flexibility rather than imposing unpopular measures on reluctant partners. The debate about opt-outs and renegotiation is currently most active in the UK, where a group of 81 Conservative MPs defied a three-line whip to call for an EU referendum in October. David Cameron has promised to conduct a review into "rebalancing competences" between Britain and the EU and has said that he will link support for treaty change to some kind of result. Many in the governing Conservative party secretly hope that the government will try – and fail – to renegotiate as a prelude to holding an in-out referendum and then withdrawing entirely from the EU.

However, it is not just the UK that demands opt-outs. In fact, the idea of opt-outs has been central to gaining consent for European integration in the past. Thus Denmark was given opt-outs in three areas (the euro; defence; and justice and home affairs), Ireland was given a protocol after its "no" vote on Lisbon, Slovakia was given an opt-out of the Greek bail-out, while Finland was guaranteed collateral on its contribution. The move towards greater fiscal integration might trigger a wall of demands for opt-outs from Eurosceptic nations – including the six eurozone countries that are poorer than Greece and might want to limit their liabilities. But if each member opts for an à-la-carte approach to Europe, it will be impossible to have a strong-enough sense of common purpose for Europe to survive.

Even if it is possible to create greater legitimacy for European integration without making the EU ungovernable, however, this may not be enough to stop the populist backlash. IMF managing director Christine Lagarde has predicted that the crisis will lead to a "lost decade" of falling wages and rising unemployment within the EU.²⁰ As a region that is more open to trade and people than any other while protectionism is on the rise in emerging and developing countries, the eurozone has borne a disproportionate amount of the cost of the adjustment since the 2008 crisis: it is the only major economic region that has had no monetary easing. The best hope of regaining credibility – and stemming the tide of disintegration that has already spread beyond the currency to the rest of the EU – may therefore be to develop political rather than institutional responses to the arguments of the populists.

²⁰ Alan Beattie and Brooke Masters, "Fears grow over global euro effect", *Financial Times*, 9 November 2011, available at <http://www.ft.com/cms/s/0/e6dab292-0a2f-11e1-92b5-00144feabdco.html#axzz1e3KF1gFF>.

The EU should therefore embrace a progressive policy agenda that serves the interests of ordinary citizens as well as bankers. It needs a growth union rather than an austerity union. As well as taking measures to increase competitiveness, it should change the rules of the Euro-Plus Pact on public finances to allow for social investment, reform the EU budget to help with adjustments and make receiving money conditional on reforms. The EU also needs to address managed migration, including more common measures on the protection of external borders and burden-sharing arrangements. Ultimately, the EU needs a coherent foreign policy to deal with other great powers such as China rather than simply acting as a channel for globalisation.

Avoiding the disintegration of Europe

According to Jan Zielonka, “we have numerous books on European integration, but hardly any on disintegration”.²¹ He outlines three possible roads to ruin for the EU: a dramatic failure through insufficient action; the rejection of a great leap forward; and what he calls “disintegration in disguise”, whereby EU leaders save the euro but destroy the EU in the process. George Soros has said that the EU is “a wonderful example of a boom-bust process in politics” that is initially self-reinforcing and eventually self-defeating.²² What he means is that while Europe’s single currency was being built, it created political and economic constituencies for integration; now the crisis is creating constituencies for disintegration in the markets and in national politics.

Europe’s crisis has stripped national governments of the luxury of hiding behind the weak leaders they installed in Brussels. For too long, they have found themselves defending an unsustainable status quo rather than facing up to Europe’s short-comings and plotting a course to correct them. To avoid the fragmentation of Europe, they should now set out a radical vision for rethinking Europe which deals with the efficiency and the legitimacy crises at the same time. Since its inception European integration has moved forward because of repetitive crises. But it requires political leadership to make these crises a source of energy rather than paralysis. This is a time not for conservatism but for re-invention.

²¹ Jan Zielonka, “Marching towards disintegration”, European Council on Foreign Relations, 3 October 2011, available at http://ecfr.eu/content/entry/commentary_marching_towards_disintegration.

²² Transcript of Remarks by George Soros, Central European University, Budapest, 3 November 2011, available at <https://www.ceu.hu/soros-transcript-nov3-2011>.

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