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EuroVisions

Turning the Tide? But still not enough

Assessing the European Council of 28-29 June 2012

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What has been at stake?

In the run up for the European Council 28-29th June, the tide of European official speak has started to turn in a new direction. There was finally the recognition that austerity needs to be complemented with growth policies, and that these require investment and not only structural reforms. Recession is spreading so widely that denial is no longer possible. Hollande's victory in France made it easier for other Prime Ministers in the European Council to speak their minds, reflecting increasing political and social tensions against a "austerity only" approach in many European Member States.

New commitments have started to be prepared to foster the role of European investment instruments, such as the European Investment Bank and the structural funds. These are relevant steps, but will they be enough to overcome the euro-zone crisis? Alas, no. Investment and jobs creation, particularly by SMEs, are confronted with a severe credit shortage by banks in many regions of Europe. Private consumption is shrinking almost everywhere, reducing the demand for many European products and services. And many public budgets do not have the fiscal space to support either investment or consumption, because their deficits and debts are too high and, furthermore, because the interest rates to issue more public debt are extremely high and unaffordable.

This is the new situation Europe is in. In order to re-launch growth, it is no longer enough to re-balance the existing policies and instrument. It is also necessary to create new ones in order to complete the architecture of the Economic and Monetary Union: better economic coordination in order to reduce the macro-economic imbalances between deficit and surplus countries; a stronger European industrial policy to develop the European competitive advantages for the global economy; a banking Union to ensure financial stability with stronger European supervision and restructuring of banks; and a fiscal Union to ensure stricter fiscal discipline together with a common instrument to bring down the cost of issuing public debt to sustainable level. That is why Van Rompuy has received the mandate to prepare a more long term vision for the Economic and Monetary Union, in collaboration with Barroso, Juncker and Draghi.

On top of these general issues, dramatic clouds were gathering around particular national cases: the referendum on the Fiscal Treaty in Ireland on 31st May, the second elections in Greece on 17th June and the mounting pressures on Spanish banks.

The political game

A first chain of events was able to reduce these dramatic clouds, bringing a certain sense of relief: the referendum in Ireland has avoided a "no", which would mean bankruptcy and exit from the eurozone; a plan to rescue Spanish banks was swiftly announced by the Eurogroup before the Greek elections, in order to contain contagion just in case of electoral surprise in Greece, but this has turned into a final choice of a "national salvation government", combining center-right and center left forces, including a weakened PASOK.

Moreover, the momentum of Hollande's victory was completed by the absolute majority attained in the national parliament by the French Socialist Party. When, the G-20 Summit started in Los Cabos, the empowered French President could find many other allies for his cause of prioritizing growth: not only Monti and Rajoy, but also Obama, and the Presidents of Brazil, India, China, South Africa and Argentina, all hit by the eurozone crisis, which has become the main global driver for financial instability and recession. In a private meeting between Obama and the European leaders, Monti presented his proposal to use the EFSF/ESM/ECB more effectively to intervene in the sovereign debt markets and bring down borrowing costs. This was not an easy situation for Merkel, but the decisive discussion would come among the European leaders themselves during the European Council.

In the meantime, Hollande has confirmed his role as first mover in this new political game. He has presented a proposal of a Pact for Growth in Europe which would frame the political decisions of this Council into three main priorities: to re-launch growth; to ensure financial stability; to define the road to complete the Economic and Monetary Union. In parallel, the Socialist and Social-Democratic family has developed coordinated initiatives to push in the same direction: a PES policy document on a European Investment Strategy, a S&D Group Declaration on a Growth and Employment Strategy for Europe and a FEPS Report on "A proposed investment programme for 2012-2015" have provided the basis for the Declaration "A Pact for Growth and Jobs in Europe" adopted by the PES Leaders on 28 June. In the meantime, the SPD has approved its Convention in Berlin, a decision which paved the way for an alternative German position, and which was followed up in detail by the PES family and by the new French Government. Hollande has even received the three German SPD leaders Gabriel, Steinmeyer and Steinbruck in the Elysée.

Most of the measures for the first priority – growth and investment- were endorsed in a pre-summit meeting in Rome between the leaders of the four big eurozone countries Monti, Hollande, Merkel and Rajoy, but it was difficult to disguise the divergences about the two other priorities: how to complete the Economic and Monetary Union and how to control the sovereign debt crisis and the banking crisis which are feeding each other, creating a dangerous spiral of states rescuing banks and banks rescuing states. This vicious circle has to be broken.

This issue became the central one in that very European Council, when Van Rompuy could not announce the Growth Compact before the dinner on the 28th, as planned, because Italy and Spain decided to block its adoption until having concrete solutions for their urgent problems of unsustainable borrowing costs and rescuing the banks. The final deal came on the 29th at 4am, after a dramatic discussion among the 17 euro-zone leaders, where Monti threatened resignation in a face-to-face discussion with Merkel. High stakes politics is back in Brussels. Nevertheless, Merkel kept her

tough style of negotiation: for each kind of financial support, there is a precise request of conditionality and control as well as compensation in another area of negotiation.

Key issues for an assessment of the European Council 28-29 June 2012

General Approach

For the first time, the European Council recognizes the need to overcome the crisis with stronger priority for growth based on investment and not only structural reforms. Yet, it misses a broader approach, which should also involve the European macro-economic management in the demand side and industrial policy in the supply side

Fiscal consolidation

For the first time, there is a reference to the need of taking into account investment and the quality of public expenditure when assessing fiscal consolidation, in line with a smarter golden rule. Yet, this is not strong enough to re-balance the current revised Stability and Growth Pact and the "two-pack", and even less the Stability Treaty under ratification

Social dimension

Member States should include Job Plans in their National Reform Programmes, but there is no reference to the increasing divergence in social standards

Youth guarantee

There are more concrete objectives regarding youth employment and training to be supported by ESF, but there is no explicit reference to youth guarantee

Public administration

For the first time there is clear focus on improving the role of public administration, but there is no reference to social services

Single market

Several commitments regarding the digital agenda, the energy market, support to SMEs. A final deal on the community patent, after more than 20 years. The social dimension of the single market is ignored, except for supporting labour mobility

Trade

There are several commitments to use bilateral trade agreements, but there is no reference to better standards in European trade policy

Investment instruments

Concrete commitments were made regarding EIB lending capacity, EIF, project bonds, structural funds with a total of 120Billion Euros. The Multiannual Financial Framework should be to be used as a leverage for Europe 2020 Strategy and there is a special reference to Horizon 2020 for Research and Innovation and to COSME for enterprises and SMEs. Yet, the scope of European investment instruments remain very limited and not sufficient to support a real European industrial policy

Tax policy

There is a move forward in a financial transaction tax by using enhanced cooperation and an Action plan to fight tax evasion was requested. Nevertheless, savings taxation agreements with third countries are lagging behind

Financial stability- banks

A stronger European supervision authority for banks should be created and be managed by the ECB. After that, there will be the possibility for EFSF/ESM to support banks directly without increasing public debt and with a conditionality which no longer involves public spending cuts. Nevertheless, there is no reference to a European deposit guarantee

Financial stability- sovereign debt

The possibility for EFSF/ESM to intervene in the markets to stabilise public debt was accepted, provided Member States respect the recommendations under the European Semester, the Stability and Growth Pact and the macro-economic procedure. Their memorandum of understanding should be more limited to that. The ECB can be used as an EFFF/ESM agent

Developing the Economic and Monetary Union

Van Rompuy's draft proposes a longer term vision for the EMU, aiming at combining the three principles of competitiveness, coordination and convergence and comprising four integrated frameworks: financial, budgetary, economic and democratic

The issue of joint issuance of debt is referred to as a possibility to be considered when the conditions of fiscal oversight will be met. Many issues remain to be clarified regarding the way to complete EMU architecture. The democratic dimension is still very poor and the social dimension is absent.

Treaty Changes

The reference to the ratification of the Fiscal Treaty has been deleted from the last version of the conclusions. The real meaning of this deletion remains to be seen. The next versions of the Van Rompuy document should identify the Treaty changes which may be necessary.

Remarks for the future

Yet, there is Gordian knot here. What should come first? Merkel argues that a banking union and a fiscal union are not possible without more political union, meaning sharing sovereignty at European level. Hollande claims that a banking union and a fiscal union should come first. The only way to cut this knot is engaging to move forward in all these areas in an articulated way. The discussion on what should come first no longer makes sense. A fair deal, with rights and duties for all, is needed to complete the Economic and Monetary Union. And the democratic legitimacy of all the decisions at European level should strengthen.

When will the key political actors move in this direction? The pressure from the markets, from the citizens, and from the EU's international partners is now huge. The risks building up in larger economies such as Spain and Italy are also worrying. When states increase their debt to rescue banks and banks increase their debt to rescue states, there is something fundamentally wrong. The euro-zone crisis has certainly reached a new and dangerous stage, but the key political actors will only move when they perceive that "your crisis is my crisis".

As long as growth is sustained, exports progress, unemployment declines, banks attract savings, public deficit and spreads are curbed, the public opinion, notably in Germany, will not have this perception. But this risk of reversal of these trends is underway, German success is not sustainable if its partners are pushed for a long recession. If this is not explained and turns into reality, this will be probably too late, for everybody.

A grand design, completing and re-balancing the Economic and Monetary Union, should now become a matter of vital interest of all EU Member States.

Maria João Rodrigues has been a special advisor in the European Union institutions, working directly with Prime Ministers in the EU Presidencies and with European Commissioners. She was in the coordinating teams in charge of designing and implementing the European strategy for growth since 2000 and of negotiating the Lisbon Treaty in 2007.

She has also been involved in the preparation of several summits between the EU and its strategic partners such China, Russia, Brazil and USA. Finally, she has been member and chair of several high-level groups to prepare EU political initiatives. She is also professor of European economic policy in the Universite Libre de Bruxelles and in the Lisbon University Institute.

Building on her experience of preparing meetings of the European Council for twelve years, she provides a special insight on the context, background and critical assessment of these meetings where the EU's political direction is shaped. European politics need to be debated to be better understood and to become more relevant for European citizens. This is the purpose of these comments.