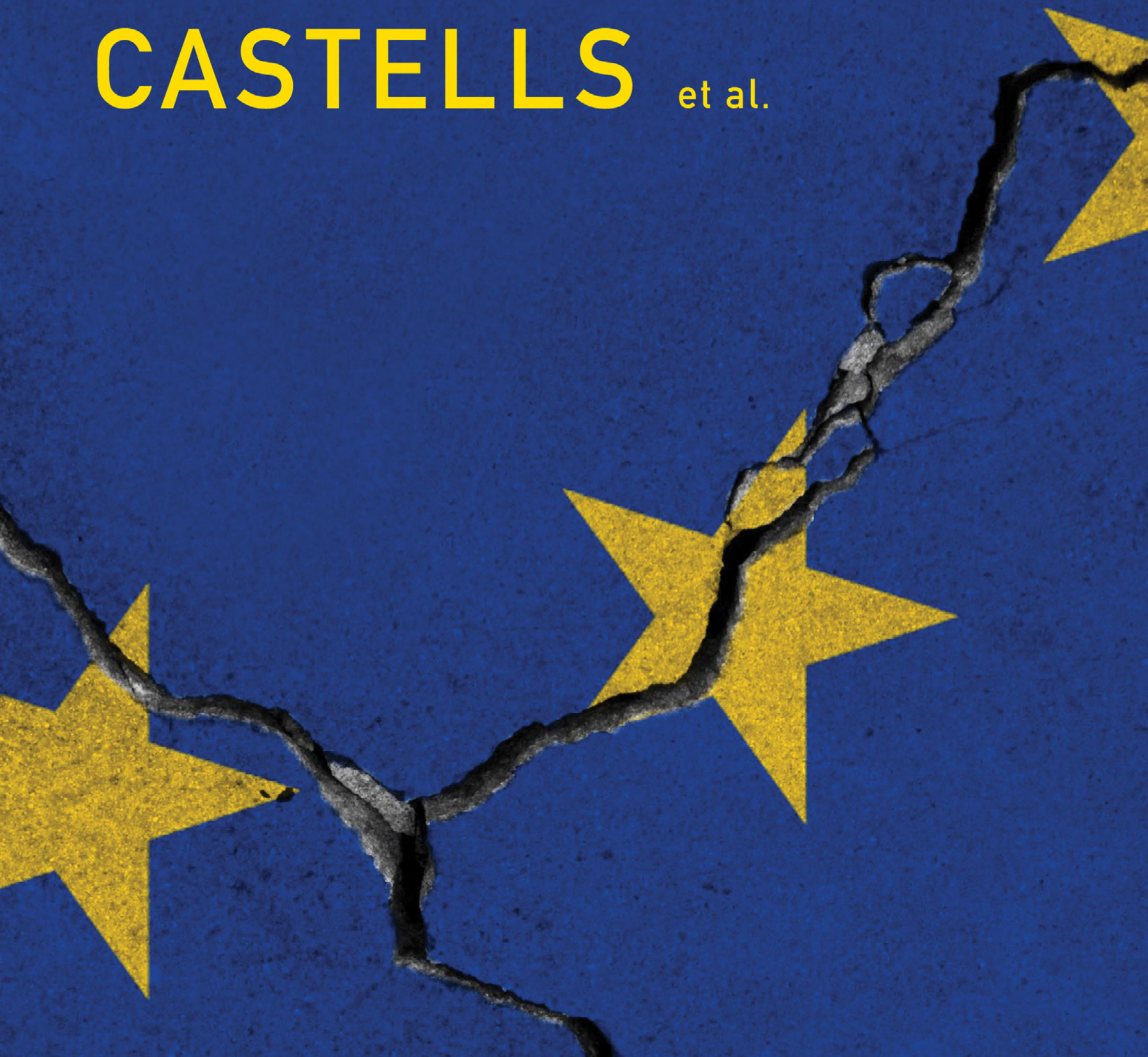
# EUROPE'S CRISES

edited by

MANUEL CASTELLS et al.



Europe's Crises

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*Edited by*


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# Introduction: Fading of a Dream?

Once upon a time, there was a dream – that Europeans would unite after centuries of war-making, nationalist confrontation and cultural xenophobia.

The carnage of World War II and the destruction of the productive infrastructure of the continent created the historical opportunity for economic integration and institutional cooperation as a way to supersede the demons of the past and set Europe on a path of shared peace and prosperity. Those who created Europe knew that a direct political process was not possible, and the economic process was a means to achieve political goals in the future. For almost six decades, a process of multidimensional integration proceeded gradually by successive waves, extending the union from the original six founding members of the European Economic Community to the 28 members of the European Union, woven together in a dense institutional network of shared sovereignty between the participating nation-states.

At the dawn of the twenty-first century the European Union, as dreamed by the visionary politicians and technocrats who dared to engage in one of the most remarkable political experiments in history, could be considered a success. It had become the largest economy in the world, with around a quarter of global gross domestic product (GDP), the largest consumer market, the largest repository of non-military science and technology knowledge on the planet, and a decisive share of global finance, with London and Frankfurt among the pre-eminent financial centres in the world. Peace and security appeared to be solidly established among EU members for the long haul, and the remaining European conflicts were ultimately contained by military cooperation with the United States, in spite of some setbacks such as the war that followed the disintegration of Yugoslavia. Prosperity in terms of income, assets and social benefits was the highest on the planet, albeit with increasing social inequality. Democracy and human rights were rooted in the daily practice of European societies, and the institutions of co-governance, however bureaucratic, kept functioning. Tolerance and international solidarity with less fortunate areas of the world were a key component of the ideology of European institutions, albeit not always reflected in practice. The project of preserving and diffusing European values, on the basis of the original project of economic integration, seemed to have been vindicated. A new round of deeper integration was launched at the turn of the century, particularly with the creation of a common currency, the euro, in most of the EU, and the constitution of Europe-wide research and technology institutions, such as the European Research Council (ERC) and the European Institute of Innovation and Technology (EIT). The power of the European Parliament was strengthened to counter the power concentrated in the European Commission. The moment appeared to have come to establish the legitimacy of the European institutions with the promulgation and approval of a European Constitution. While the notion of the United States of Europe was never seriously considered, the creative construction of a supra-national political union made up of a network of nation-states was paving the way for a historically novel form of continental federalism.

However, this process was accompanied by stagnating economic growth coupled with demographic atrophy and an unhealthy emphasis on intra-European politics. And then the process of integration was stalled as it was challenged by the growing salience of anti-EU feelings in many European countries, culminating in the unthinkable: Brexit, the voluntary exit of a member country (the outcome of the UK referendum of 23 June 2016). Suddenly, the European Union became something quite different from a stable institutional construction: its shape and competences could vary, as could its membership. Will the paralysis of the EU mark the beginning of the twenty-first century, as the collapse of the Soviet Union, an unthinkable event at the time, marked the twentieth century's end? Is the European dream fading? Why? How? What are the roots and the potential dangers of disintegration? What are the prospects and consequences of the multiple crises of the European Union in the early twenty-first century?

These are the questions explored and analysed in this volume from an intellectually pluralistic perspective that aims at minimizing normativity to maximize clarity in the analysis and diagnosis of the crises. We use 'crises' in the plural because the rampant crisis of the European Union as an institutional system stems from the convergence of diverse, interrelated and overlapping crises – financial, monetary, industrial, social, political, ideological, moral, geopolitical, migratory – that feed into each other while being distinct in their origins and their development. The tentative answers to these questions are developed in the various chapters of the volume. However, there is a common thread that may explain the contours of the institutional crisis, and therefore clarify the terms of the debate for the eventual overcoming of this crisis.

We start from the assumption that crises of any institutional system can occur when the performance of the system is perturbed and the perturbations become increasingly serious in character, giving rise to the very real possibility that, without taking further action or implementing new policies or regulations, the system may spin out of control and break down. We also contend that such systemic crises are induced by the characteristics and contradictions involved in the process of institutional formation. Concretely speaking, what this means in the context of Europe is that the crises that have plagued the European Union in the last decade stem to a large extent from the flaws in its construction. And these flaws are almost necessary consequences of the political processes that led to its formation. In other words, the decisions that made possible the development of the EU created the conditions for its multiple crises. Of course, these crises are not *only* the result of flaws in the construction of European institutions: there are other factors involved too, in some cases stemming from sources well beyond Europe; but only by understanding the institutional flaws can we understand why these crises occurred as they did in the European context, and why they have (or have had) the characteristics and consequences that they have.

Let us review the argument in its historical specificity (much of the data and detailed analyses in support of this argument can be found in the chapters in this volume).

First of all, any stable political-institutional construction requires some convergence of interests among the actors that build the institutions, as well as some form of common identity among the people involved in the process. In the case of the European Union, there is consensus on the fact that there was originally a defensive project, intended to prevent another war breaking out in Europe, that was later used by a few visionary leaders to put forward a utopian project. This was a project of the political and economic elites without the real participation, commitment and full understanding of most citizens. Every major step of economic and institutional integration was intended to make irreversible the process of European unification, with the creation of the common currency, the euro, being the most blatant expression of this strategy of the '*fait accompli*'.

European construction started as a defensive project aimed at superseding past wars and preventing future wars. It therefore had to involve the traditional warring nations, France and Germany above all, and the powerful American ally in deterring the Soviet Union in the future – NATO was a necessary complement to the European Union. However, the integration had to start with the economy, the most obvious necessity after the devastation of the war. Integrated markets required broader economic integration that proceeded by leaps and bounds to reach some partial monetary and financial integration.

The utopian project included political integration and cultural integration, as the assertion of European values – whatever their meaning – was an intrinsic part of the project. The tension between economic integration and political/ideological integration was a permanent feature of the European Union and a permanent source of conflicts, primarily between the nation-states that were economically interested but politically aloof vis-à-vis the project, the UK and Scandinavia, on the one hand, and the major continental powers, France and Germany, on the other hand.

This difference in interests took a paradoxical twist in the decision to enlarge the EU towards the East. The interests of the two major nation-states, Germany (after re-unification) and the UK, converged in favour of enlargement but for opposite reasons. For Germany, it was a way to reconstruct its traditional geopolitical hinterland as part of the European project without raising fears of hegemony. For the UK, opposed to political integration, the more nations that joined the EU, the more difficult it would be to create a joint political decision-making body, thus weakening Brussels vis-à-vis the autonomous logic of markets that were becoming increasingly integrated globally. Ironically, it was the enlargement towards the East, and the subsequent migration of workers from Eastern Europe to the UK, that in part fuelled the anti-EU sentiments that found their dramatic expression a decade later in Brexit.

The result of these diverse strategies of integration was the construction of a complex network of nation-states with very different economies and cultures, whose full integration would prove hazardous. Thus, an economically strong EU was managed by a politically indecisive EU, without a common foreign policy, and hindered in joint decision-making by contradictory interests that could only be conciliated by a shift of executive power to the European Commission. The increase in efficiency was achieved at the cost of a crisis of legitimacy, as citizens around the continent resented the dependence of their lives on decisions taken by anonymous Eurocrats, barely controlled by the European Parliament. The shift of local and national power to European Union power, with the increasing transfer of sovereignty, created over time a ‘democratic deficit’ of representation in the EU countries.

In the context of a widespread crisis of the political legitimacy of representative democracy in many parts of the world, the distance between citizens and their representatives increased in the European Union. There was a growing gap between citizens and the decisions taken by the Council of Ministers away from the control of national parliaments. There was a gap between citizens and the European Parliament, whose composition and competences only indirectly reflect national constituencies. And, even more important, there was a gap between the powerful bureaucracy of the European Commission (sometimes symbolized by Presidents of the Commission who see themselves as Presidents of Europe), on the one hand, and citizens and the media in every country, on the other. In situations of normal institutional life, the tensions induced by the democratic deficit are tolerable. However, when there is any crisis of some significance (financial crisis, geopolitical crisis, migratory crisis, etc.) the distrust of European institutions accentuates the crisis of legitimation and ultimately may induce social unrest and political separatism.

Furthermore, the notion of a European identity has remained elusive. If we understand by 'identity' a set of values that provide symbolic meaning to people's lives by enhancing their feeling of belonging, it is difficult to discern the existence of a strong and distinct European identity. A self-defined European identity is indeed present in the minds of many citizens, particularly in contrast to 'others' (to the United States, to Asian cultures, to Islam, etc.), but largely as a rejection of the 'others' rather than as a specific identity that is valued and embraced in and for itself. Moreover, what surveys show is that even when self-identification as being European is stated, it is a weak identity, and it tends to be replaced by local, regional or national identities when the identity boundary has to be asserted in a situation of crisis.

This is precisely our argument. As long as there is smooth functioning of the fundaments of everyday life, work and livelihood in all dimensions, to have a European passport is an added value that is generally enjoyed and supported. But in the event of a crisis that requires solidarity between Europeans at large, the weakness of European identity gives way to the prevalence of national interests protected by the nation-state. Why bail out the Portuguese, said one-fifth of the Finnish electorate, by using 'our savings'? Why prevent the collapse of Greek banks, said the majority of Germans and Dutch, if they are responsible for their irresponsible behaviour? And why do Germans have the right to control our finances, answered the Greeks, if their only interest is to save German banks from their irresponsible lending? In sum: European identity, thus European solidarity, stops at the line (and the cost) of sharing the pain of crises that affect 'the other Europeans'. Moreover, many Europeans feel that the institutions of the Union are biased in favour of the dominant economic powers in the EU.

In a historical perspective, when nation-states had to construct their national identity, they used the powers of the nation-state to support their institutional projects. But in the case of the EU, the attempt to impose an identity to fulfil the European project triggered strong resistance that threatened the entire construction.

In short, in the absence of a crisis in the everyday life of citizens, the European project muddled through to become part of their experience. But when crisis hit, national identities quickly reasserted themselves to overrun a project identity that was, in any case, largely confined to economic and political elites. Furthermore, because of the democratic deficit in the European institutional system, every crisis deepened the crisis of political legitimacy, and fractured societies between 'the cosmopolitans and the locals', between North and South of Europe, and for many, between 'us and the others'.

There was an attempt to sanction the strategy of integration from above by a European Constitution to be approved by citizens. But the fiasco of the French and the Dutch referendums, when proposals to ratify the treaty establishing a Constitution for Europe were rejected by significant margins, stopped the legitimation strategy. The establishment of powerful mechanisms of integration, such as the euro, the free circulation of capital, goods, services and people, or the elimination of borders, were left to treaties approved by national parliaments under the control of mainstream parties, governed by the established political class.

The alliance of the visionaries of the European project and the economic and political elites favoured by European integration succeeded in accelerating the process of integration, adopting measures that were extremely difficult to reverse, such as the creation of the euro. Many economists at the time considered it an aberration to establish a common currency encompassing national economies vastly different in productivity and competitiveness, without a common fiscal policy and without integration of the diverse banking systems. But the real motivation behind the decision to create the euro was to integrate the economies, markets and policies, to bind together the participating nation-states with an economic glue that would be difficult to break, however imperfect it may have been and whatever the cost.

The global financial crisis of 2008 derailed the project because there were no institutions able to manage the crisis at the European level. In fact, in order to save the euro, Germany and the European Central Bank imposed tough policies of fiscal austerity that were able to contain the debt crisis temporarily, but with a high social cost in terms of the suffering of citizens in southern Europe and elsewhere and an even greater cost in terms of the political legitimacy of European institutions, to the point that Mario Draghi, the European Central Bank, and even Angela Merkel had to soften their stand on austerity policies after staunch resistance emerged from different quarters of the Union.

But it was too late. The price paid for the materialization of the European dream by the imposed unification of economic policies was the deepening crisis of legitimacy of the European project. Furthermore, the economic and social costs of the crises stemming from this forced integration were unevenly distributed between countries, between regions and between social classes and age groups within countries, fracturing any sense of pan-European solidarity and generating feelings of resentment among those who suffered most.

The tensions and flaws built into the European integration process created institutions that were crisis-prone, and their weaknesses were exposed when crises hit. In some cases these crises were of Europe's own making, while in other cases the crises had a broader international character, or were precipitated by processes that began outside of Europe; but in all cases it was the weaknesses in institutional design, stemming from the process of European integration, that gave Europe's crises their distinctive character. The financial crisis of 2008 stemmed initially from large-scale defaults in the subprime mortgage market in the US, but as the crisis spread it quickly brought the euro under stress and exacerbated the weaknesses that were already part of the eurozone. Moreover, the austerity policies designed by Germany and the European Commission to save the euro aggravated the economic and social crisis in Europe, particularly in the poorer countries of southern Europe and in the poorer segments of the population. The geopolitical crises with Russia and with the Middle East wars diverted resources and brought the whole of the EU into international confrontations that were only relevant for some of its members. And the refugee crisis, resulting in part from foreign intervention in Iraq and Syria (with the participation of some European countries), broke the solidarity among Member States and antagonized large segments of national populations, seeding xenophobia and anti-European sentiment throughout the territory of the Union.

Yet the crisis of the euro, and its impact on austerity policies, was the result of a flawed monetary and financial construction that resulted from the determination of a minority of countries, led by Germany, to make the integration deeper and irreversible, creating the conditions for a federal Europe – against the explicit opposition of the UK, Scandinavia and Eastern Europe. A similar argument could be developed on a number of European policies, including agriculture, trade and immigration. For instance, the Schengen agreement eliminated borders inside the Union without strengthening the controls at the external borders of the EU, thus creating institutional vulnerabilities that were brought into stark relief by the refugee crisis of 2015 – a crisis that also exposed the inability of European governments to act together in a concerted effort to assert the proclaimed European values in practice.

In sum: the ambition of the European project was belied by the weakness of European institutions, ultimately dependent on the dominant elites of the most powerful countries. The interests of these dominant elites shaped decisively the lives of European citizens via the impact of European legislation and institutional decision-making. In the absence of a strong European identity and under the conditions of the democratic deficit and the crisis of political legitimacy, the EU was unable to manage its crises as a single institutional entity and was unable to respond effectively and flexibly to the multiple fires that began to flare up inside the Union. Rather than dealing effectively with crises, let alone anticipating them and preventing them from arising in the first place, it found itself faced with increasingly severe internal social and institutional fractures. Brexit was perhaps the most dramatic expression of these fractures, epitomizing the potential reversibility of European unification. And the redesign of the European Union in the so-called 'Union at different speeds', as debated in the Bratislava informal summit in September 2016, was a sign of a new-found political realism that seemed to accept the fading of a dream in the interest of preserving what could be saved in terms of economic benefits and social stability.

The research presented in this volume explains the whys, hows and whats of the contradictory process of unification of Europe, both in its successes and its failures, as well as its consequences in the form of multiple, intertwined crises. Any future attempt to re-enact the European dream will have to consider first the European reality, coming to terms with the findings of our and similar inquiries in the hope of saving the project of a shared Europe, at peace with itself and its neighbours, as a key condition for a better world.

# Part I

## Economic Crises

# Chapter 1

# The End of European Integration as We Knew It: A Political Economy Analysis

*Olivier Bouin*

This paper presents a political economy perspective on the European integration process over the past sixty years. It analyses the very singular process that has been implemented for building up the European Union – a process that has been a strange mix of utopia, pragmatism, ideology and compromises. The central question of this paper is whether this complex process has delivered the promise of creating a sustainable, inclusive and efficient economic model for Europe. The first section looks at the systemic implications for the European building process of the increasing reliance on market-based solutions. The second section analyses the economic and social outcomes of European integration with a special focus on the convergence of economic performance across member countries. The third section focuses on the impact of the Economic and Monetary Union – by far the most audacious integrative step undertaken by European countries since the Treaty of Rome – on the future of Europe. The paper ends with concluding remarks on the plausibility of the end of the European integration process as we knew it.

## The choice of building the European Union relying on market forces

In this section, we will briefly discuss how the building of the European Union and the unfolding of its integration path have privileged the economic route, initially as a second best in the minds of the most pro-European leaders but increasingly as the main engine of European integration.

Chronologically, the economic route has been used because political integration and federalism were not possible. The failure of the

*Communauté européenne de Défense* in 1950, the limits of the idealistic federalist visions à la Spinelli and the lack of national political will in Europe had created a political context in which the founding fathers considered that economic integration – first trade, then financial or monetary integration – would lead to cumulative integration, known as the 'positive chain reaction' generally attributed to Jean Monnet.

Economic growth would be triggered by many positive factors. Larger internal markets would create economies of scale and would reduce transaction costs. Trade liberalization would better specialization and significantly reduce national opportunistic behaviours. A better allocation of resources – labour and capital – would lead to productivity increases that would support steady economic growth. The sheer size of the growing European economy would offer protection against destabilizing external shocks. All countries would benefit from the economic prosperity – the least favoured countries would be helped by structural funds to help catch the European bandwagon.

All this would lead to a convergence of national economic results, which would in turn reduce heterogeneity among European nations. Such a decline of heterogeneity would lower the cultural and political oppositions at the nation-state level towards a more integrated Europe. It would create the conditions for the production of European public goods, leading to further systemic integration and the final stage of political integration.

This narrative about the succession of integration steps can be considered the positive side of the chain reaction attributed to Monnet and present in the minds of his many followers (including European Commission presidents Walter Hallstein and more recently Jacques Delors and Romano Prodi). And, in all fairness, this narrative has been a powerful principle of action, because the European Union to a large extent delivered much of its good spillover effects between 1957 and 1985 (see the next section).[1]

But this positive chain reaction strategy has been critically and increasingly questioned on two grounds: the first dealing with the effectiveness, legitimacy and sustainability of such an integration strategy,[2] the second

[1] The large EU structural funding – mostly available for material and social infrastructure investment – kept playing a positive role in the catching up process of Southern European countries after the 1980s and of Central and Eastern European countries after the 1990s.

[2] A very significant amount of literature has looked at this issue. For recent contributions, see Meunier et al. (2015) who introduced the notion of 'failing forward'. In previous versions of this paper, I proposed the football metaphor of the 'kick and rush' to depict the European integration strategy. It is an indication of how doubtful I am about the possibility of proceeding with European integration as we saw it developed over the

considering the economic and political end point of the European integration process.

On the first question, a darker version of the chain reaction progressively gained importance in Europe as many of its member countries increasingly faced economic problems (the slowing down of economic growth since the mid-1980s, economic transition to a post-industrial system) and social hardships (rising unemployment and income inequalities). This darker version of the chain reaction can be described as follows: when some economic integration created (or was not able to avoid) economic and social imbalances and disruptions across Europe, the response to these problems would be more integration. Integration would continue to proceed with new initiatives because there would be no other (less costly) alternative. At stake would be a possible *remise en cause* of the entire European building process. An extreme – and rather cynical – version of such a building strategy is the reference to the half-built house (Bergsten 2012) that goes as follows: one begins constructing a house knowing that it will be too costly to stop – one has no alternative other than to finish building the house. Many authors since the end of the 1990s have been pointing out the increasingly negative and forced nature of the integration process and its consequences for the overall sustainability of the European construction (Scharpf 1999).[3]

As far as the second question is concerned, there is a very significant uncertainty about where the European integration process will lead its member countries. This uncertainty is to some extent instrumental to the process as most countries have a divergent view of what should be the end point of the entire process. This uncertainty can be observed at two levels. The first is fundamental beyond the scope of this paper: the equilibrium point between European integration and national sovereignty. The euro-federalists also have never given up their dreams to build a federal Europe (United Nations of Europe) and a strong ally has been the European Commission that has always pushed – with some ups and downs – for more Europe, with the ultimate aim of some degree of

past decades. A nineteenth-century English football tactic recycled by twentieth-century European politics is certainly not the safest strategy to lead Europe well into the twenty-first century.

[3] Because of the power of intimidation of the TINA (there is no alternative) argument, national governments and public opinion have been constrained to support further European integration and to accept intrusive European regulation and supervision. The emergence of the so-called ‘democratic deficit’ of Europe is in part rooted in this forced integration strategy pursued by the European Commission with the consent of most European leaders. Other significant factors explaining the ‘democratic deficit’ are the lack of a positive European identity (Castells, this volume) and the complex – and too many non-transparent – European decision-making institutions (e.g., Commission, Council, Parliament, etc.).

political integration. In that perspective, the referendum on the UK membership of the European Union in 2016 (and obviously its very striking outcome) has made very clear that for some member countries the objective was not at all more Europe but less European integration.

The lack of clear and shared adhesion to a joint integration objective has been a constant problem in the European building process. But as the integration process unfolded and the loss of sovereignty became more and more visible and problematic (touching upon increasingly key 'regalian' missions of the nation-state), the *qui pro quo* about the end point of the European integration became destabilizing enough to almost derail the entire process with the exit of a key EU member.[4]

Yet there is another troubling uncertainty or disturbing hidden perspective in the European building process. As we mentioned before, the European integration process has predominantly relied on an economic agenda and on economic forces, ever since the early 1950s and the creation of the European Coal and Steel Community. Social matters were not prominent in the Treaty of Rome and with the exception of the founding of the European Social Fund (the first structural fund to be created by the European Community) in 1960 and the signature of the European Social Charter in 1961, social policies were not put at the forefront of the European agenda. However, the general policy orientation of most national economies in the 1960s and in the 1970s (and therefore in an aggregated way at the European level) was a mixture of social democratic welfare state with some degree of Keynesian macroeconomic intervention to regulate cycles of mixed economies. The fruits of economic growth to be gained from European economic integration would be redistributed to the weak and the needy.

The progressive change of orientation at national levels towards more liberal, free market and private property based economic systems at the end of the 1970s/early 1980s changed the overall perspective. These national changes were reinforced by the pro-market approach supported by the European Commission. The Single European Act of 1986 that transformed the 'Common Market' into a 'Single Market' marked that change. It was the beginning of a new phase in the economic integration promoted by the European Commission. It was in the zeitgeist since, in 1985, the so-called Washington Consensus started a long cycle of liberalization, deregulation and privatization at a global scale (developed

[4] The Five Presidents' Report released in June 2015 favoured a deepening of integration – section 3 and 4 are respectively about the Financial Union and the Fiscal Union. Even though it applies to the eurozone members (and thus not to the UK), the overall objective and its implications for eurozone members and non-members seem to be clear: Europe is heading towards more integration in the coming years.

economies, developing economies and after the fall of the Berlin Wall post-socialist economies were to be subject to this implacable policy shift).

In this global context – even though the creation of the Single Market was accompanied in the mind of President Delors by a strong social pillar – it resulted in a radical but implicit change of perspective. Even though the social pillar was to be built and was high on the agenda of Presidents Delors and Prodi (with, for example, the revised European Social Charter in 1996), these efforts delivered little. The European Commission increasingly leaned towards more liberalization and deregulation. Lobbyist or vested interests obtained gradual deregulation of key markets including commodities that were not supposed to be exposed to market forces such as money, land and labour (see Polanyi 1944).

On paper, some European leaders were continuing to promote a social market economy but the change of policy orientation (away from Keynesian policies towards more austerity policies and away from a regulated version of capitalism towards a widely deregulated version of capitalism) impacted significantly the building of the European project.[5] The freeing of capital movements in 1998, the massive deregulation supported by the Amsterdam Treaty in 2000 (with the famous article 133 on qualified majorities), the Maastricht Treaty creating the Monetary Union in 2002, the Bolkenstein directive on Services in 2005, to name only a few milestones, changed the very nature of the European project. The end point of the European economic integration changed progressively from a social market economy (whether of Beveridgian or of Bismarckian origin) into a capitalist market economy (in the 1990s) into a capitalist market society (in the 2000s).[6]

It is ironic that social democrats such as Presidents Delors and Prodi did not see the sea change coming, that helping the economic genie to get out of the bottle would have systemic effects not only on economic structures and income distributions but on the type of social systems that would emerge and prevail for the decades to come. The strengthening of market forces in the late 1950s had a very different magnitude and meaning than the one that took place after 1985. Some European leaders

[5] Several heads of government in Central and Eastern European countries strongly supported such a pro-market and deregulation approach after their entry in the EU (e.g., Poland, Czech Republic, Estonia) and thus contributed to the strengthening of the shift towards reduced state intervention and an increasing private sector.

[6] Reference to the analyses of the embedding of market economies (à la Polanyi) as well as to the strong affinities between private property and market coordination (Kornai 1990) is here helpful. One can conclude from Kornai's analysis that in a dynamic economic system, market deregulation tends to favour private property and that privatization of state-owned enterprises tends to favour market coordination mechanisms.