OVERCOMING THE INSTITUTIONAL MISMATCH OF THE EURO AND EU

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1. Financial liberalization fuels and then reveals the Euro crisis

Since monetary stability does not imply convergence of the real economies nor financial stability, a form of financial federalism was necessary.
Figure 1 – Half century of European integration: building European public goods out of recurring crises

**PEACE IN EUROPE**
the founding public good

Prevention of European Wars → Coal and Steel markets → European Markets → Lowering of internal customs duties → European Directives → Collapse of the IMS → Single Act, revival of the common market → Recurring exchange rate crisis → European Monetary System → Worsening of exchange rate crises → Creation of the Euro

**COMPETITION**
The second European public good

**FINANCIAL STABILITY**
The missing fourth public good

A transitory compensation of real economic disequilibria → Financial integration

**MONETARY STABILITY**
The third European public good

Euro zone crisis
2. The institutional mismatch of the Euro zone is the real origin of its crisis

The incoherence of European / national institutions explain the painful process of “muddling through” from the Spring 2010 to June 2012.

1. The paradoxical consolidation of contradictory visions

2. Persist in the error: continue and strengthen austerity policies
3. A succession of erroneous diagnoses, a permanent underestimation of the severity of the crisis. Slow deliberation of European authorities, fast and imperative moves of financiers.

4. Slow deliberation of European authorities, fast and imperative moves of financiers.

5. The Rawls’ veil of ignorance is no more available for renegotiating an adequate, effective and fair European Treaty: losers and winners are known!

Figure 2 – The muddling through in the Euro-zone: the consequence of the conflict between the objectives and interests of a web of actors.
3. In the era of global finance, the only actor able to stop financial panic is the Central Banker.

1. In early June 2012, the most likely scenario was a victory of international finance in the breaking-down of the Euro zone...

....Since the European authorities had shown recurrently their inability to design relevant policies in response to the pressure of financial markets.
This pessimist scenario is brutally reversed by the bold statement from Mario Draghi on July 26\textsuperscript{th} 2012:

“\textit{Within our mandate, the ECB is ready to do whatever it takes to preserve the Euro. And believe me it will be enough [...]}

\textit{To the extent that the size of the sovereign premia (borrowing costs) hamper the functioning of the monetary policy transmission channel, they come within our mandate [...]}

\textit{We think that the Euro is irreversible”}. 

- Speech at an Investment conference in London
3. This strategic move sets into motion a virtuous process of “positive contagion” and makes credible the decisions of the 28-29th June European summit.

The financial international community is convinced that the Euro will last

A rapid decline in the cost of refinancing the public debt of the weakest European Economies

3. The European crisis is not over: the financiers are transitorily happy but Europe enters a recession and structural unbalances remain.

1. Any lag in implementation or bad surprise may again reverse the expectations of international finance.

2. The risk of collapse has decreased, but new unbalances have to be corrected: an austerity-led recession.

3. National governments disagree in their understanding of the 28-29th June agreements and quarrel about their implementation.
### Table 1a - Major structural disequilibria remain

<table>
<thead>
<tr>
<th>EU reaction</th>
<th>Positive</th>
<th>Impact</th>
<th>Negative</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Project of fiscal setting strict rules for public deficit</td>
<td>• Try to prevent the recurrence of Euro crisis</td>
<td>• A strait jacket stricter than SGP</td>
<td></td>
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<tr>
<td>• ECB decision: 3 years long credit to banks</td>
<td>• Comply with the expectations of international finance</td>
<td>• Austerity feeds a recession</td>
<td></td>
</tr>
<tr>
<td>• Banking regulation at EU level</td>
<td>• Remove the probability of bankruptcy</td>
<td>• Still no massive credit surge</td>
<td></td>
</tr>
<tr>
<td>• Surveillance, resolution and possible bailing out by ECB for major/key banks</td>
<td>• A response to Spanish dilemma</td>
<td>• Fear of speculative bubbles and inflation</td>
<td></td>
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<td></td>
<td>• A response to trans-border spill over</td>
<td>• Reluctance of Spanish government to ask for these funds;</td>
<td></td>
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<td></td>
<td>• A necessary complement to European monetary integration</td>
<td>• An excessive centralization, conflict with domestic authorities</td>
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<td></td>
<td>• Another transfer of a national sovereignty</td>
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<td></td>
<td></td>
<td>• Possible adverse impact upon the autonomy of monetary policy</td>
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## Table 1b - Major structural disequilibria remain

<table>
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<th>EU reaction</th>
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<tr>
<td>ECB states that the EURO will be defended at any cost</td>
<td>• A fast decline of related interest rate</td>
<td>• False feeling “the crisis is over”</td>
<td></td>
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<tr>
<td>Use the European budget to foster growth by infrastructures and help to innovations</td>
<td>• Return to private capital inflows</td>
<td>• No transmission to the real economy</td>
<td></td>
</tr>
<tr>
<td>European Summit June 2012: reduction of Greek debt, 3 years Commitment</td>
<td>• Recognition of a major weakness, on top of public finance issues</td>
<td>• Rebuttal by Germany of Euro-bound financed growth</td>
<td></td>
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<td></td>
<td>• (Provisional) end of Greek exit from Euro expectations</td>
<td>• Blocking of a EU budget /GDP increase</td>
<td></td>
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<td></td>
<td></td>
<td>• Pro growth / Competitiveness expenditures are the victims of the bargaining of Member-States</td>
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<td></td>
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<td>• Social sustainability of austerity programs</td>
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<td></td>
<td></td>
<td>• Ireland and Portugal ask for the same access to ECB</td>
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<td></td>
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<td>• UK threat that it cold exit from EU</td>
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</table>
4. - Nobody can anticipate for sure the future of the Euro: it is up to the strategy behavior of a complex web of actors.

1. Prolonging the past has become impossible.

“Europeans would be as strong as if Europe was united, retain as much sovereignty as if it was not. This contradiction has become untenable.”

Sylvie Goulard and Mario Monti (2012), *De la démocratie en Europe*, Flammarion.
### Table 2 – A tentative assessment of the seven scenarii

<table>
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<tr>
<th>Scenario</th>
<th>Strengths</th>
<th>Weaknesses</th>
<th>Political viability / Legitimacy</th>
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<tr>
<td>1. “Federalism by Technocratic Rationality”</td>
<td>Search for coherence and resynchronization of EU institutions</td>
<td>New reduction in national sovereignty</td>
<td>Weak unless strong political impulse by a charismatic leader</td>
</tr>
<tr>
<td>2. “Ordoliberalismus für Alle”: a German Europe</td>
<td>Integration without fiscal federalism</td>
<td>Does not overcome North/South structural unbalances</td>
<td>Deepening of the Maastricht Treaty principles that failed</td>
</tr>
<tr>
<td>3. “A North/South Divide”: a flexible exchange rate between two Euros</td>
<td>Overcomes the basic present unbalances by a return to growth in Southern Europe</td>
<td>A de facto breaking down of the EMU</td>
<td>A partial recovery of national autonomy but large political costs for federalists</td>
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<tr>
<td>4. “Chacun pour soi”: A wave of nationalism and protectionism</td>
<td>Recovery of national sovereignty</td>
<td>Possible large economic costs</td>
<td>A response to both left and ultra right demands</td>
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### Table 32 (follows) – A tentative assessment of the seven scenarii

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<td>5. <strong>“A British victory”: Free Trade Zone + Ad Hoc Partnership</strong></td>
<td>A reconciliation of the diversity of national interests</td>
<td>The end of the political federalism in Europe</td>
<td>A third way between complete collapse and a federalist Europe</td>
</tr>
<tr>
<td>6. <strong>“More democracy”: As a condition for a path towards a federal Europe</strong></td>
<td>A response to the erosion of EU legitimacy</td>
<td>Assumes that an European citizenship can be the cornerstone of a new EU</td>
<td>Dubious in the midst of economic depression</td>
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<tr>
<td>7. <strong>“International finance strikes back”: The storm after the calm</strong></td>
<td>Puts a pressure upon an unsustainable European configuration</td>
<td>Puts at risk the very basic European project</td>
<td>The real economic global power: complete mobility of huge amount of capital</td>
</tr>
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</table>
To learn more


- The Institutional and Political Crisis of the European Union and Some Ways for Overcoming It, *Perspective on Europe*, Special Issue, August 2013.
Early works on the Euro


More recent works


Last but not least


• *Overcoming the institutional mismatch of the Euro-Zone. Undetected by conventional economics, favoured by nationally focused politics, fuelled and then revealed by global finance*. Just published in Japanese, Fujiwara Shoten, Tokyo, February 2013.
Thanks for your attention and patience

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