

# ➤ The Strategic Opportunity of the Euro Crisis

John Stevens

**W**hen, on 15 October 1806, Heinrich vom Stein listened with unaltered composure to the tremendous tidings of the crushing Prussian defeat by Napoleon at Jena, his companions were astounded. They were even more astonished by his subsequent remark: 'Now, at last, Germany can be made.' How could the great patriot be so calm and so sanguine? Was not Prussia the principal hope of all who dreamed of German national unity? Had it not, through the genius of Frederick the Great, become the one country of that still nebulous *Volksgemeinschaft* which possessed the military and the Enlightenment virtues to resist the revolutionary imperialism of France? Had not Voltaire concluded his praise of the 'Teutonic marriage of Sparta and Athens' with the famous observation that 'in other countries the state has an army, in Prussia the army has the state'? Now that this army had been destroyed in an afternoon, the eclipse of the state would surely follow: its territories halved, its society humiliated.

But a quarter of a century in Prussian government service had persuaded the Freiherr not just of the brilliance and audacity of the Alte Fritz's achievements, but also of their fragility, stemming from their lack of rigour and popular support. And it had confirmed his conviction as to the intractable conservatism of German culture: the profound parochialism which prevented both rulers and people from realising the immense accretion of wealth and power that might flow from greater political integration. These were the roots of the disaster, but now that they had been exposed they could be dug out. Vom Stein saw, in short, that this supreme crisis was also the supreme opportunity. For only such a shock would be sufficient to shake Prussia, and thereby the whole nation, into making the fundamental reforms not just of substance, but even more of sentiment, that were necessary to secure survival and lay the foundations of future greatness.

## THE EURO'S FLAWED FOUNDATIONS

The creation of the euro was an act of astonishing audacity. It must be rated amongst the most ambitious economic policies ever attempted by a free society. Its central purpose was to release the potential revealed by the remarkable fact that for all its divisions and internal barriers, the per capita production of the European Union is not significantly inferior to that of the United States, with all its advantages of internal cohesion. If Europe could even approach a comparable level of cohesion, it would easily be the greatest economy, and consequently the greatest power, on earth. Its central premise was that the instrument of promoting greater European cohesion – the Single Market – could only continue with a single currency, since exchange-rate movements act as tariffs. Competitive deficiencies must be addressed directly, not evaded by devaluation and covert, politically manipulated protectionism. The euro also had a central prejudice, which seemed obvious but has now moved centre stage: that such cohesion needed to be achieved by harmonisation on the level of the best; not by an averaging out, let alone by converging towards the worst: levelling up, not levelling down.

Greece's performance must become like Germany's, not Germany's like Greece. All this is as clear now, as it was in the mid eighteenth century that Prussia, and all it represented for Germany, could only sustain itself by expansion, and could only expand by embracing liberal reforms.

For monetary union also has, of course, an ulterior purpose: as the apotheosis of Jean Monnet's method for bringing about his dream of a political Europe, a united European state. This had two aspects: what his biographer Sherrill Brown Wells has described as the incremental and the revolutionary. The euro is the supreme incremental economic initiative, which by becoming effectively irreversible forces a political and thus constitutional objective. But the euro is also the policy that is so big it breaks the boundaries of the elitist sphere of economics and becomes overtly political, precipitating the revolutionary moment Monnet, for all his gradualism and caution, always knew must eventually come, the 'transition from a technocratic unification of governments to a democratic unification of peoples.'<sup>1</sup>

The principal architects of the single currency were adept adherents of such incrementalism. They knew that its original design was flawed. The Germans knew they had failed to move the French (then vigorously supported by the British), away from the Gaullist vision of a 'Europe des nations' towards accepting a greater surrender of national fiscal sovereignty. The French knew they had failed to move the Germans (again vigorously supported by the British) away from the Bundesbank vision of national sovereignty in monetary management. Both knew that a coalition of other states (vigorously orchestrated by Britain) had blocked the harmonisation of tax rates and the increase in shared resources they considered essential for effective economic governance and monetary management. All the founding states of the euro accepted these flaws because they were convinced that sooner or later events – a crisis in other words – would force the changes they sought from each other, and even perhaps the changes they recognised they would have to make themselves. Would it have been better to have had a fuller, pan-European debate about the means and ends of monetary union before proceeding? Certainly. But as Jean-Claude Juncker chillingly confessed last year, 'we all know what to do, we just don't know how to get re-elected after we've done it.' The perennial dilemma of democratic rule, between leadership and followship, dictated that the art of what was possible in the present prevailed over the science of what was sustainable in the future.

Indeed, the tenets of the Maastricht Treaty were not just accepted as inadequate, but as unimportant. The frame of mind which welcomed the prospect that events would, in due course, force the improvements necessary to ensure the euro's sustainability also ensured that Belgium, the inner core of the European project par excellence, could not be excluded from its creation, despite historic debt levels in excess of the Maastricht criteria. And if Belgium, then surely Italy too, especially since Spain and Ireland had heroically achieved compliance. And if Italy, then Greece also. Did the other capitals suspect Athens of misrepresenting their deficit numbers? Certainly. Did they conclude it was manageable all the same? Absolutely. Such optimistic fatalism continued. Not only did those countries persist in failing to bring their finances within the limits prescribed by the Treaty, but first the Germans, then the French, then almost all the rest joined them in breaking the very rules that they had collectively committed themselves to as the proper starting point of the most significant act of integration since the Treaty of Rome.

Thus what Jorg Habermas has called the 'necessary and inevitable crisis of the single currency' was both expected and intended. What was not envisioned was that it would come as part of the gravest general crisis of the international financial system for three generations. Not that even this, now that the initial shock has passed, is perceived as particularly problematic. The stakes have certainly been raised dramatically by the turmoil of the credit crunch. The level of suffering being experienced right across the Union, especially by the young unemployed in the south, is truly tragic. But the levelling up of standards of practice and

---

<sup>1</sup> Jean Monnet, *Memoirs*, (1978).

performance in government, labour and money markets of which this is the inevitable price is already proving impressive. Who can doubt that clientism in state employment and tax evasion in Greece, and the profligacy and incompetence of regional administrations in Spain, are being addressed as never before. Who can deny the cleansing catharsis for politics and society of the eclipse of Silvio Berlusconi in Italy and Brian Cowen in Ireland? Who can dismiss the efforts to reign in spending and restore international competitiveness being undertaken all the way from Latvia to Portugal?

In the most crisis-hit countries of the Eurozone, the exposure of these flaws and the opportunity to address them goes far beyond matters of public and private economic management. It embraces every aspect of their national life. For instance, is it merely chance that in ascending order, Italy, Ireland, Spain, Portugal and Greece are the members of the single currency with the highest levels of income inequality between men and women? Though the measurements are perforce more tentative with regard to their ranking, also have the highest levels of inequality in employment between men and women?<sup>2</sup> Certainly not. Encouragingly, these statistics, and the broader reality behind them, are increasingly recognised in the public debates about addressing the crisis now underway in these societies. In short, what beckons is precisely the sort of national renewal and comprehensive modernisation that vom Stein envisaged, and to a very significant degree achieved in, Prussia from 1806 to 1814.

## REENGINEERING THE SINGLE CURRENCY

There is of course still an immense amount that must be done to secure the euro's stability and sustainability. But since this summer at least, the outlines of a resolution of the principal structural questions left open at its inception can be discerned. The capacity of the European Central Bank to drive interest rate differentials by the purchase or sale of government debt, to ensure they reflect real distinctions of performance rather than the speculation of a systemic collapse. A banking union, mutual fiscal oversight and enhanced economic policy co-ordination. The historic compromise between a Germany that breaks, to a degree, with the old narrow definition of the proper remit of monetary policy as price stability alone in favour of a broader recognition of the legitimacy of targeting employment and growth; and a France that breaks, perhaps by rather more than a degree, with the old narrow definition of the exclusively national context of budgetary control. Moreover, beginning with the nearly six thousand banks in the Eurozone, we are clearly going to see ferocious cross-border rationalisation, a harbinger of comparable, powerfully positive integrative processes in aerospace, telecoms, general utilities, retailing and transport.

There is every reason to suppose that provided the global economy remains stable, the Chinese economy recovers and re-orientates further towards domestic consumption, and the United States averts a fiscal crisis, the measures now in train will prove sufficient over the next two to three years to lift the Eurozone out of its current recession and return even its most depressed regions to the path of prosperity. Few now fear a recurrence of the imbalances and excesses which were the cause and the expression of the current collapse in production and employment. Who, for at least a generation, will lend excessively to the Greek or Italian governments, or invest with leverage in Spanish or Irish property? The guiding prejudice of the German government throughout the crisis is correct: that the more southern Europe resembles northern Europe in terms of fiscal discipline and competitiveness the greater and sounder that prosperity will be. Denying or evading this is to deny or evade the whole logic of monetary union. But the French instinct is equally accurate: that a much more politically and economically united Eurozone need not act externally, globally, merely like a larger Germany, but could enjoy a greater freedom to protect and promote the living standards of its citizens. The most cogent case for Eurobonds, for example, is not the mutualisation of liabilities *per se*, but that only

---

<sup>2</sup> K B Frederiksen, 'Income Inequality in the European Union', *OECD Economics Department Working Papers*, No. 952 (2012) <http://dx.doi.org/10.1787/5k9bdt47q5zt-en>

with an integrated government bond market comparable in scale, as a pool of liquidity, to US treasuries will the euro enjoy the full advantages of reserve currency status, which would include lower borrowing costs, eventually even for Germany.

However such a sanguine prognosis ignores the deeper, historic dimension of the global financial crisis: that at its core lies the sobering and related facts that the globalisation of the past three decades has, for the first time since the sixteenth century, precipitated a shrinkage of the Western middle class, and a fundamental shift of wealth and power from the West to the East. This has undermined our confidence in the depth and breadth of any return to European prosperity. Will the return to growth, even in the most competitive and developed regions of the Eurozone be sufficient to maintain, let alone enhance, our standard of living and of welfare? The rate at which this would certainly be so, and allow an orderly reduction of the accumulated debt overhang to manageable levels, is widely estimated to be between 3.5 and 5 percent. Is even that lower figure really plausible, even whilst allowing for the vast improvements in productive capacity locked up in Europe's myriad internal divisions?

Such pessimism is not, however, primarily economic. It resides instead in our current loss of confidence in many of the values our middle class promoted and made their own: the rule of law, civil liberties, meritocracy and democracy. Europe in general and the euro in particular have come to be seen, in far too many quarters, as part of this disenfranchising (one might even say alienating) mismatch between the power of markets – which has become international – and the power of politics, which has remained national despite being clearly crucial to resolving the crisis. Plainly, the economic opportunities of a completed monetary union will only be realised if the political opportunities it affords are also realised. Or rather, it is in the political realm that the truest hopes of the current crisis are to be found.

## **THE POLITICAL OPPORTUNITY OF ECONOMIC CRISIS**

Monnet never properly spelled out how the emergence of a European demos, which could confer democratic legitimacy upon the transition from an essentially economic to an essentially political union, should come about. He would not himself have called it 'revolutionary'. Rather he seems to have envisaged a gradual process of awakening. What else would one expect of the man who complained of '*les chocs rudes de l'histoire recente de la France*'? But history almost invariably advances by shocks and crises, and our present travails are no exception. Inseparable from the deep disenchantment and fear that the struggle to preserve the euro has generated across the Continent is an unprecedented awareness of a shared economic fate. If anything, the politicians are behind the people in this regard. Most have been reluctant to admit to their electors the degree of interdependence inherent in the euro. But the suggestion that it could be easier to put the whole enterprise into reverse than to carry on has not been believed, as the elections in Greece and in the Netherlands have demonstrated, however much the progressive realisation of the scale of the burdens this will entail is resented. Milward's pretence of national sovereignty that sustains the status of the European political class has been cruelly laid bare.

Some leaders have begun to rise to this new reality. For a brief period at the start of the year it seemed as if Nicholas Sarkozy would be receiving the overt support of Angela Merkel in the French Presidential elections: a dramatic step towards trans-national party politics in which the capacity to cooperate in delivering a shared solution to a shared problem would have become the centrepiece of the UMP campaign. In the event, caution in Paris rather than Berlin prevented the initiative, though now several of the ex-President's advisors admit that it might have delivered victory. Even if Francois Hollande's success was very much one of the old national politics, subsequently he has skilfully played upon his party's international ties with, for example, the German SPD and the Dutch PvdA. This is part of a wider increase in interest in the possibility of the June

2014 European Parliament elections being used to decide between candidates for the Presidency of the Commission, with names put up by the principal political groupings. Already, for example, Donald Tusk has been suggested by the centre-right European Peoples Party (EPP). There is the further dimension that such a contest could also constitute a de facto European-wide referendum on a new constitutional treaty, containing the changes in economic governance and the rest deemed necessary for the maintenance and further development of the monetary union.

However, if there has been one European institution which has signally failed to seize the political opportunities of the euro crisis it is surely the Parliament. Where were the MEPs when there was so desperate a need for someone to 'speak for Europe', to explain, at a supra-national level, the hard realities but also the potential rewards of making the euro work, to balance grim austerity with a vision that would make such austerity worthwhile? They were certainly not empathising, listening and campaigning in their respective countries, or making their chamber the focus of a continent-wide debate. This is in sharp contrast to the role played in Spain for example, by several leading MEPs in the late 1990s during the enormous patriotic effort made to achieve eligibility for euro entry. The key Economic and Monetary Affairs Committee (EMAC) has not become the forum its unique status as the body to which the Governor of the European Central Bank reports could have allowed. The decision of Mario Draghi to address the Bundestag to explain his bond buying programme must open the way for direct engagement by the ECB with other national parliaments, much to the detriment of the European Parliament.

In part this has been because the chairmanship of EMAC was both British and not a member of either the EPP or the European Socialists and Democrats, the two dominant affiliations in the Parliament. But it also reflects the continuing detachment of MEPs from the mainstream political debate in their home countries and their dependence on and deference to their national colleagues. The search for European democratic legitimacy seems likely to move to national parliaments. All sorts of ideas are being canvassed: synchronising national electoral cycles;

drastically reducing the numbers of directly elected MEPs and making up the numbers with delegates of national parliamentarians; granting to the latter the power to elect the President of the Council and the High Representative, with the former to choose the President of the Commission. It is too early to assess which of these may gain traction, but it is abundantly clear propositions are now being considered for realisation within the next two or three years that before the crisis would have been regarded as only achievable in some remote future. Jose Manuel Barroso's speech to the September Strasbourg Session of the European Parliament, for all its deficiencies of context and content, clearly marked a watershed in that it set out, for the first time in such a forum, a clearly federalist objective for the development of the European polity.

Achieving that most ambitious of objectives will require far more than a dry exploration of particular institutional innovations. It will need a new political narrative in all the member states of the single currency. I mentioned earlier that the crisis has clearly created an unprecedented sense of shared economic fate across the Eurozone, though obviously one which is far more a matter of resentment, rather than relief. But the real point is that it is recognised as being irreversible. Contrast this with the disappointed hopes of a number of the euro's advocates, including this author, that 'Europe in your pocket', notes and coins, would lead to a significant shift in European consciousness. There has long been anxiety amongst pro-Europeans that the old 'grand reason' for 'ever closer union', the prevention of war, had ceased to have saliency. Now, however, there is the chance to identify more Europe with real reforms of deeply entrenched deficiencies in national societies and cultures; the answer to mass anger against corruption, tax evasion and maladministration; the instrument for bringing down over-remunerated and parasitic elites whether in banks, or other privileged private cartels or publically-funded bureaucracies; the engine, in short, of a great modernisation.

## THE RISKS OF 'MORE EUROPE'

Of course, there are plenty of dangers here. So far, the anger generated by the crisis has been expressed almost exclusively by anti-European interests. Can that be turned around? Anger is invariably an important element in all radical reforms of public attitudes and behaviour, but especially for processes of unification. Who is the enemy now? I have been struck by the parallels between the emergence of internal enemies in the crisis countries, such as corrupt officials and tax evaders, and the discourse over trade unionism in Britain during the 1980s. But historically it is usually external enemies that prove to be decisive in forging political unifications. The Cold War provided this for the founding phase of the European project, in as much as it was perceived as the economic and political underpinning of NATO on this side of the Atlantic. The fall of the Soviet Union removed this *raison d'être*.

Globalisation has brought forth a mixed bag of new potential enemies. The collapse in competitiveness across southern Europe is already linked in the popular mind to the rise of Asia, and especially of China. So far, however, there has been little appetite for the logical conclusion from such concerns: that the exclusive competence the Commission enjoys in external trade policy should be deployed to ensure import substitution. This is despite the fact that the Citizens Initiative created by the Lisbon Treaty could easily become a powerful tool for pushing such a policy. The United States could take a protectionist turn in the near future. Eventually when fiscal and monetary means of promoting employment are exhausted, there remains nothing else. Such policies would surely have an impact across the Atlantic.

Great though the potential of efficiency gains across the Eurozone from 'more Europe' is, it remains a big ask, even making allowance for the diminishing advantages of low labour costs in the evolution of the global economy, to imagine that this will manifest itself in the short run by a return to the levels of growth experienced across the Continent in the 1950s or 1960s. Yet these are the levels we will need to painlessly pay down the current accumulation of debt and secure the basic architecture

of our welfare provision, especially for retirement. Even Germany's export orientation is stressed by counterfeiting and plagiarism. More managed trade will probably prove more palatable in Berlin than a prolonged period of structurally higher inflation, which is the plausible alternative. The part played by preferential trade policy in the creation of both Germany, following the Napoleonic War (Friedrich List considered himself a disciple of vom Stein), and the United States, following their civil war, is well known. It would be an extraordinary exception if the construction of a more united Europe did not, to some degree, follow a comparable path.

Even more troubling has been the significant overlap between hostility to European integration and hostility to immigration. The increase in labour mobility within the Eurozone, precipitated by the crisis, is beginning to be on a scale sufficient to have quite some beneficial economic effects. Whilst this has been welcomed in, for example, Germany, elsewhere there are concerns it could exacerbate existing tensions, in particular with significant resident and naturalised Muslim minorities. Islamophobia is not necessarily, nor very obviously, in the strictest historical sense, anti-European. But it is plainly in crass contradiction to the general liberal values of tolerance and multiculturalism shared by the overwhelming majority of those promoting further political integration for the EU. Identifying the internal enemies who are holding back modernisation will be very tough. But it will also have to be very disciplined, so as not to allow sentiments to come to the fore which do long-lasting damage to the underlying purpose of the process: the preservation and further development of the compassionate, open, free law-based culture that has come to be seen as quintessentially European.

The economic opportunity of the euro's crisis is a substantial qualitative improvement in the efficiency of the southern European economies, which will feed through into a fundamental rationalisation of the whole Eurozone. This will start with the financial sector, but will widen out from that over time to grip every sector. But the political opportunity is even grander: nothing less than to prove that an international democracy is possible. It is no exaggeration to say that the very future of democracy turns upon the

outcome, for unless representation can operate upon the same level as the economic forces it seeks to balance and modify in the public interest, it will surely perish. Undoubtedly there are enormous uncertainties over whether these opportunities will be seized, even partially, and there are also great dangers along the way. Vom Stein was deeply disappointed by the imperfections and inadequacy of what he achieved. Many of his liberal and democratic proposals were rejected, with lasting malign consequences. Nevertheless, it is generally recognised that his vigorous response to the crisis Prussia faced 200 years ago made the eventual emergence of a strong, unified German state inevitable. I am confident that we are now seeing the process which will make the emergence of a strong, unified European state inevitable too. ■