

## **Debate on an EU fit for purpose in a post 2009 global age**

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**London School of Economics and Political Science**

**Foreign Secretary, David Miliband**

**Foreign Secretary, David Miliband, took part in a debate on an EU 'fit for purpose' in the global age at the London School of Economics on Monday 9 March.**

### **Speech**

This is an important moment for the world economy, and therefore for the European Union. Markets with effective regulation and institutions built for cooperative politics have been at the heart of the European model for five decades. They have been the basis of its successes. I want to talk today about the tests Europe faces in the coming months, and how the EU can respond.

I don't believe it is an exaggeration to say that the economic crisis is challenging the European Union's core values and institutions. Our belief in the long term benefits of the freedom of people, money, goods and services to move across borders is confronted with the short term temptations of protectionism. The leadership the EU has shown over climate change is faced with calls to step back and reconsider. The sense of solidarity within Europe, between East and West, rich and poor, new and old is under strain. The achievements of the last thirty years - from the single market and enlargement to the euro - are being tested as never before.

The Prime Minister has set out the global nature of the crisis and the need for a global response. He has set out the national and local impacts of the crisis, and the need for national and local action. But he has also explained that European action needs to be part of the response too. The global economic crisis shows the need for Europe and the need for reform in Europe. That is what I want to focus on today.

The economic crisis will be used by many people to argue that the EU should postpone reform. I believe the opposite is the case. Now is the time we need new reform to preserve the gains of the past. The truth is that the single market, enlargement and the creation of the Euro have made Europe more effective not less. But the way to preserve these gains and to defend them is to build on them, by developing the flexibility, resilience and global reach that is essential in the modern world.

My argument is that reform is the friend of pro-Europeans not its enemy. Reform of the way we regulate and supervise financial services to promote resilience of the whole system. Reform of how we use European budgets to promote low carbon recovery. Reform of our labour markets to put the emphasis on skills and human capital, helping workers if they lose their jobs. Reform of our energy system to increase support for vulnerable European countries. And reform in the way we cooperate with our neighbours South and East, so that the EU is a partner and not just a destination for countries beyond its borders. Comprehensive reform can help Europe survive the crisis and come through it - in the words of your report - more 'fit for purpose for a global age'.

To defend and advance the European project, I believe we need make progress on three areas.

## **Economic reform**

First, economic reform. The European added value here is at least three fold:

- bringing the weight of coordinated action to macroeconomic need; this has been done through successive European decisions, notably in respect of the necessary fiscal stimulus across Europe
- upholding and aligning national financial regulation and infrastructure
- and using European budgets to promote the skills and science of the future.

For some time globalisation has brought increasing prosperity through trade in goods, the exchange of ideas, the movement of workers and cross-border finance. But financial globalisation has also created the conditions for a truly global crisis. Many of the fastest growing economies have been thrifty, pushing up global savings and pushing down global interest rates. This, in turn, created the "search for yield" as investors in developed countries sought higher returns. And it sparked an unprecedented wave of financial innovation as bankers responded by finding new ways to package risk and move it off their balance sheets, allowing them to lend more with less capital.

But we now know that this financial innovation did not reduce risk; it simply moved it around the system. And as the banks lent more and more, the risk within the system built up. Regulators around the world failed to keep up with financial innovation and stop the build up in systemic risk. This failure threatened the security of people's savings and pensions, and now, as it moves to the real economy, of their jobs and homes. This is why regulation needs to change in response to this crisis, in Europe and globally.

As both Alastair Darling and Adair Turner have argued, we need to look again at how much capital banks are required to hold. We need to look at how to regulate liquidity. And we need to regulate the shadow and near banking sector so that institutions that perform bank-like functions are regulated in the same way as banks. However, the biggest intellectual leap we have to make is to focus on systemic risk, rather than just specific institutional risk. The interplay between different factors have to be monitored not just the activity of a particular organisation.

Market-wide, systemic risk does not stop at the border of any one country. The potential for problems to spill over between institutions, sectors, and countries requires better coordination between finance ministries, banks, and regulators. This must happen at a global scale - hence the importance of the London Summit - but also regionally.

Alistair Darling has welcomed the de Larosiere report as an important contribution to the debate on improving supervision and regulation within Europe. Building on the ideas in the report the Chancellor has proposed:

- a new, independent European early warning body bringing together macro economic and financial market issues;
- a single independent body to become the source of technical financial rules, ironing out national divergences;
- EU single market rules to deliver a legislative framework for closer integration and consolidation of EU financial infrastructure; and
- And a fundamental review of the safeguards for cross-border banking models in the single market.

Beyond addressing the current crisis, we must also prepare Europe for the long term. The financial bail-outs must be used to support the longer-term restructuring of the European economy. Europe needs more world class universities and more investment in R&D if it is to compete on quality and innovation rather than cost. Many countries still need to make their labour markets more flexible - as the recovery begins companies must be both able and willing to risk employing additional staff, to try to expand and grow. The economic crisis should not be used to abandon our commitment to completing the single market and taking forward the Lisbon agenda for jobs and growth, but a spur for its renewal.

## **Energy and Climate Change**

The second area of reform is energy security and its twin climate security. Last December, the EU adopted a bold energy and climate package to cut greenhouse gases by 20 per cent by 2020, or 30 per cent if other developed countries adopt similar reductions.

This year we need a similar level of ambition at a global scale at the summit in Copenhagen. The pressure will be for the world to delay the transition to a low-carbon economy, to lower our sights. We simply cannot afford to do so. Avoiding dangerous climate change requires investment now to stop a new generation of high-carbon infrastructure from being built.

The transition to a low-carbon economy is not just an environmental issue or a long term one. It is core to European security and prosperity now. In January, the dispute between Russia and Ukraine left Bulgaria and other parts of Europe without gas for two weeks during one of the coldest winters in years. Last year, soaring commodity prices led central banks to act to curb inflation, just as the credit crunch was starting to demand lower interest rates. Now, to fight the recession and prepare for a sustainable recovery, the EU has an important and underestimated role to play.

- As we face rising unemployment, investment in new energy infrastructure - including energy storage, interconnectors, efficient homes, renewable power and Carbon Capture and Storage - could be a major source of new jobs.
- The EU Emissions Trading Scheme and EU regulation must be used to push forward technologies such as carbon capture and storage and electric cars.
- Open and transparent energy markets - critical to ensure more solidarity between Member States and to effective competition that will benefit consumers - must be rapidly taken forward.
- The EU budget will need to be aligned with today's problems of energy and climate security, rather than the post-war problem of food security.

## **Neighbourhood**

The third area of reform is our relations with our neighbours. The last year has shown the interdependence between EU Member States and those on our periphery. Problems spill over, they are not bounded by geography. Some central European banks are exposed when they lend Euros to countries facing stark economic contraction. British savers were affected when Icelandic banks collapsed. A Ukrainian gas crisis turns the heating off in Sofia.

The temptation, given the severity of the economic crisis, is to turn inwards and focus on domestic problems. That is understandable. But solidarity and support between nations is a vital part of the European compact.

Why? Because we have seen over the last twenty years how the prospect of EU membership can transform countries, and embed both peace and stability. It is a powerful tool.

Thanks to intensive political engagement, peacekeepers, development assistance much of the Western Balkans is unrecognisable from the images we saw in the 1990s. But the region is still scarred by ethnic tensions. Scratch the surface, and the nationalist politics is still very much alive. If we want to overcome these divisions, to generate stability for the long-term, the offer of EU membership, and the process of reform that EU accession involves, is our best, perhaps our only hope.

As for Turkey - a country of huge potential - the EU accession process and the reforms that it requires is already bringing benefits. Turkey is now a much more stable and attractive economy for foreign investors, and until the recent downturn it was growing at an impressive 7% a year. Of course we have other key interests at stake in Turkey: its strategic position makes it a logical transit route for energy from both the Middle-East and Central Asia, and a key force for stability and prosperity in regions on Europe's fringe.

But beyond these countries, there are others - Iceland or Ukraine for instance - for which, though there is no formal membership commitment, we must keep open the prospect of membership. And for those that are either not eligible for full membership or do not want to join, we need to intensify our cooperation on areas of mutual interest.

That means more effort to dismantle the barriers to trade and strengthen our economic ties with the countries of the Maghreb, the Middle-East and on our Eastern borders. If we are serious about diversifying our energy sources, it means examining how we might harness the solar power of North Africa. And it means more intensive engagement to resolve the conflicts on our borders - whether the Arab-Israeli dispute or the problems in Georgia - because the impact of these conflicts is felt far beyond their epicentre.

The new initiative on the Eastern Partnership, which will be launched in Prague in May, is an important step in the right direction. Because the focus is about bringing these countries more closely into the European economy and about learning from and replicating the Union's successes. So while there will be more EU projects and refocused EU funding, there will also be more emphasis on the countries of the region work together on areas of mutual interest. Because if Ukraine, Belarus, Moldova, Georgia, Armenia and Azerbaijan can cooperate on energy, forge common standards on environmental protection and dismantle their own barriers to promote free trade, it will boost stability and prosperity across the region and help raise standards to EU levels.

## **Test for Eurosceptics and Europhiles**

I have talked so far about how the economic crisis is a test for Europe's values and institutions. But I want to end by talking about how it is a test for the assumptions both of Europhiles and Eurosceptics.

To eurosceptics, to those who feared "too much Europe", who argued that the EU should be a single-market or trading block and no more, I have a simple message. Instead of beating up the straw man of a federal-state, I would urge eurosceptics to defend Europe against the real threats we face - for example the fragmentation of the single market, which would have a devastating affect on the UK economy. But today, the best defence against encroaching protectionism is an effective European Commission. You cannot be in favour of the single market, but against the very institutions that preserve the rules of the game. This is the fundamental contradiction at the heart of the eurosceptic position.

Over the next year, we need to defend the political institutions in Europe, if we want to maintain our economic freedoms. We will need to be fleet of foot, adapting and innovating, in order to deal with

unprecedented and rapidly changing risks. The scale of the economic crisis has forced politicians across the political spectrum to re-think their view of the role of the state in stabilising markets. I hope too it forces a re-think in how we view Europe.

To Europhiles, there are also lessons. The correct decision not to join the Euro when the five tests were applied has not left Britain at the margins of Europe.

The so-called British agenda but in fact the agenda of progressive forces around Europe - of social and economic reforms under the Lisbon Strategy, of budget reform and enlargement - are not a means of diluting the European project but strengthening it, and have been seen as such and developed strength as a result.

## **Conclusion**

This evening, I have focused on the test that Europe faces. Let me finish by talking about the opportunity.

Last summer, after the Irish referendum result, I said that it was no longer clear to the citizens of Europe, what purpose the EU served. Europe's success had left people wondering about its future *raison d'être*.

The economic crisis is a reminder that the historic successes of the EU - the single market, the euro, enlargement - cannot be taken for granted. They need nurturing and reform if they are to be truly lasting achievements.

Your report talks of 'a global age'. But the global age is no longer a given. Like the last age of globalisation, which unravelled on the streets of Sarajevo, today's global age is fragile. It is a fragility born of the fact that while our economy has gone global, our politics remain primarily national. The sense of powerlessness that breeds can either force us to scale back our economic life and embrace protectionism and nationalism. Or it can inspire us to scale up our political institutions to match the continental and global reach of our economies. The EU - for all its faults - is the best way of bridging the gap between a globally interdependent economy, and strong national political identities. That is the case we must make to our citizens in the next year.