## Summary of the report

# Which Economic Governance For the European Union? Facing up to the Problem of Divided Sovereignty

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For a long time, successive French governments were a voice in the wilderness in favor of stronger economic governance (*gouvernement économique*) within the European Union. In February 2010, however, German Chancellor Angela Merkel mentioned for the first time the necessity of a European economic government (*Wirtschaftsregierung*). Merkel's unexpected rapprochement with President Nicolas Sarkozy gave a second wind to the notion of *gouvernement économique*, yet the path to stronger economic governance remains elusive. The main difficulty today no longer stems from lingering French-German disagreements, but from an originally unforeseen conflict between national sovereignty and a new conception of sovereignty that called for its exercise at the European level. Sovereignty over Europe's Economic and Monetary Union is fundamentally divided – monetary policy is unified at the EU level, yet most other powers remain firmly in the hands of national governments.

In fleshing out this argument, this report considers critical issues of economic governance from the perspective of sovereignty in the European Union and highlights key political obstacles that must be surmounted if these issues are ever to be addressed in a satisfactory manner. Far from being new, the problem of economic governance emerged with the origins of the euro at the time of the Maastricht Treaty – and it has nagged policymakers ever since.

The report begins by reviewing the existing literature on economic governance. Despite the fact that French politicians have talked about *gouvernement économique* for many years, there are few academic and policy papers fleshing out the notion in concrete terms. Some scholars have envisioned the problem of economic governance as a tractable problem that would be resolved over time. Others have considered economic governance as a critical problem that could undermine the very existence of the euro. The report highlights both the lessons and the shortcomings of this literature. While the second interpretation has become more salient over time and especially since 2008, the literature suggests no magic formula to strengthen the European Union's economic governance without further encroaching on the economic sovereignty of its member states.

After reviewing the literature, the report dissects political actors' aspirations for a *gouvernement économique* as they have manifested themselves since the origins of the euro. It interrogates the remarkable resilience of this aspiration, not only within but increasingly beyond French political circles. Europe's political leaders started groping for a more collective way to exert their sovereignty at a time when the European Monetary System was periodically the object of speculative attack and when many member states resented the dominance of the German central bank in monetary policy. Until 2010, however, the longstanding French aspiration to stronger economic governance seemed like a non-starter at the EU level. German political leaders were especially critical of *gouvernement économique*, suspecting the French of a desire to curtail the independence of the European Central Bank. Yet the global financial crisis acted as a spur for new political initiatives on economic governance. As early as the second half of 2008, the French presidency of the EU pushed for an orderly European response to the banking crisis and to the risk of a Europe-wide recession. By 2010, the sovereign debt crisis revealed a crisis of economic governance within the euro area and led to a flurry of new initiatives.

The question now is whether member states are ready to continue moving toward greater sovereignty at the EU level, or whether they will want to reassert the national locus of sovereignty. Assuming that the member states will not want to jettison the euro, the report concludes with policy guidelines toward a more crisis-proof economic governance structure at the EU level. It starts by explaining why the current status quo of sovereignty divided between the EU and the member states in the governance of the euro has become increasingly untenable. The Greek and then the Irish debt crises have demonstrated that the euro area is not immune from a major crisis of confidence that would cut access to capital markets for its most vulnerable member states and potentially spread across the region. The challenge at this point is to shift toward an economic governance model that is realistic for the member states to adopt, yet bold enough to convince financial markets that the EU has found a credible development scenario for its Economic and Monetary Union.

The report considers three boundary conditions that dictate clear guidelines for establishing stronger economic governance in the short term. First, the member states are not willing to hear of any kind of transfer union. This dictates that member states must find better ways to enlist the support of financial markets for debt consolidation and fiscal discipline. Second, the member states are reluctant to delegate more power to Brussels. This implies that the debt consolidation framework must be externalized to non-EU bodies or independent European agencies as much as possible. Third, the member states are reluctant to see their autonomy curtailed. Any new economic governance framework must therefore give as much say as possible to governments in the decision-making process, in order to foster ownership of potentially painful decisions by all euro-area governments.

The above guidelines are no panacea to resolve the deep problem of divided sovereignty within the euro area. The newly found discursive consensus in favor of stronger economic governance will be tested, and it may not survive under stress. At that point, more radical action may become necessary. In the long run, a need to rebalance divided sovereignty within the EU is almost certain to emerge. If they want the euro itself to survive, the member states must be prepared to put their money where their mouth is.

*The full report is available at www.sieps.se*

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