EU Political Economy Newsletter

Newsletter of the EUSA EU Political Economy Interest Section
http://www.eustudies.org/pesection.html

The EU Political Economy Interest Section is an official section of the ***European Union Studies Association****.*

Section co-chairs: Erik Jones and Amy Verdun
Managing editor: Alasdair Young

Issue 2 Spring 2004

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Letter from the Section Chairs

We are approaching the end of our fourth year as section chairs and the section has grown dramatically since its founding. We started with something like 10 signatures. Now we have more than 200 members, representing institutions in more than 20 countries.

We hope that as many of you as possible will be able to make it to the EUSA Ninth Biennial International Conference that will be held in Austin, Texas on 31 March to 2 April 2005. There is an enormous amount of work being done on the political economy of the European Union and the EUSA conference is the best place for us all to get together. The call for proposals will be issued sometime this spring. If you need help pulling together a panel of your own (or joining one that is under construction), please make use of the interest section, its mailing list, newsletter, steering group, and, of course, its co-chairs. These avenues make the section an ideal resource for putting scholars in touch with one another and for developing panel proposals. Nevertheless, the program committee is primarily responsible for accepting proposals.

In the meantime, we remain active on other fronts. Our edited volume on the political economy of European integration is nearing completion, and we plan to submit the final manuscript at the start of March. Routledge will publish the volume in both paper and hard-cover, and we hope that you will find it suitable for course adoption in the fall of 2004. Once the publication schedule is confirmed, we will be sure to send you more detailed information about the volume and its contents.

We have also been active in attracting EUSA members to other conferences. The ECPR Standing Group on European Union Politics will hold its second Pan-European Conference in Bologna, Italy, June 24-26, 2004. Erik Jones and Meltem Muftuler Bac (Sabanci University) are the main local organizers of the conference on behalf of the ECPR Standing Group. The conference (continued overleaf)

Also in this issue

is subdivided into fifteen so-called 'sections'. Amy Verdun and Francisco Torres are organizing the political economy section of the conference, and the number of proposals that they have received has been impressive. We hope many of you will be able to attend the conference even if you do not present. The conference details can be found at http://www.jhubc.it/ecpr-bologna and it is updated regularly.

Finally, we have approached the editors of the new on-line journal *European Political Economy Review* in order to see how we could establish some basis for closer cooperation between the journal and our interest section. We have been impressed with the quality of the journal in its first two volumes and would encourage you to take a look. You can find it on-line at http://www.lse.ac.uk/collections/EPER/default.htm.

Looking to the future, we have agreed with the management of EUSA to stand down as section chairs after the EUSA conference in Austin. As we noted in our previous letter, the steering group that we put into place after the Nashville conference is providing ever more stable leadership. The newsletter has regularized communication. All that remains is to find candidates to take the organization into the future. We hope that you will regard this need to change the section chairs as a strong incentive to come to Austin and to participate in the elections that we will be holding. The group is only as strong as the participation of its members. We are proud to have brought the EU political economy interest section this far, but realize that new leadership is required to take the next step.

We very much look forward to seeing you all in Austin. Once again, please let us know if there is anything we can do to help you in responding to the call for papers.

Sincerely,

Amy and Erik

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Review Forum

Turbulent Times for the Stability and Growth Pact

Mary Farrell, Forum Editor

The European Union's Stability and Growth Pact, designed to ensure the smooth functioning of monetary policy by requiring governments in the euro-zone to limit budget deficits to no more than 3% of gross domestic product, came under severe criticism at the end of November 2003. For many observers, the failure of the Council of economics and finance ministers (Ecofin) to stick with the rules of the pact and impose sanctions on Germany and France, two countries about to breach the deficit rule for a third year running, was a reflection of a weakened commitment towards the pact.[i] Barely a month later, the member states failed to agree on the draft constitutional treaty proposed by the European Convention under the leadership of Valéry Giscard d'Estaing. As the EU approaches the date for the accession of ten new member states (all of whom are committed to euro entry in the future) the question is whether the difficulties in implementing the Stability and Growth Pact constitute a fundamental threat to the functioning of euro-area policy and ultimately to European monetary integration.

Monetary integration was never going to be easy. The Maastricht Treaty and the subsequent Stability and Growth Pact were both attempts to facilitate the process through institutional arrangements and binding political commitments by the member states. Despite the economic difficulties and recessionary conditions across Europe during the early 1990s, the member state governments made strenuous efforts to cut public spending, reduce debt and bring inflation under control in their national economies in order to meet the commitments of monetary integration.

From the beginning, the nature and pace of adaptation to monetary integration was uneven across countries and, even as governments took the necessary steps to bring public finances into line. Broad public support and national consensus over the future implications were never really considered.[ii] The top-down nature of monetary policy-making in the individual countries and at the European level meant that opposition to fiscal rectitude was muted. These are not policy areas generally characterised by participatory democracy or by wide-ranging consultation beyond the narrow band of elite groups within government and financial/banking circles.

The objectives of the Stability and Growth Pact stem from the anticipated difficulties in keeping governments to the budgetary limits once the euro was adopted.[iii] The pact was intended to prevent budgetary deficits and to ensure sound management of public finances so as to avoid a situation where one member state's budgetary policy would adversely affect the other member states through higher interest rates, and ultimately impinge upon the economic stability of the euro area.

The European Commission is responsible for monitoring the implementation of the Stability and Growth Pact. Since 2001 a number of infractions of the pact's rules on budgetary policy have occurred, prompting the Council to issue warnings to Ireland in 2001 and to Portugal, France, and Germany in 2002. The budgetary positions of all these countries have subsequently deteriorated, and by the end of 2003 most of the larger euro-zone countries were in breach of the pact.[iv]

It is not surprising then that the Ecofin Council's decision not to impose sanctions under the excessive deficit procedures called into question the very sustainability of the pact and renewed debate over the reform and future of the arrangement.[v]

What is the current problem with the Stability and Growth Pact? Is it simply a question of the technical content of the arrangement, and the difficulty of keeping governments within the fiscal constraints? Or is the problem a more fundamental one related to the underlying premise upon which the arrangement is based, namely the assumption that stability and growth are possible within a single policy framework?

The rationale for having common rules on budgetary policy is to prevent deficit spending by one country increasing inflation, and hence forcing the European Central Bank (ECB) to raise interest rates.[vi] This is a perfectly reasonable position in the context of the overall aim of stability. In practice, the euro-zone has succeeded in maintaining price stability, although inflation hovers above the range set by the ECB.

The real problem lies with growth, and it is here that the European economies have failed to reach their targets. Economic growth is desirable in itself, but it is also essential to the continued ability of the member states to operate within the guidelines and strictures of the Stability and Growth Pact. In particular, for governments to increase public spending over the medium to long-term and still remain within the 3% limit on public deficits, it is estimated that annual economic growth would need to average around 5%.[vii] So far, none of the European economies has growth rates anywhere near this level.

Many of the deficit-prone countries have argued that the obligation to cut public spending adversely affects economic growth at the very time when it is most needed, in the downswing of the economic cycle. Instead of having to cut public spending under the deficit rules, there is a growing support for allowing countries some leeway in public spending, particularly to support structural reforms and for capital investment. Critics of this position say that the Stability and Growth Pact does not prevent governments from investing, provided they can raise enough in taxation to cover such expenditure. On the other hand, there is the problem of defining and identifying what public spending is for investment and what should be categorised as current expenditure. This is indeed not a new problem, and member state governments have resorted to creative accounting in their public finances since the plan for monetary union was first mooted. So, growth is needed to keep European member state governments within the straitjacket of the deficit rule.

There is a second reason why growth is significant – it relates to the structural and demographic conditions within the member states. Across Europe the dependency rate for the population aged 60 and over is expected to rise and birth rates to continue to fall. With more retired people and fewer people of working age, European governments will have increasing difficulties in meeting their rising commitments on pension liabilities while remaining within the strict guidelines of the Stability and Growth Pact.

Without economic growth over the long-term, the dilemma will be where to make the cuts, and who to target in assuming the burden for the state's conflicting set of responsibilities. Currently, the European countries finance pension payments out of tax revenue with up to one-fifth of public spending being allocated to pensions and healthcare. While Britain has gone some way to changing the funding system towards private pension provision, very few of the other countries have followed the same route. The British case also highlights the pitfalls of privately-funded pension arrangements, and particularly the need for greater regulation and stronger governance to guarantee future entitlements.

Pension reform is one area of policy that will need to be addressed if the Stability and Growth Pact is to continue to operate in the future. The other broad area of concern is that of structural reform. European governments declared their commitment to structural reform at the Lisbon summit meeting in 2000, with the aim to establish the European Union as the leading global, knowledge-based economy by 2010. Progress towards the achievement of the Lisbon Strategy goals, however, has been slow – structural reforms in the labour and goods markets, improved productivity and technological innovation have still to be realised.[viii]

These are worthwhile goals for any and all of the European countries – the underlying argument for structural reform rests on the need to make labour markets more flexible (hence leading to higher employment) and more competitive (through greater productivity) – yet there is a tendency to regard growth as being directly attributable to the degree of market flexibility. However, modern growth theory suggests that other factors play a part, including the quality of labour, and the quality and quantity of the physical and technical infrastructure. This means that growth factors are closely bound up with public investment levels through the education system, the technological and innovation system, and the stock of physical infrastructure in a country.

The Stability and Growth Pact was not the result of any detailed academic discussion. Nor indeed was it discussed or debated widely at the national level, with different social groups and the broad spectrum of political opinion seeking to make an input and defend their particular interests, and collectively reaching a form of consensus on the nature, substance and rationale for the pact. Instead, it was a pragmatic response to the concerns of many (especially in Germany) that EMU would lead to inflation, and was very much a top-down decision.

The real import of the Stability and Growth Pact is only now becoming apparent, as national interests across the member states begin to face the consequences of the cutbacks and limitations upon public spending. What was limited opposition is now building up into a debate among economic analysts, politicians, and representatives of business and social groups.

Discussions over the reform of the pact had already begun before the end of 2002.[ix] Much of the reform proposals centre round the technical nature of the pact, and in particular the 3% rule. The argument is that the rule is arbitrary without any sound economic rationale, and is inflexible with regard to the conditions prevailing in the particular national economies.

One reform option to consider would be to replace the 3% deficit rule with an institutional reform index, to reflect the functioning of national fiscal institutions and how well a country is faring against the others – particularly with regard to the reform (i.e., privatisation) of public enterprises, pension systems, unemployment and disability reform, and the revenue sharing arrangements between the different levels of government. Currently, the Stability and Growth Pact focuses on short-term commitments and disregards structural reforms, treating equally countries with different medium- and long-term budgetary prospects and debt levels. Consideration is now being given to making the pact more flexible, more symmetrical, and to allow for more public investment.

Over the next few months, debate over the Stability and Growth Pact will continue, and the Commission has promised an early report on possible reform options. In the meantime, the European Court of Justice will decide on the decision by the Ecofin Council not to adopt sanctions against Germany and France.

It is likely that the precise reforms eventually put forward for adoption by all the countries will be technical and relate to quantitative measurements and surveillance mechanisms. Generally, the EU has a preference for tinkering at the edges rather than opting for a radical and fundamental overhaul of the system. It will not be enough.

Enlargement will constitute an ongoing challenge to the Stability and Growth Pact. All the new countries will join the euro at some point and become subject to the strictures on fiscal management. Public investment and spending levels vary considerably across the acceding states, and these countries will continue to require sustained public investment over the medium- to long-term in order to support growth as well as the convergence with EU-15 levels of development. Consequently, existing tensions in the operation of the pact are likely to continue within the enlarged community, making the issue of reform more than simply a question of tweaking the technical features of the arrangement.

We are witnessing the re-emergence of domestic interests in the contemporary phase of European integration. The trouble over the Stability and Growth Pact is the outcome of a hardening of national interests, and part of the wider pattern that includes the failure to agree the draft constitutional treaty, and the criticism by many EU member states of the mini-summit meeting in Berlin between Germany, France, and Britain in February 2004.

The discord over the Stability and Growth Pact, like the draft constitutional treaty, has brought to the surface differences in the interests of the large and small states. These interests diverged during 2003 as many small states demand the equal application of the rules on fiscal management.

In addition, there are differences over key issues of economic ideology. This is an extra complication in trying to understand the path towards cooperation and integration, since the small-big country divide does not allow for a simple compartmentalisation of national perspectives and preferences with regard to the emerging European Union economic model. For instance, the Dutch, Estonian, Italian, Polish, Portuguese and Spanish governments, which signed a letter to the Irish presidency calling for the Stability and Growth pact to be administered equally, all support more flexible labour markets, yet the grouping comprises both small and large states. Their priorities relate to more and better employment, innovation and technological development, macro-economic stability, enhanced regulation and competitiveness. These priorities are shared by the majority of the EU-15 member states.

What is still in doubt is the capacity of the EU to reconcile the different and sometimes conflicting perspectives over the key issues of economic ideology, and to arrive at some consensus over the nature of the European model of capitalism. This is a political question, and the answer to it will determine future policy choices and long-term priorities with regard to macro-economic stability, economic growth, and the state-market mix in the European economic space. More immediately, the failure to address this political question will limit the capacity of European leaders to agree on more technical/economic questions such as the rules for a Stability and Growth Pact that could serve both the objective of macro-economic stability and the credibility of the political, economic, and institutional communities that must ultimately implement the agreement.

Notes:

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[i] The *Economist* (29 November 2003) reported the decision of the EU finance ministers rather dramatically as the 'death' of the Stability and Growth Pact.

[ii] For an excellent account of the wider political economy considerations see R. Youngs, 'The Politics of the Single Currency: Learning the lessons of Maastricht', *Journal of Common Market Studies*, 37/2, 1999, 295-316.

[iii] Implementation of the pact was based upon annual multilateral surveillance of member state budgetary policies, with the requirement that each country frame its economic policies in accordance with broad economic policy guidelines prepared annually by the Council on a proposal from the Commission. The procedures for dealing with a country experiencing an excessive deficit, include issuing a warning and, subsequently, requiring a deposit that could be retained as a fine should the country not cut its deficit.

[iv] For an up-to-date position see K. Barysch, 'A Pact for Stability and Growth,' London, Centre for European Reform, 2003.

[v] European Commission President Romano Prodi's widely reported criticism that the pact is a static instrument that does not help growth, did nothing for the credibility of the arrangement. Commissioner for Economic and Monetary Affairs Pedro Solbes has promised a reform document in the coming months.

[vi] In the early 1990s different policies and economic conditions among the European countries produced monetary instability. At that time Germany raised interest rates to counter the inflationary pressures associated with the post-unification boom. The D-mark was effectively the anchor currency within the Exchange Rate Mechanism (ERM), and the German interest rate increase precipitated a rise in interest rates in the other member states in order to prevent capital outflows, which would have caused their currencies to lose value relative to the D-mark. Unlike Germany, however, the other countries were experiencing recession, and higher interest rates only exacerbated the situation.

[vii] W. Buiter, G. Corsetti, P. Pesenti, 'Excessive Deficits: Sense and Nonsense in the Treaty of Maastricht,' *Economic Policy*, 8/16, 1993, 57-100.

[viii] O. Issing, 'On Macro-economic Policy Co-ordination in EMU,' *Journal of Common Market Studies*, 40/2, 2002, 345-358.

[ix] See the contributions in *Intereconomics*, January/February, 2003.

Data Resources Review

EUpolitix

Tal Sadeh

EUpolitix.com is a new internet service of EU-related news, with a guide to all EU legislation in the pipeline, interviews and a bank of regularly updated public affairs positions from non-governmental organisations, trade associations and corporations. EUpolitix.com also provides coverage of EU events, from major political struggles, to minute changes in obscure draft regulations. All this information is provided in four ways: a general news section (News), a technical legislation section (Legislation Watch), information by third parties (the Forum) and e-mail attachments (the Bulletins).

The News section provides some 15 new stories a day, 200-500 word each. Stories include interviews with policy makers (such as commissioners and ministers), currency market updates, and reports on developments in the EU's foreign relations, deliberations in the European Parliament, decisions of EU regulators and policy reviews. Each story provides the user with references to other stories on the same topic, as well as links to relevant Forum mini-sites (see below).

Legislation Watch contains updates on pieces of legislation going through the EU decision-making process, sorted into 30 issue areas and containing more than 400 stories at any one time, according to EUpolitix.com. For each piece of legislation there is a simple summary of the proposal, and a constantly-updated timeline of its progress through the institutions, with links to the relevant official documents.

The Forum contains mini-sites for anyone wishing to make their views on EU policy known. Forty-three organizations (Forum members) use the Forum list public affairs information. The members include commercial companies in a variety of industries and markets (such as Barclays, Levi Strauss, Microsoft, and Volvo), NGOs and charities, diplomatic missions (such as the United States Mission to the European Union), various trade and industry associations.

The information provided can involve a description of what the organization does, its views on relevant policies and legislation, pertinent press releases and policy briefings. In addition, a tab on the EUpolitix.com website's menu allows the user to access interviews with officials of such organizations. For example, Volvo details its position on the Kyoto Protocol and how it would be affected by it. Barclays provides evidence it submitted to the House of Lords committee inquiring into the EC's Financial Services Action Plan. ITV1, a commercial television channel in Britain, posts a series of documents reflecting its position on a communication bill the British government is considering. The Amsterdam Group -- an alliance of European producers of beers, wines and spirits -- provides a thorough overview of the regulatory environment for advertising alcoholic beverages in Europe, including in the acceding countries. The International Fund for Animal Welfare (IFAW) details its actions to promote EU-wide fisheries measures to protect harbour porpoises.

EUpolitix.com also provides three free daily e-mail bulletins to interested users. The Morning Bulleting is a summary of major news stories and a list of meetings and sessions in the EU's institutions (these can be accessed also trough EUpolitix.com's homepage). The Press Review is a review of Europe's most influential newspapers, such as the *Financial Times*, *Le monde*, *Le Figaro*, and *Corriere della sera*, as well as smaller newspapers, such as Romania's

Hospodarske noviny, carrying important local stories. It is basically a menu referring the user to a page on EUpolitix.com's website, which includes headlines and links to websites of relevant newspapers. This page cannot be accessed any other way. An evening bulletin – Tomorrow's Agenda – summarizes the day's news and the next day's institutional agenda (also accessible through EUpolitix.com's website).

In addition to these services EUpolitix.com also provides a series of one-day seminars on the decision-making process within European government (accessed by the 'training' tab).

EUpolitix.com's home page presents the recent news stories and interviews, special reports (such as on the new Commission of 30), press reviews, and the current week's agenda of the different EU institutions. The home page also refers the user to reports on recent action taken by Forum members with respect to EU activity and legislation. Recently, for example, there was information on responses by MEPs and human rights organizations to the French National Assembly's decision to ban headscarves and all religious symbols from state schools.

A search engine binds the news, legislation, interviews and forum members together with contextual links to relevant parts of the site. Thus, a news item on the EU savings tax plans is accompanied by links to the relevant legislation summary, previous news articles on the subject, any interviews that might have discussed it, and the relevant policy positions of forum members. Users can search by organization, policy sector or subject area to find out the views of the Forum, as well as related news and legislation.

The services provided by EUpolitix.com are disappointing at times. For example, quite a few of the Forum members provide mundane advertisements and public relations material, with very little information about how they engage with the EU, its institutions and other relevant actors, or what their opinions and actions are with regard to specific policies and legislation. The interviews are mostly of a public-relations character rather than the investigative journalism type. Also the links to Forum members' mini-sites from the news and the legislation sections could do better to direct the user to specific actions by members rather than their homepages.

Legislation Watch is very useful for anyone researching a specific issue area, but its list of recent stories is out of date, the latest having been filed in December 2003. Also, the institutional agenda could provide greater detail.

On the whole, however, EUpolitix.com is a gold mine and potentially a very powerful source of information for students of policy, decision-making and legislation processes in the EU. Given that this is a relatively new service (no data dating before May 2003 was found on the website) its weaknesses can be excused.

The services are provided in English and in French, and are free to access. According to EUpolitix.com the source of income which enables the service to be free is Forum members' annual membership fees. EUpolitix.com is part of the Parliamentary Communications Limited (PCL) group, which also comprises *The House Magazine* and *The Parliament Magazine* (British parliamentary journals) and ePolitix.com (a British parliamentary-news internet site). For more information contact info@eupolitix.com or +32 2 285 0819.

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Members' News

Tal Sadeh was elected to Tel Aviv University's senate.

Alfred Tovias received a grant from the FEMISE Network, financed by the European Commission, to lead a joint project involving 5 researchers from the Hebrew University (Israel) and Yildiz Technical University (Turkey) on 'The Potential of Economic Cooperation among MENA countries.'

Members' Recent and Forthcoming Publications

Michele Chang, *Realigning Interests: Crisis and Credibility in European Monetary Integration*, Palgrave Macmillan, June 2004.

Rainer Eising, 'Interest Groups: Opportunity Structures and Governance Capacity,' in Kenneth Dyson and Klaus H. Goetz (eds), *Germany, Europe and the Politics of Constraint*, Oxford University Press 2003 (Proceedings of the British Academy 119), 147-72.

Rainer Eising, 'Multi-level Governance and Business Interests in the European Union,' *Governance*, 17/2, 2004, 211-45.

Michael P. Gerace, *Military Power, Conflict and Trade*, Frank Cass, 2004.

Johan Lembke, *Competition for Technological Leadership: EU Policy for High Technology*, Edward Elgar, 2002 (USA, 2003).

Johan Lembke, 'Strategies, Politics and High Technology in Europe,' *Comparative European Politics*, 2003, 1, 253-75.

Tal Sadeh, 'Israel and a Euro-Mediterranean Internal Market,' *Mediterranean Politics*, 9/1, 2004, 29-52.

Tal Sadeh, 'Some Trade Effects of the EMU Process on Israel,' in Efraim Karsh (ed.), *Israel: The First Hundred Years - Volume IV Israel in the International Arena*, Frank Cass, 2004, 156-76.

Alfred Tovias, 'The Southern European Economies and European Integration,' in A. Costa Pinto and N. Severiano Teixeira (eds), *Southern Europe and the Making of the European Union*, Social Sciences Monographs-Columbia University Press, 2002, 159-81.

Alfred Tovias, 'Israeli Policy Perspectives on the Euro-Mediterranean Partnership in the Context of EU Enlargement,' *Mediterranean Politics*, 8/2-3, 2003, 214-32.

Alfred Tovias and R. Al Khouri, 'An Empirical Investigation of the Potential Economic Effects of a Bilateral Free Trade Area Agreement Between Israel and Jordan in the context of the Euro-Mediterranean Partnership,' EUI Working Papers, RSC No. 2003/11.

Alasdair Young, 'The Incidental Fortress: The Single European Market and World Trade' *Journal of Common Market Studies*, 42/2, June 2004

Notice of Forthcoming Events

ECPR Standing Group on the European Union
Second Annual Pan-European Conference on EU Politics
24-26 June 2004
Bologna, Italy
Details at:
http://www.jhubc.it/ecpr-bologna

UACES 34th Annual Conference and 9th Research Conference
University of Birmingham
6 - 8 September 2004
Details at:
http://www.uaces.org/D410401.htm

ECPR Standing Group on International Relations
2004 Pan-European Conference
The Hague, The Netherlands
9 - 11 September 2004
Details at:
www.sgir.org/conference2004/T

Deadline

for submissions to the next issue

Monday 6 September 2004

Please direct all correspondence concerning the Forum and the Data Resources Review to the appropriate editor. All other correspondence to the Managing editor.

In particular we are looking for:
◊ Members' Recent publications (since this issue)
◊ Members' news (since this issue)
◊ Calls for papers (due dates prior to 28 February 2005)
◊ Notice of forthcoming events (taking place prior to 31 March 2005)

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