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Economic Crisis Management in the EU: From Past Eurozone Mistakes To Future Promise beyond the Covid-19 Pandemic

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Introduction

The responses to the Covid-19 crisis, in which the rules of the Stability and Growth Pact (SGP) were suspended and the EU took on significant EU level debt for the purposes of redistributive solidarity, constitute a great leap forward for the EU. They also represent a tacit acknowledgement that the policies put in place in response to the Eurozone crisis, focused on 'governing by rules and ruling by numbers,' with punitive conditionality for countries in trouble, were not fit for purpose. The question for today is: Will the EU go back to the *status quo ante* of the Eurozone, focused on rules-based, numbers-targeting governance, with limited common EU instruments for investment in the future? Or will it instead move beyond the Eurozone and Covid-19 crisis effectively and democratically, toward more sustainable and equitable growth and prosperity for all Europeans? These questions gain all the more importance in light of the Ukraine crisis, and the need for more common EU level responses to energy and security challenges.

I argue herein that in order to meet the current challenges, including the green transition, the digital transformation, and addressing socio-economic inequalities, the EU should not go back to Eurozone crisis management rules. Much the contrary, to ensure the greatest possible success in the future, the EU needs more instruments to promote EU-wide sustainable development in a context of more flexible and inclusive economic governance. For the instruments, the EU needs to build on the pandemic Next Generation EU response, making the Resilience and Recovery Facility (or its equivalent) permanent and much bigger. For the governance, the Eurozone needs to become more decentralized, with fiscal guidelines allowing for differentiated member-state goals in a process that is more bottom up, not just from national capitals but from regional and local governance. Importantly, that process also needs to become more democratic, with greater participation by the social partners and citizens along with parliaments at every stage of the process, along with industrial strategy and macroeconomic dialogues to set overall goals.

I proceed by first discussing the EU's management of the Eurozone crisis and then the new initiatives undertaken during the Covid-19 crisis. I next consider in greater detail some innovative ideas for the Commission with regard to industrial policy and the European Semester and then the ECB with regard to macroeconomic governance. I conclude by pointing to potential obstacles and stumbling blocks to any such innovations, and then reiterate the governance requisites for a more sustainable and equitable EU economy.

The Eurozone Crisis

In the Eurozone at the outset of the crisis, instead of immediately providing some form of debt forgiveness and instituting the mutual risk-sharing instruments necessary for any fixed-currency zone to work, the EU reinforced the rules of the Stability and Growth Pact (SGP). By mandating austerity and structural reform policies overseen through the European Semester, the Eurozone came to be characterized by 'governing by rules and ruling by numbers,' with the wrong rules and numbers, which didn't work. This in turn led to what I have called the EU's 'crisis of legitimacy,' in which doubling down on the procedural rules led to poor economic performance and increasingly toxic politics (Schmidt 2020a).

Crisis Management

The EU chose the wrong course in 2010 in its response to the Eurozone crisis. Rather than bold initiatives that would quickly resolve the crisis, EU actors doubled down on the rules, claiming that 'moral hazard' was the main danger, austerity the answer, with harsh austerity and structural reform for countries in trouble. Because the crisis was perceived as asymmetrical and framed as resulting from public profligacy (based on Greece) rather than private excess (the case of all other countries forced to bail out their banks), the causes were diagnosed as behavioral (member states not following the rules) rather than structural (linked to the euro's design). In consequence, EU leaders saw little need initially to fix the euro or to moderate the effects of the crisis. Instead, they chose to reinforce the rules enshrined in the treaties, based on convergence criteria toward low deficits, debt, and inflation rates. And they agreed to provide loan bailouts for countries under market pressure in exchange for rapid fiscal consolidation and 'structural reforms' focused on deregulating labor markets and cutting social welfare costs. These measures did little to solve the underlying problems, and the crisis went on and on.

By late 2012, however, as the crisis slowed following ECB President Draghi's famous pledge to 'do whatever it takes' to save the Euro, which stopped market attacks dead in their tracks, European leaders and officials began to change Eurozone governance slowly and incrementally. They did this by reinterpreting the rules and recalibrating the numbers, albeit mainly 'by stealth,' without admitting it publicly or even, often, to one another (Schmidt 2016, 2020a). The Commission became more and more flexible in its application of the rules in the European Semester (such as derogations for Italy and France based on their having primary surpluses), despite continuing its harsh discourse focused on austerity and structural reform. The ECB in the meantime reinterpreted its mandate more and more expansively, even as it claimed to remain true to its Charter, ending up deploying quantitative easing (QE) by 2015, and thereby came ever closer to becoming a lender of last resort (LOLR). Finally, the Council also began to change its tune. Along with innovative instruments of deeper integration such as Banking Union and the

European Stability Mechanism came acceptance of the need for growth ‘and stability’ by 2012; for flexibility ‘within the stability rules’ by 2014; and for investment in 2015.

Things got better as a result. But because EU actors in the first five crisis years largely reinterpreted the rules by stealth, legitimacy remained in question. Fundamental flaws persisted, with suboptimal rules hampering economic growth and feeding populism, as citizens punished mainstream parties while anti-system parties prospered. Even though, by 2015, most EU actors had begun to acknowledge their reinterpretations, and growth began to return across the EU, the damage had been done.

Economics

With regard to the economics alone, academic scholars and policy analysts alike agree that Eurozone crisis management failed to deal effectively with the problems of the Eurozone in terms of policy effectiveness and performance. The United States, which had faced what were arguably even greater economic problems earlier on as a result of the 2008 financial crisis, nonetheless managed to emerge from its crisis more quickly, and without the double-dip recession experienced by the Eurozone (Mody 2018; Tooze 2018). In the EU, economic growth was generally sluggish while deflation remained a threat in a Eurozone characterized by increasing divergence between the export-rich surplus economies of Northern Europe and the rest (Blyth 2013; Mody 2018; Tooze 2018).

Europe more generally was also facing a ‘humanitarian crisis,’ affected as it was by rising poverty and inequality among the European citizens along with continuing high levels of unemployment, especially in Southern Europe and in particular among young people (Council of Europe 2013; European Parliament 2015). Largely to blame for prolonging the economic crisis in the Eurozone was the imposed austerity in the South together with the lack of investment in the North—as even the IMF (2013, 2014) and the OECD (2016) reported. Adding to this were the ‘one-size-fits-all’ remedies implemented in diverse national political economies with different institutional configurations and potential engines for growth (Scharpf 2012; Mody 2018).

Although between 2015 and 2020 the economic situation across Europe did improve while more was done to ‘socialize’ the European Semester and to make it better adapted to member-states’ different needs ((Zeitlin and Vanhercke 2018), the austerity budgeting baked into the rules nevertheless entailed that those without the fiscal space *could not* invest (read Southern Europe) while those with the fiscal space *did not* invest (Northern Europe). This meant not only that Southern Europe was unable to invest in growth-enhancing areas such as education, health, training, and R&D, let alone infrastructure (physical as much as digital), but that Northern Europe also did not do enough in these areas, or even in greening their economies. Much of this can be attributed to the debt brake constitutionalized throughout the Eurozone (via the Fiscal Compact) and the obsession with balanced budgets, in particular in Germany, with the ‘*schwarze null*’ (black zero). To illustrate the problems for federalized Germany, where the Länder are responsible for university education and local governments for local infrastructure, the rules limited new investment for the poorer (and therefore already more indebted) regions and localities, thereby increasing inequalities among sub-federal units while stunting growth potential (Roth and Wolff 2018).

Politics

The EU's comparatively poor economic performance also added to the EU's declining political legitimacy, as evidenced by citizens' loss of trust in the EU along with their increasing dissatisfaction with and disaffection from EU and national politics. Eurobarometer surveys, for example, chart the decline in the positive image of the EU, which went from 52% in 2007 to 30% in 2012 while the negative image went up from 15% in 2007 to 29% in 2012—neck and neck with the positive responses (Eurobarometer December 2012). Although in 2019 (before the pandemic), the number of those with a positive image had come back up to 45 percent, it was still lower than in 2007 (Eurobarometer Spring 2019). Citizens came to perceive the EU as more and more remote (read technocratic) (Fawcett and Marsh 2014), and national governments as less and less responsive to their concerns—often as a result of EU policies and prescriptions (Hobolt 2015; Berman 2021). The dilemma facing national governments—caught between the need to act responsibly by implementing unpopular EU policies and the need to be responsive to citizens' demands (Mair 2013)—translated into more and more volatile national politics. National elections became increasingly unpredictable, as incumbent governments were regularly turned out of office while new parties with populist anti-euro and anti-EU messages got attention, votes, and more and more seats in parliaments (Hopkin 2020). Much of this has been a function of the growth of Euroscepticism and the mounting strength of the populist extremes, but it also reflects the increasing divisions between winners and losers in the crisis, within member states as well as between them.

Such discontent has its sources in a range of long-standing socioeconomic, sociocultural, and political trends, linked to the effects of globalization and Europeanization, which were only exacerbated by the Eurozone crisis. The socioeconomic discontent is centered on workers' feelings of being 'left behind' in low-paying jobs with few prospects of better pay, working conditions, and living conditions (Hopkin 2020; Rodrik 2017). Such discontent was particularly in evidence in peri-urban or rural settings where good jobs are scarce and public services have been dwindling—representing the "revenge of the places that don't matter" (Rodríguez-Pose 2018, p. 201). But the discontent is also linked to national sociocultural concerns, in particular worries about loss of social status (Gidron and Hall 2017), fears about the 'changing faces of the nation' with larger flows of immigrants (Berezin 2009), or even rejection of more liberal 'post-materialist' values (Norris and Inglehart 2019). This said, a lot of the discontent is purely political, as people feel their voices no longer matter in the political process, and want to 'take back control,' as in the case of Brexit (Berman 2021). These varied sources of discontent have constituted the 'milieu' in which populist anti-system 'messengers'—including leaders, parties, and activist networks—were able to spread their anti-elite 'messages' via the 'medium' of the social and traditional media in ways that got them votes, seats in parliaments and, in some cases, governing power (Schmidt 2021b).

Governance

Governance in the Eurozone was also increasingly in question. For program countries, complaints focused not only on the counterproductive economic effects of rapid fiscal consolidation and the inefficacy of the structural reforms. They also concerned the opaqueness and unaccountability of the Troika (and later the 'Institutions') involved in dictating the terms of the pro-cyclical reforms required in exchange for the loan bailouts—not to mention the secret letters from ECB President Trichet threatening to pull the plug on their economies unless they entered a conditionality program. For the non-program countries, meaning all the rest, as EU institutional actors became more flexible in their interpretations of the rules from 2013 on, perceptions among citizens and political elites alike increasingly polarized between the Northern Europeans and Southern Europeans, as 'the sinners' versus 'the saints' (Matthijs and McNamara 2015).

This split in perceptions in turn only added to the increasing politicization of EU governance writ large. The rising politicization 'at the bottom' due to increasing national level Euroscepticism and from 'the bottom up' due to national pressures on member-state leaders in the Council (Hooghe and Marks 2019) was joined by increasing political contestation 'at the top,' within and between EU actors at the supranational level (Schmidt 2019a, 2020a). Such politicization involved not only increasingly acrimonious disputes among member-state leaders in the Council (in particular in the Council of Ministers of Finance) but also between members of the Council and other institutions. In the Council, for example, while some member state leaders (mainly German, Dutch, and Finnish Finance Ministers) contested the Commission's increasing flexibility with regard to the application of the rules in the European Semester, claiming that it was 'politicized,' others defended such action as appropriate administrative discretion. The Commission itself also pushed back against member states' rebukes about politicization at the same time that after 2015 it declared itself a 'political' body responsive to European citizens. Meanwhile, the ECB also became increasingly politically sensitive, engaging in more informal dialogue with Council members to gain tacit agreement for its increasingly bold monetary policy initiatives and in more communication with the 'people' (as well as the markets) regarding its increasingly expansive monetary policy. And finally, the EP also became increasingly contestational politically as it criticized Council and Commission actions in its hearings and reports.

The result is a new politicized dynamics of interaction among EU actors. We could ask whether such politicization is a bad thing, because the substance of what is said by different EU actors was generally negative, or a good thing, because the process of discursive interaction is what normally happens in democracies, and therefore can be seen to make the EU appear less technocratic and arguably therefore itself more democratic. But whether a good thing or a bad thing, it is a 'thing,' and here to stay (Schmidt 2019a, 2020a). Notably, however, the kind of negative politicization that took hold during the Eurozone crisis seemed to have receded during the Covid 19 crisis, in which a more 'positive' politicization ensued.

It is equally important to recognize that as time went on during the decade of the Eurozone crisis, certain governance practices during this period of 'emergency politics' (White, this book) seemed to be legitimized by being normalized whereas others appeared delegitimized by being rolled back. The monetary policymaking of the ECB is the prime case of legitimation, with its monetary easing not just normalized but progressively ratcheted up during the Eurozone crisis, and even more so during Covid 19. In contrast, the reinforced 'governing by rules and ruling by numbers' of the Council and Commission are examples of delegitimization, as evidenced by the roll back of the stability rules via reinterpretations in favor of growth and flexibility during the Eurozone crisis, and then their suspension during the Covid 19 pandemic (Schmidt 2021b).

The Pandemic Response—A New Beginning

Only in 2020 was there a major reversal in policy, as the EU responded to the Covid-19 health pandemic, which was to create an economic shock even greater than that of the sovereign debt crisis. The pandemic crisis response appeared in great contrast to the muddling through of the previous Eurozone crisis, with its hit or miss policies that were mostly incremental and largely unsatisfactory. Rather than the piecemeal (non) solutions of the past, in particular the doubling down on the SGP rules, EU pandemic crisis management, after a short period that seemed to foretell a replay of previous crises, appeared to have engineered a major shift in economics, politics, and governance. The Next Generation EU plan, with the Resilience and Recovery Facility that broke the taboo on EU level debt—promising to kick-start sustainable growth throughout the EU by way of the green transition, the digital transformation, and addressing social inequalities—represents a great leap forward in all these domains. But although a game-changer in many ways, whether this constitutes a paradigm shift in the EU's economic governance depends upon what happens next.

Crisis Management

In the first months of the crisis, the response seemed like a *déjà vu* with regard to the Eurozone crisis, as EU actors' hesitations and discordant views had only made matters worse. In the first weeks of the pandemic, EU institutional actors were very slow to respond. The Commission was nowhere; the EP played no role; the President of the ECB claimed it was not within the ECB's mandate to deal with spreads between German and Italian bonds (which triggered an increase in the spreads for Italian bonds); and member state leaders in the Council failed to act in concert, even as they quickly introduced national policies without EU-level consultation or coordination.

At the national level, member states' economic policies represented a major reversal of Eurozone budgetary orthodoxy. The member-states violated the SGP deficit and debt rules as they provided massive infusions of money to sustain businesses, protect jobs, and support individuals and families. At the same time, their simultaneous closing of national borders without informing neighboring countries or the EU looked like the refugee crisis *redux*. Moreover, the export bans on medical protective equipment, ventilators, and pharmaceutical supplies appeared to violate the spirit of the single market as well as European solidarity. It seemed like the member-states had forgotten that the virus does not respect borders, and that the very interdependence of the Eurozone economy required some form of joint action.

Very quickly, however, EU institutional actors stepped up to the plate, as did the member-states. There were symbolic acts, such as patients from Italy and France transferred to German hospitals. But there were also very important initiatives taken by all institutional actors. To begin with, the Commission immediately suspended the budgetary criteria of the European Semester to allow for unlimited government spending; cleared the way for member states to rescue failing companies by suspending the state aid rules; put into place the European instrument for temporary Support to mitigate Unemployment Risks in an Emergency (SURE), a €100bn to help maintain employment; proposed the creation of an EU-level health authority (EU4Health); and closed the EU's external borders to travelers from outside the EU.

In the meantime, the ECB quickly made up for its initial misstep on the spread between German and Italian bonds by launching the Pandemic Emergency Purchasing Program (PEPP), at an initial €750 billion in March 2020, later increased to €1.85 trillion, to save the euro. This went way beyond its previous 2015 quantitative easing, and came without the *quid-pro-quo* demands for austerity and structural reforms of the Eurozone crisis. Additionally the ECB abandoned the Eurocrisis ratio of bond-buying that had limited its ability to help countries in greatest need, thereby enabling it to better target its bond purchases to those countries potentially under market attack.

Moreover, in the Council, the Franco-German duo made an initial taboo-breaking proposal for a Recovery Fund of €500 billion in grants on May 18, 2020, and then sent that proposal to the Commission for review and further recommendations. The Commission followed quickly on May 27 by upping the ante with the Next Generation EU proposal containing a Resilience and Recovery Facility (RRF) for €750 billion with two thirds grants and one third loans to be financed by market-based EU bonds as part of a much larger multi-year EU budget (the Multi-Annual Financial Framework, or MFF) in which the EU would gain its own tax-generated resources. The European Council agreement in July consecrated the RRF with €390 billion in grants, €360 billion in loans, compromising on the generosity of the fund as well as rule of law conditionality to get the package through. Finally, the EP, which had had little influence over the initial pandemic response, had an important role to play in the budget negotiations beginning in October 2020 not only by strengthening the rule of law clause in the compromise but also ensuring more resources, in particular for EU4Health.

Economics

In the economics of the COVID-19 pandemic, the EU's responses with regard to Economic and Monetary Union (EMU) represent a major break from the past, in particular in contrast to the path dependent trajectory taken during Eurozone crisis (Ladi and Tsarouhas 2020). The EU took a great leap forward in economic integration by allowing for EU level debt covered by the EU's own resources to pay for EU initiatives for the first time. Notably, these new initiatives were largely focused on fixing the damages incurred by the failures of Eurozone crisis management, as opposed to addressing those resulting from the pandemic. This is evident from the fact that NGEU resources were allocated to countries on the basis of pre-existing economic and political conditions likely to make them more vulnerable to a post-Covid austerity adjustment as well as to Euroskeptic forces, rather than on the severity of the pandemic (Armingeon et al. 2021).

It is perhaps still too early to say anything much about the economic effects of the pandemic response. But one thing can be certain. Without that response, the EU would have been in dire straits, with the Single Currency under attack, the Single Market in free fall. Moreover, the Eurozone divergences that had been exacerbated by Eurozone crisis management would have only increased, due to countries' differing levels of economic capacity as well as fiscal space. At the inception of the crisis, as member-states locked-down in order to stop the spread of the virus, Germany launched a major fiscal stimulus in which it promised state aid that constituted over half of that pledged by all other member-states combined (51%, at close to €994.5bn). Contrast this with France's 17% of all aid (€331.5bn), Italy's 15.5% (€302.2bn), the UK's 4% (€78bn), and Belgium's 3% (€58.5bn (*FT* May 18 2020). Had the EU not intervened with the RRF, it would have faced real problems with regard to ensuring a level playing field for the Single

Market when Northern Europe could spend massively to prop up jobs and businesses in contrast to Southern Europe, which could provide much lower levels of support, and Central and Eastern European countries even less.

As it is, the Eurozone economy appears to have been recovering well. Growth rates have picked up across member-states, with better than expected predictions in cases like Italy, slated for a 6 percent growth rate for 2021—due in large measure to the increased business and market confidence related not just to the boost coming from the RRF but also the Draghi-led coalition government. But much is still to be done. The pandemic itself not only revealed pre-existing major economic disparities in the EU, within as well as between member-states, it exacerbated them. Among such disparities have been rising poverty, gender-related inequalities (as women were more likely to have to leave their jobs to care for their children), and youth unemployment (in particular the increase in NEETs) along with a growing digital divide. This has been both geographic—differentiating between urban and rural settings—and class-related—as poorer students lacked the digital tools as well as the services to enable them to connect to the internet for online learning.

The main question for the EU's economic response to the pandemic going forward is: Is it enough? Although all of this EU level funding constitutes a tremendous boost to the EU's economic capacity to confront the crisis, it appears very small indeed when compared to the United States' initial $1.9 trillion of March 2020 (equivalent of 9% of US GDP, and thus five times the size of NGEU—Stiglitz 2020; see also Armingeon et al. 2021), leaving aside potential differences from the massive legislative initiatives by the Biden administration to fund infrastructure as well as to increase social spending. Even if national automatic stabilizers in the EU are more robust than in the US, it is clear that economic divergences among member-states will persist if not increase. More EU funding on a permanent basis will surely be necessary to ensure a robust economic recovery for all. And for this, rather than seeing such funding as increasing EU debt, consider it for what it really is: investment which can ensure that the EU will grow its way out of debt. The lesson from the Eurozone crisis is that you cannot cut your way out of debt. Investment for sustainable growth is the only way out.

Politics

Perceptions at the very initial stage of the pandemic were divided. There were those who saw this crisis, much as in the Eurozone crisis, as an asymmetric shock to be dealt with by the member-states in trouble, whereas others felt from the beginning that it was a symmetric shock, and that solidarity was required. Most infamous was the Dutch Finance Minister Wopke Hoekstra who blamed the victims, notably Italy, for not having the room to maneuver to weather the economic impact of the crisis (*Politico*, March 27, 2020)—an accusation even more egregious once we remember the informal conditionality and SGP rules that had made it impossible for Italy to invest in its health system. Although the Dutch minister was roundly condemned, his comments only fueled the sense in those initially most hard hit by the pandemic that the EU lacked solidarity or even empathy—leading them to ask why were they part of the EU at all (*Financial Times* April 6, 2020). Southern Europeans, and Italy followed by Spain in particular, felt abandoned if not betrayed by the EU and fellow members-states in March, April, and May 2020.

The mood seemed to shift only once the Franco-German duo came out publicly recommending a major grant-based recovery fund in mid May, and the Commission came back quickly with an even larger amount. The change in mood was evidenced not only by member-state leaders but also EU citizens, as trust in national governments and the EU overall increased. At the national level, the Edelman Trust Barometer (Spring Update, May 2020)[1] found an upsurge in trust in government generally, with a 10 percent increase in Germany from January to May 2020 (46% to 56%), with smaller increases in France (45% to 49%). A Pew survey (Aug. 27, 2020) similarly found increased trust in national governments, as judged by citizens' approval of their country's response, with a large majority seeing it as good in Spain (54%), France (59%), Belgium (61%), Sweden (71%), Italy (74%) Netherlands (87%), Germany (88%), and Denmark (95%), in contrast to the UK (46%). As for the EU, which at the outset of the crisis had little governing authority in the health domain, highly constraining economic rules, and limited fiscal capacities, trust comes out in general citizen support for enhancing its powers. A Eurobarometer poll (June 2020)[2] carried out between 23 April and 1 May 2020, found that a majority of respondents (57%) were dissatisfied with the solidarity shown between EU member-states, while close to two-thirds (69%) wanted the EU to "have more competences to deal with crises such as the Coronavirus pandemic."

This general increase in public trust in national governments and the EU largely continued, despite subsequent ups and downs in public approval, in particular in response to the slow vaccine roll-out and then lock-down measures. Moreover, and perhaps surprisingly, across Europe populism was for the most part held at bay. There is no doubt that anti-system populist parties in many member-states decried government elites, mainly blaming them for being too harsh on mask-wearing rules and lockdowns, even as mainstream opposition parties complained that populist governments were too late and lax on lock-down measures. There were also sporadic protest marches against mandates to wear masks, to get vaccinations, and later to use health passes to get into restaurants and theaters or even to places of employment. But the vast majority of Europeans seemed to have accepted the emergency measures to keep people safe. That said, in some European countries with populist governments, their leaders exploited the crisis for their own political purposes, for example, to restrict access to abortions or to limit freedom of the press, as in Hungary and Poland.

Governance

While the negative politicization of Eurozone crisis management largely characterized the initial period of pandemic crisis management, a more positive politicization 'at the top' began once France and Germany together proposed the grants-based recovery fund via EU-level bonds. Before this breakthrough, however, the splits in the Council reflected those of the Eurozone crisis, with the 'frugal coalition' (made up of Germany, the Netherlands, Austria, Denmark, and Sweden among others) against the 'solidarity coalition' (made up of mainly of France and other Southern European, joined by some Central and Eastern European countries) (Fabbrini 2021). Once Germany shifted sides, however, by joining the solidarity coalition, the stage was set for more positive politicization not only within the Council but also with the Commission, which it

[1] https://www.edelman.com/sites/g/files/aatuss191/files/2020-05/2020%20Edelman%20Trust%20Barometer%20Spring%20Update.pdf

[2] https://www.europarl.europa.eu/at-your-service/en/be-heard/eurobarometer/public-opinion-in-the-eu-in-time-of-coronavirus-crisis

empowered to carry out the agreed programs. This more cooperative relationship constituted another reversal of Council patterns typical of the Eurozone and earlier, in which the 'new intergovernmentalism' of member-state leaders meant that they seemed intent on avoiding empowering the Commission at all costs by establishing administrative bodies outside the control of the Commission, as in the case of the ESM (Bickerton et al. 2015).

The story of how Germany moved from the frugal coalition, of which it was a leader during the Eurozone crisis, to the solidarity coalition championed by France, has yet to be told in full. There are those who attribute the switch to German leaders' reconceptualization of their interests, both economic, to ensure the continued functioning of the Eurozone's interdependent economy (in particular as German automotive manufacturers clamored for an Italian rescue to shore up their supply chains in Northern Italy as much as their sales across Europe), and political, especially once polling showed that a majority of their citizens actually were in favor of the creation of EU funds to support countries in need (Schramm 2021). However, beyond the cognitive shift in interests were norms and values, or even emotions. Merkel's change of heart is arguably similar to her previous switch on migration policy in 2015 and on national nuclear policy. But French policymakers also need to be given a lot of credit for the breakthrough, as they argued persuasively in the name of Europe for solidarity in a health crisis in which all countries were equally at risk of contagion, but some had been hit harder than others and did not have the wherewithal to recover economically without support (Crespy and Schramm, 2021). The shift itself followed from discursive interactions over a period of months, from late March on, between French President Emmanuel Macron and Chancellor Merkel, backed up by discursive coordination deep into the executive bureaucracies of both countries, as well as with the Commission (Crespy and Schramm, 2021; Schramm 2021).

Negative politicization did not entirely disappear, of course. A case in point was the German Constitutional Court's judgment questioning the ECB's actions in terms of quantitative easing (PSPP), which cast a shadow over its pandemic-related monetary policy (PEPP). Needless to say, politicization also continued with the efforts by the frugal coalition to block EU-level grants in favor of providing only loans with conditionality to Southern European countries in need. But there was also the resistance by the 'Sovereignty Coalition' consisting of Poland and Hungary and other Central and Eastern European countries to any rule of law conditionality linked to the disbursement of RRF funds (Fabbrini 2021). The Council agreement in July 2020 was a compromise in which the frugal coalition failed to scuttle the recovery fund but nonetheless succeeded in altering the ratio of grants to loans at the same time that Poland and Hungary managed to water down the 'rule of law' conditionality clause. Notably, however, here the EP, which had had little impact initially, managed during the budget negotiations to reinsert more robust rule of law conditionality into the final agreement, along with more money for EU4Health.

Finally, the Commission not only came through with innovative ideas adopted by the Council. It also overhauled the European Semester in ways that eliminated many of its remaining drawbacks. It is useful to remember that at the inception of the Eurozone crisis in 2010, the Semester was converted from a soft law coordinating mechanism (akin to the 'open method of coordination') into a top-down punitive mechanism of control which was then eased (beginning in 2013) by being applied with greater and greater flexibility in order to ensure better performance, accompanied by an increasing focus on addressing social concerns. Today, in light of the pandemic response, the Commission's mission has been transformed. It has largely left behind its roles of enforcer and then moderator in the Eurozone crisis to promoter of the new industrial strategy initiatives through the National Resilience and Recovery Plans (NRRPs). These are more bottom-up exercises by member-state governments, at the same time that the Commission still exercises oversight via conditionality and makes recommendations for reform—such as determining whether certain pre-agreed 'milestones' in terms of economic reform are met before disbursing the next tranche of funding.[3] But this 'conditionality' is a far cry from what it was during the early phase of the Eurozone crisis, when structural reform meant largely cutting welfare states and deregulating labor markets. It is focused on attacking national economic vulnerabilities and administrative hindrances as well as social 'fairness' by addressing inequalities of opportunities as well as of outcomes.

What Next? How to Improve EU Economic Governance

As we have seen, after a brief moment of *déjà vu* with the Eurozone crisis, it seemed that the EU had learned the lessons of that crisis by responding much more proactively to the Covid 19 crisis. Suspension of the rules and numbers was accompanied by massive national bailouts and EU creation of an unprecedented European recovery fund focused on greening economies, digitalizing societies, and addressing inequalities. Legitimacy, so much at risk during the Eurozone crisis seems to have improved as a result of this new EU-level solidarity. But will it last?

To ensure a brighter future for the European economy, much more needs to be done. The EU needs to rethink European economic governance beyond the old ideas, to repair the damage wrought by euro crisis management, with an enhanced role for 'state' actors—EU and national—as public entrepreneurs to promote growth and provide investment to meet the challenges of the green transition and the digital transformation while ensuring greater social equity. But this cannot be done solely as a technocratic fix, nor as a top-down process. Rather, economic governance needs to be both decentralized and democratized—with more bottom-up involvement of social partners and citizens at local, national, as well as EU levels, and greater roles for both national parliaments and the European Parliament.

So how do we get there from here, that is, to effective economic policies and efficient governance procedures that at the same time enhance democracy? For this, we take a closer look at some innovative ideas for Commission industrial strategy and the European Semester as well as for ECB macroeconomic coordination.

Industrial Strategy and the European Semester

The EU has made a great leap forward through the Next Generation EU, focused on investing in the green transition, the digital transformation, and social equity, together with the temporary Resilience and Recovery Facility (RRF) targeted to member-states most in need. But this kind of industrial strategy needs to be reinforced through the development of permanent EU level debt

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[3] Marco Buti, Head of Cabinet of Commissioner Paolo Gentiloni, sees it as the move from 'referee' to 'investment enabler.' Talk at the Center for European Studies, Harvard University (April 14, 2021)

that could provide investment funds for all member-states on a regular basis. Think of a permanent RRF as an EU wealth fund, akin to national sovereign wealth funds, which issues debt on the global markets to use to invest through grants to the member-states in education, training, and income support; in greening the economy and digitally connecting society; as well as in big physical infrastructure projects (Lonergan and Blyth 2018, pp. 132-141). It could also be used for redistributive purposes through a range of innovative targeted EU funds, including a common European unemployment reinsurance scheme; a refugee integration fund for municipalities (Schwan 2020) and a migration adjustment fund to support the extra costs for social services and retraining needs; an EU fund for 'just mobility' focused on brain drain; or even a guaranteed (basic) minimum annual income?[4] Such funds would provide carrots and not just sticks to encourage greater buy-in from member-states in particular in a range of areas. Different countries would benefit at different times from the funds, which could be triggered when any one country finds itself overburdened by the extra costs it incurs because of the asymmetric functioning of the Single Market and the Single Currency, or because of its openness to refugees and migrants.

With all such funding initiatives, the next question to arise is how to ensure that they succeed. For this the European Semester is the ideal vehicle for oversight and assistance, but only if we rethink the rules and numbers. Clearly, the Eurozone's restrictive numbers-targeting deficit and debt rules, reinforced during the Eurozone crisis, did not work, and in any event need to be changed to meet the new circumstances and goals. The numbers alone are now completely out of whack, given member-state debt on average at over 100% of GDP and government deficits way above the previous levels. But rather than simply readjusting the rules and numbers, they should be permanently suspended, to be replaced, say, by a set of 'fiscal standards' to assess sustainability in context (Blanchard et al. 2021). But if this is not feasible, then a much more flexible set of rules needs to be developed, focused on counter-cyclical economic policy, with more fine-tuned assessments of where individual member-states sit in the business cycle in relation to deficits and debt as well as growth outlook and prospects of meeting investment targets. Flexibility needs to be the watchword, sustainable and equitable growth the objective.

Moreover, national level public investments beyond those that are part of NGEU should not be counted toward deficits or debt when deemed to benefit the next generation because enhancing sustainable growth (e.g., investments in education and training, greening the economy and digitalizing society, as well as improving the physical infrastructure). This is known as the Golden Rule for public investment. An IMK report found that had the 'golden rule' been applied for public investment rather than deficit/debt rules from 2010-2017, economies of the four largest economies would have gained in GDP—1.8% higher for all 4, but Spain 3.5% higher GDP, Italy 2% higher, France 1.8% higher, and Germany 1.5% higher (Dullien et al., 2020).

In fact, public debt itself could be ignored if it is sustainable, meaning that the government can borrow at a rate lower that the average rate of growth of GDP—otherwise, raise taxes (Lonergan and Blyth 2018). So long as all debt to GDP ratios will be much higher than 60% or even 90% for a while, why not allow any amount of debt so long as sustainable (i.e., the country can

[4] This could be paid for, say, by the 'digital dividend,' by having digital platforms pay for our data (which means establishing our property rights on our data, licensing private corporations to use it), and then using this as tax pro minimum income (Lonergan and Blyth 2018)

service its debt—think of Japan, at 200%), with growth helping to pay down debt in the long term. Why continue to punish countries with higher debt to GDP ratios in terms of expenditure rules? One of the lessons of Eurozone crisis management is that you cannot cut your way out of public debt through austerity; the only way out is through growth. In this vein, another initiative should be to eliminate the debt brake from national constitutional legislation. As noted earlier, this was a hindrance not only for those without the 'fiscal space,' who could not invest, but also for those who had it, and did not invest. And in both cases, it constrained those countries, regions, and municipalities that needed such investment the most.

Decentralizing and Democratizing EU Economic Governance
European Semester procedures also need to be reimagined. The Semester provides an amazing architecture for coordination. But it remains a highly technocratic exercise that is largely concentrated in the executive branches of national governments in coordination with the Commission. Our question here is what is the best way to exercise coordinating oversight while decentralizing and democratizing the process? And for this, we need to consider EU as well as national levels.

In its Communication on the 2021 Annual Sustainable Growth Strategy published on September 17, 2020, the Commission calls for member-states to "engage as soon as possible in a broad policy dialogue including social partners and all other relevant stakeholders to prepare their national resilience and recovery plans" in order to ensure national ownership (COM (2020) 575 final, p. 13). Given the short timing, however, it was understood that such dialogue would be difficult for member-states to manage in the first year of National Resilience and Recovery Plans (NRRPs), given the need to ensure speedy action. But it doesn't appear that much has been put into place for the next round, in particular because the 2021 cycle of the Semester did not issue new country-specific reports. As a result, whereas powerful industrial lobbies were likely to have been able to exert influence in the design and adoption of NPPRs, the same is not true of social stakeholders. Nor did the Commission itself seem to have done much to ensure this kind of broad dialogue at the EU level. Although social stakeholders were heard (via online communication), how much they were 'listened to,' meaning had an impact on practices, remains open to question (Vanhercke and Verdun 2021).

In view of all this, most important would be for the Commission to ensure that the national planning processes for the National Resilience and Recovery Plans (NRRPs) are not only democratized by bringing in the social partners, civil society actors, as well as elected officials but also decentralized to regional and local levels. In this context, the existing fiscal boards should be transformed into industrial strategy advisers and the competitiveness councils into industrial policy councils. This kind of vast decentralized consultation could be likened to the French 'Plan' of the postwar period, which succeeded remarkably well not only because it had clear objectives for targeted funding but also because it brought in the *forces vives* of society, with widespread consultation ensuring common cause along with the circulation of ideas and information (Schmidt 1996). Bringing in social stakeholders and regional and local levels could also help guard against corruption and clientelism.

But beyond encouraging the decentralization and democratization of national level dialogues in the context of the NPPRs, the Commission would do well to open up on-going dialogue with all stakeholders on its goals for economic governance, so as to democratize the planning process at the EU level. We could call this the 'Grand Industrial Strategy Dialogue,' and task it with recommending overall targets and goals, say, for greener investing, more society-driven digitalization, and addressing social inequalities in addition to promoting the 'strategic autonomy' of the EU economy. This could arguably build on the existing Economic Dialogues and Monetary Dialogues regularly organized by the EP with EU executive actors, but be more inclusive with regard to bringing in civil society actors and more ambitious in terms of setting objectives for sustainable and equitable growth.

This kind of dialogue could also serve a larger purpose, by providing a venue for more democratic debate and deliberation on EU macroeconomic governance. Alternatively, there could be a separate macroeconomic dialogue. Let's call it the 'Great Macroeconomic Dialogue,' as a yearly or biannual conference to outline the grand economic strategies, making for a space for all EU institutional actors—including the EP, the Commission, the Council, and the ECB—along with representatives of industry, labor, and civil society from across Europe. It could be the venue for considering the general targets for the Eurozone on an on-going basis—as a substitute for the currently suspended SGP rules and numbers. Additionally, it could provide the ECB with more public input and legitimation on moving forward in terms of its secondary objectives. Such objectives include targeting full employment on a par with fighting inflation; ending 'neutral' bond-buying (meaning stopping buying the bonds of polluting industries); creating green bonds for the environment; or even providing so-called 'helicopter money' to offer direct support to households in need.. The 'political guidance' offered through the Great Macroeconomic Dialogue would not impinge on the ECB's independence at the same time that it could provide legitimacy of the kind afforded to national central banks, which operate in the shadow of national politics, by putting the ECB more clearly in the shadow of EU level politics.

More inclusive EU level dialogues focused on industrial strategy and macroeconomic governance, accompanied by a more bottom-up approach for the NPPRs, are likely not only to promote better economic performance but also much more political legitimacy. At the national level, decentralization and democratization of the NPPRs would put responsibility for the country's economics back in the hands of the member-states while opening up economic planning to all potential stakeholders—thereby ensuring real national 'ownership.' This could also help counter the populist drift in many countries, as political parties of the mainstream right and left could begin again to differentiate their policies from one another, with proposals for different pathways to economic health and the public good. At the EU level, moreover, it would allow for more democratic deliberation about goals for sustainable and equitable development while helping to combat populist claims to be the only 'democratic' alternative to EU-led technocratic rule.

Conclusion

All in all, the pandemic response was certainly a radical break with the Eurozone crisis response, and a historic achievement, although not a 'Hamiltonian moment.' The RRF is a temporary fund focused on the pandemic, rather than the fabled 'Eurobonds' that many had hoped for during the Eurozone crisis, let alone the 'Coronabonds' France and Southern Europeans had called for in first month of the pandemic. Moreover, the ‘governing by rules and ruling by numbers’ of the SGP is only suspended, not officially revoked, while the Eurozone still lacks many of the instruments it needs to ensure optimal performance. And the populist revolt that stemmed in large part from citizens’ negative reactions to the Eurozone crisis is not over. But the response to the Covid-19 crisis, which reverses some of the Eurozone’s worst legitimacy lapses, is at least a very good start!

Notably, the Covid-19 pandemic response further legitimated the emergency politics of the ECB with Eurozone monetary policy, which not only normalized its increasingly expansive programs of quantitative easing but further galvanized them in 2020. In contrast, it delegitimated the emergency politics of the Council and the Commission with regard to the SGP’s fiscal rules and numbers which, having been slowly rolled back beginning in 2013, were suspended in 2020, while being accompanied by the taboo-breaking mutual risk-sharing of NGEU. As a result, we could conclude that the EU’s decision-making process during Covid-19, fraught as it was, may very well be what Sévile (this book) defines as ‘modern politics.’ Unlike during the Eurozone crisis, the EU system, albeit under stress, found a positive solution that avoided the coercive imposition of emergency measures to which it had resorted during the Eurozone crisis (see also White, this book).

That said, the EU faces many possible obstacles and stumbling blocks with regard to moving forward. The question of how the EU repays the NGEU debt, with which ‘own resources,’ remains on the ‘to-do’ list. Moreover, political divisions remain in the EU Council, in particular between the frugal coalition and the rest, on future developments. How things play out depends in large measure upon whether the Resilience and Recovery Facility (RRF) proves successful in spurring growth while appearing to be effective, efficient, and devoid of corruption. If it fails to deliver on growth or if the extra investment is not used wisely in the main countries targeted (Italy and Spain), or if rule of law issues emerge, with money going to government cronies (Hungary and Poland), enthusiasm will wane, and the likelihood of creating a permanent fund will diminish.

In addition, the austerity hawks are likely to be back once things get back to some kind of new normal. If the rules are not changed, or at least relaxed, the exit from the ‘escape clause’ of the SGP will have deleterious consequences for those countries that still need time to grow their way out of deficits and debt. Without formal changes in the rules, or at least informal agreements on rules reinterpretations, the ‘austerians’ will have legal grounds to take the Commission to court.

This is equally a problem because the restrictive rules and numbers are written in so many different places in the Treaties and legislation—the Fiscal Compact imposed the institution of the debt brake in national constitutions, the Six-Pack and Two-Pack codified not just the numbers on deficit and debt but also the sanctions to be applied (Jones 2020). And how does one change the Treaties if even one member-state is against, given the unanimity rule on these issues? This can set up almost unsurpassable roadblocks.

In large part because of these obstacles and stumbling blocks, economic, political, and institutional, we need to think innovatively with regard to the future of Eurozone economic governance. Eurozone governance demands a Commission able to deploy a permanent fund to invest in the key areas required for sustainable, equitable growth, while coordinating member-state efforts via flexible guidelines for differentiated evaluations of member-states' economies. It additionally would do best through dialogues that establish general industrial strategy goals as well as macroeconomic targets. But in addition to all of this, it also needs greater bottom up decentralization and democratization, which alone could combat the deteriorating politics 'at the bottom' in which citizens vote for populists out of frustration for their lack of voice and choice. Only by bringing European economic governance closer to the citizens can the EU be sure to build a more sustainable and equitable EU.

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