Introduction

At the Intergovernmental Conference concluded in Maastricht in 1992, all European Community (EC) countries seemed to have come around to the view that a credible and sound counter-inflationary monetary constitution should be adopted (although not necessarily a European monetary constitution, in the cases of the UK, Denmark and Sweden). As was pointed out at the time in the flourishing new political economy literature, joining a monetary union based on institutions capable of delivering price stability was probably the best way to implement this strategy.

In such a case, there would be a tendency for high-inflation countries to benefit more than low-inflation countries from sharing their monetary autonomy in a common monetary institution. The problem therefore became motivating countries that already had credible monetary institutions (and hence low inflation) to share their monetary autonomy with recently ‘converted’ countries with higher rates of inflation and/or higher levels of debt that might resort to their old (inflationary/spendthrift) habits. This explains why the German central bank was perceived as reluctant to embark upon the project of European monetary integration. It was also for this reason that the October 1993 ruling of the German Federal Constitutional Court (BVerfGE 89, 155) ‘exercising its jurisdiction regarding the applicability of derivative Community law in Germany in a “co-operative relationship” with the European Court of Justice’ made German participation in Economic and Monetary Union (EMU) conditional on the guarantee of monetary stability.

In the run-up to EMU, the Committee of Governors of the Central Banks limited the financial stability responsibilities of the future common monetary authority, while the Monetary Committee restricted its scope for policy coordination beyond the monetary area to the fiscal provisions laid out in the Maastricht Treaty. There was a clear division of tasks between these two technical committees and politicians, who, along with the European Commission, confined themselves (or were limited by the circumstances) to setting the conditions for irreversibility and the extraordinary pace of EMU’s implementation.
As a consequence, the broader aspects of economic and political governance in EMU were either not given full consideration or were rejected due to a lack of consensus.

The compromise at Maastricht involved a rapid leap forward to a one-speed monetary union requiring the fulfilment of entry criteria that would test whether (or show, to those opposing EMU or too large an EMU, that) there was a ‘sufficient’ prior convergence of preferences with regard to both inflation and budgetary and fiscal discipline. As in the case of the creation of the European Monetary System (EMS), there were a number of unresolved institutional questions that remained open in order to allow the establishment of a timescale for the creation of EMU (Torres 2009: 57, 62). These questions primarily concerned how to enforce the convergence/stability (entry) criteria once countries had joined EMU and how to further coordinate budgetary and various other policies in order to guarantee the sustainability of EMU. The entry requirements, arbitrary as they might have been, enabled a compromise on various unsettled issues and, as a non-negligible side-effect, made a considerable contribution to the reduction of significant imbalances during the convergence period.

The Maastricht fiscal (entry) criteria were complemented in 1997 by the establishment of the Stability and Growth Pact (SGP). The SGP provided an operational clarification of the Treaty’s budgetary rules and defined the procedures for multilateral budgetary surveillance in its preventive arm (soft law), as well as the conditions under which the excessive deficit procedure would be applied in its corrective arm (Schuknecht et al. 2011: 9; see also Stark 2001). Although its corrective arm was based on ‘hard coordination’ through legally binding obligations, the SGP’s enforcement provisions remained weak, not least because it entrusted the ECOFIN Council (rather than a more representative and long-term-oriented principal such as the European Parliament [EP]) with the capacity to uphold the procedures initiated by the European Commission (Torres 2006: 41). It should be noted that the ECOFIN Council includes member states that have not abided by the Excessive Deficit Procedure (EDP) and those whose future noncompliance is expected.

However, unlike the case of national central banks, which were made independent as qualifying criteria before the inception of EMU, there was no parallel establishment of enhanced national fiscal rules or institutional fiscal arrangements in future Eurozone member countries. Consequently, the monitoring of fiscal policies and debt accumulation was not effective: neither financial markets nor the SGP (with its weak enforcement mechanisms) functioned satisfactorily as fiscal disciplinary devices. The same can be said as far as private debt accumulation is concerned.

In the light of the incomplete Maastricht EMU blueprint in the economic sphere, member states committed themselves to common European Union (EU) objectives and indicators under the heading of the Lisbon Strategy (2000–10) in order to make the internal market deliver sustainable growth. However, member state commitment under the Lisbon Strategy relied on soft coordination (the open method of coordination, OMC) for implementation. This reflects the fact that coordination failure in this case was not expected to put EMU at risk (Pelkmans 2006: 380–5). This risk assessment was only reconsidered after the onset of the financial and economic crisis and the sovereign debt crisis – more specifically, in view of the negative spillovers from the economic side of the Union to the monetary sphere.

Despite a rather successful first decade by many accounts, EMU’s incompleteness (due to a lack of consensus on the institutional model beyond monetary policy) implied institutional fragilities and allowed for building up disequilibria. For example, during EMU’s first decade the lack of national reforms in some member states and the incapacity of financial markets to distinguish between Eurozone sovereigns paved the way for increasing intra-EMU macro-economic imbalances. In addition, economic, financial and fiscal governance institutions were unable to handle increasing policy interdependence. This left EMU institutions, already affected
by the 2008–9 global financial crisis, incapable of dealing with the sovereign debt crisis that began in 2010. In response to the global financial crisis, the EU moved towards increased (albeit insufficient) coordinated financial supervision. With the sovereign debt crisis, new mechanisms of economic governance and stronger fiscal and macroeconomic surveillance mechanisms have been established in an incremental and cumulative fashion in an attempt to sustain EMU and prepare for an eventual leap forward in terms of the increased fiscal and political integration necessary to implement a banking union and avoid financial fragmentation.

This chapter proceeds to examine how EMU’s incompleteness and member states’ unsustainable policies have given rise to economic divergence within the Eurozone and to negative externalities from the economic side to the monetary side of the union, affecting its sustainability. It then analyses EMU’s legitimacy, discussing the strategic political role of the European Central Bank (ECB) in conditioning EU and domestic reforms and in promoting the completion of an economic union in accordance with the sustainability requirements of monetary union. Finally, the chapter discusses how the politicization of EMU has facilitated the internalization at the domestic level of previously agreed-upon EU objectives, and how (despite political conflict in the short run) this may contribute to EMU’s sustainability, enhancing its legitimacy and efficiency and promoting sustainable integration.

The incompleteness of EMU: economic divergence and negative externalities

Admission to the EU club provides access to a larger market but also presupposes some degree of institutional convergence as a precondition for membership through the implementation of the *acquis communautaire*. The possibility of improving economic governance in what had been an open-ended economic union design is conditioned by member states’ views on whether nominal convergence (on rules) and real convergence are mutually reinforcing, or whether there is a trade-off between the two. At earlier stages of EU economic integration, differences in preferences and in national institutions had much less impact than they do now, in a monetary union with more significant interdependencies.

In contrast to monetary union, neither the concept of an economic union nor its significance with respect to the EU is well defined. An economic union could be a stand-alone construct, or it might be designed to meet (at least essential) requirements for the functioning of the monetary union, in line with the Optimum Currency Area (OCA) theory (see Box 41.1).

The EU concept of economic union as set out in the Maastricht Treaty does imply some coordination of economic policies, but was left incomplete with regard to the requirements of monetary union (Pelkmans 2006: 380–5). However, the well functioning of a monetary union (its sustainability) makes additional demands on the concept of economic union with respect to macroeconomic stabilization. Later attempts at reinforcing economic coordination at the European level – notably, increased fiscal coordination through the SGP and the coordination of economic and structural reforms under the Lisbon (thereafter the Europe 2020) Strategy – have been dependent on member state commitment, with weak enforcement mechanisms.

Divergence

The sovereign debt crisis has once again placed the lack of convergence at the top of the European agenda. The former cohesion countries – Greece, Ireland, Portugal and Spain (but also Italy) – diverged (or, in the case of Italy and Portugal, continued to diverge) from the Eurozone core countries in terms of real GDP growth; their low growth rate became an important factor in
their negative risk assessment by the financial markets, which put the sustainability of EMU at risk. EMU had been expected to provide greater macroeconomic stability in cohesion countries, but it was also predicted that it would intensify economic competition and further affect patterns of specialization. The economic consequences would very much depend on domestic policies, as convergence seems to be responsive to policy decisions (Ardy et al. 2002).

Member state progress on the Lisbon Strategy goals, which were intended to create a foundation for competitiveness and sustainable growth, can be seen as an indicator of convergence. A member state that scores poorly will be less competitive and have lower growth (and a lower growth potential). In an analysis of member state and EU progress by policy area and overall, what stands out (apart from the significant persisting differences between member states) are the low rankings of Greece, Italy, Spain and, to a lesser extent, Portugal. These findings suggest that, with the exception of Ireland, those member states that have failed to achieve progress on the Lisbon goals are the countries that have started or continued to diverge.

Spillover effects across policy areas

Prior to the eruption of the crises, most discussions on EMU’s legitimacy and sustainability considered the impact of (the lack of) European political integration as exogenous to the process of monetary integration and governance. There was also a distinct focus on spillovers from the monetary side to the economic side of EMU.

The academic and policy debates during EMU’s first decade of existence (see, e.g., Enderlein 2006) concentrated on the fact that EMU’s one-size-fits-all monetary policy triggered spillover effects across various policy areas. These spillovers from the monetary side to the economic side of EMU could affect its legitimacy and therefore its sustainability. Some authors (notably De Grauwe 2009, 2011) have consistently argued that EMU could not survive without a political union, since the Eurozone has fewer explicit compensation mechanisms than the United States (no automatic fiscal transfers, lower labour mobility and wage flexibility, and less integrated financial markets).

However, there were endogenous legitimizing mechanisms at work – a wider output legitimization of EMU, provided by the EMU cum EU governance framework – that may have contributed to a collective acceptance of EMU’s redistributive implications. These expected

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**Box 41.1 An Optimum Currency Area (OCA)**

Traditional Optimum Currency Area (OCA) theory states that the condition for a country to surrender its monetary autonomy and join a monetary union is that the (microeconomic) efficiency gains must outweigh the macroeconomic costs of participation. These factors are dependent on the characteristics of the country in question. OCA theory has tended to focus on the stabilization policies (the macroeconomic costs) of a monetary union, namely the loss of the exchange rate as an adjustment mechanism; see Torres (2009). For an analysis of the role played by OCA theory in the process of European monetary integration, see Mongelli (2010). The political science perspective, also departing from a cost–benefit analysis at the member state level, concentrates on (political) equilibrium, treating EMU as a problem concerning international relations (i.e. member states making binding/irrevocable commitments) and the assessment of the sustainability of the system (Jones 2002: 84–5).
endogenous effects of the monetary integration process (some of which were political in nature) could compensate in part for non-satisfaction of the traditional OCA criteria, sustaining EMU. In fact, monetary policy spillovers to other policy areas (the concern most frequently discussed in the literature before the crises) seem not to have had much effect on EMU’s legitimacy. This suggests the existence of endogenous legitimizing mechanisms.

On the other hand, the joint impact of the financial and economic crisis and the sovereign debt crisis have made it clear that member states have insufficiently accounted for negative (systemic) spillovers running not from the monetary to the economic sphere but the other way around: from the economic part of the union, where there has been insufficient (financial, fiscal and economic) policy coordination and domestic adjustments to prevent macroeconomic instability and imbalances, to its monetary side. Table 41.1 summarizes the types of spillover effects across policy areas, the mechanisms through which they have materialized and the responses they have provoked.

**Table 41.1 EMU spillover effects across policy areas**

<table>
<thead>
<tr>
<th>Direction of spillover</th>
<th></th>
</tr>
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<tbody>
<tr>
<td>From the monetary side to the economic side of the union</td>
<td>From the economic side to the monetary side of the union</td>
</tr>
<tr>
<td><strong>Mechanism</strong></td>
<td></td>
</tr>
<tr>
<td>One-size-fits-all monetary policy</td>
<td>Insufficient (financial) regulation and (fiscal and economic) policy coordination and structural reforms to prevent major macroeconomic imbalances</td>
</tr>
</tbody>
</table>

**Responses by monetary and fiscal authorities**

- Pressure by some national governments on the ECB to soften its stance by lowering interest rates
- Attempts by member states to coordinate economic and social policies (Lisbon Strategy) and to strengthen the EU’s role in other areas (social, environmental)
- Noncompliance with the rules of the SGP and disregard for the need to control the possible effects of a common interest rate (on bubbles and increasing unit labour costs)
- Resistance of some MS to a real banking union; complaints against OMT as *ultra vires* (with the GCC referring the case to the ECJ)

- Pressure by the ECB on national governments to correct fiscal and macroeconomic imbalances and (also on the Commission, EU Council and European Council, through a strategic collaboration with the EP) to enact institutional reform (increased surveillance, automatic sanctions and clear division of responsibilities with regard to rescue mechanisms)
- The ECB’s non-conventional measures, including the Securities Markets Programme (SMP), Long Term Refinancing Operations (LTRO) and Outright Monetary Transactions (OMT)
- Pressure by some member states on the ECB to act as the lender of last resort
- Enhanced economic governance (six- and two-pack, Euro Plus Pact, as additions to the SGP and the Europe 2020 Strategy, and a new stability pact for Eurozone members with limited treaty changes to enforce fiscal discipline)
- Banking union: the ECB assumes the role of bank supervisor in the Single Supervisory Mechanism
The sovereign debt crisis added urgency to the completion of economic union, as member states sought to address the causes of the crisis (banking fragilities, competitiveness differentials between member states and budgetary disequilibria) and to impede spillovers into the monetary sphere, in particular in the Eurozone.\footnote{11}

In fact, the new mechanisms and institutions reflect member state recognition of the fact that the interplay between monetary policy and wider EU governance and coordinated action will be essential for a successful response to the crisis.\footnote{12} This enhanced governance includes non-standard (arguably quasi-fiscal) ECB measures such as the Securities Markets Programme (SMP), Long Term Refinancing Operations (LTRO) and the establishment of Outright Monetary Transactions (OMT),\footnote{13} the European Semester, the economic governance reform package or ‘six-pack’ (including the reinforced SGP, national budgetary frameworks and the new Excessive Imbalance Procedure), the ‘two-pack’ and the Fiscal Compact (TSCG), the Europe 2020 Strategy,\footnote{14} and further structural reforms as envisaged in the Euro Plus Pact and the new EU financial institutional architecture, notably the Single Supervisor Mechanism (SSM), which is a first step (with bank resolution and deposit insurance mechanisms under discussion) towards the creation of a banking union.\footnote{15} Structural reform has also been part of the formal EU/IMF (Greece, Ireland, Portugal, Cyprus and, in part, Spain) and informal ECB (Italy and Spain) conditionality programmes.\footnote{16}

With the creation of these mechanisms and the implementation of these policies, the issue of the collective acceptance of EMU’s redistributive implications changed in nature, becoming significantly more politicized. As a result, significant divergences and political conflicts have erupted within the member states enacting reforms, as well as among member states and between them and EU institutions (which, as in other key historical occasions referenced above, have generally been bypassed by intergovernmental or even bilateral cooperation). Beyond the achieved consensus, domestic approaches have remained divergent, and the old divisions that impeded a more complete economic union than EMU have resurfaced, even within the European System of Central Banks and the ECB, creating the impression of apparently insurmountable differences.

**EMU legitimacy and the role of the ECB**

Since the outbreak of the crises, despite a consistent level of net support for the Euro (Roth et al. 2012), trust in European and national institutions has decreased substantially. Both the 2008–9 financial crisis and the 2010–11 sovereign debt crisis have also had a negative impact on European citizens’ trust in the ECB, although trust in national institutions, other EU institutions and other central banks (such as the Federal Reserve and the Bank of England) has declined further.\footnote{17} In a situation characterized by a high level of economic, social and political uncertainty, it is hardly surprising that trust would be negatively affected. Surveys (Standard Eurobarometer surveys 74 to 79) also indicate that in the Eurozone, on average, there is a large majority (continuously increasing since January 2009) in favour of further broadening the EU regulatory (EMU cum EU governance) model – that is, establishing greater policy coordination between countries – in order to overcome the sovereign debt crisis.

Unlike a new intergovernmental treaty approved through a ratification process involving all national parliaments, incremental institutional changes do not provide input legitimacy, or at least not to the same extent. In fact, multilevel governance can only be legitimized through rather complex channels of responsiveness. This implies the pursuit of innovative forms of legitimacy, such as throughput legitimacy (as illustrated by the European Parliament’s role as co-legislator in the ordinary legislative procedure, notably in the case of the ‘six-pack’, and in the monetary and economic dialogues)\footnote{18} and (both narrow and wider) forms of output legitimacy for EMU.
The ECB responded to the crisis by providing liquidity (including through non-standard measures), acting as the only European institution that could step in to avert major credit incidents; at the time, intergovernmental funds were either not in place, not operational for buying government bonds or simply not sufficient for the needs of countries such as Italy and Spain. For the same reasons, it also engaged in fostering new mechanisms and the establishment of new institutions, such as (the modalities of) an EU banking union, and agreed to take on supervisory powers. Moreover, in August and September 2012 the ECB announced that it would impose strict conditionality on member states; that is, governments would have to ‘stand ready to activate the European Financial Stability Fund/European Stability Mechanism (EFSF/ESM) in the bond market with strict and effective conditionality in line with the established guidelines’ (ECB 2012) for OMT in secondary sovereign bond markets. These purchases and potential interventions (readiness to act) and other ECB rescue actions throughout the sovereign debt crisis, such as the lowering of the creditworthiness requirement for the collateral that banks had to offer for their refinancing credit, have triggered controversy.19

The ECB has promoted reform in the terms in which it can exert pressure over Eurozone governments: proclaiming its treaty-based independence and withholding its support until governments take the necessary political steps to resolve the crisis. In fact, the ECB has been acting strategically in a consistent way throughout the sovereign debt crisis – specifically, with its support for the European Parliament against the position of the Council on the approval of the ‘six-pack’, and in letters with specific policy recommendations to the Italian and Spanish governments in Summer 2011, in which the ECB made interventions in secondary debt markets conditional upon domestic reforms.

This wider interpretation of the ECB’s mission (its inflation and burden-sharing impacts across member states) has been controversial even within the institution, among members of its Executive Board and its Governing Council. Some members of these bodies have publicly emphasized their disagreements over particular aspects of the ECB’s role, as in the case of the SMP and other non-conventional measures, and over the best way for the ECB to preserve its independence. These divisions within the bank’s Governing Council have affected the overall political equilibrium of the EMU construct, but they also reflect the strategic political role that the ECB plays vis-à-vis the Council and individual Eurozone states. Divergent positions on non-standard measures within the ECB’s Governing Council (namely, between a member of the Executive Board and a national central bank governor of the same nationality) have also resulted from strategic interactions with a particular Eurozone member, notably Germany.

Building on its strategic role and its sense of mission as a solitary institution (Padoa-Schioppa 2000: 37; Dyson 2009; Jabko 2009: 401) in the EMU’s incomplete political construct, the ECB will remain the Eurozone’s ultimate lender of last resort in one way or another. The ECB has been acting strategically in response to the perceived threat to its independence from an incomplete EMU (on its economic side), seeking to derive its legitimacy not only from delivering price (and financial) stability but also from its role as the guardian of EMU objectives, doing ‘whatever it takes to preserve the Euro’. In that sense, it has sought to guarantee what may be viewed as its foremost objective: the sustainability of EMU. This implicit objective has led the Bank to engage in exceptional policies beyond standard monetary tools and wider economic policy debates, pushing for ‘a gradual and structured effort to complete EMU’ (Draghi 2012).20 The strategic role that the ECB has come to play in the multilevel governance context has been particularly relevant for promoting the completion of the economic side of EMU in accordance with the sustainability requirements of monetary union.

However, the EMU’s legitimacy extends beyond the ECB. The EMU cum EU multi-level regulatory model can also affect EMU’s (wider output) legitimacy and sustainability, as it...
encompasses European coordinated action through common agreed-upon principles. These wider political goals feed back into EMU’s legitimacy, in the sense that the steps that have been taken or are envisaged in favour of enhanced economic governance are an open-ended process, associated with a new equilibrium between EU institutions and member states. Although such a response is compatible with the notion of incremental changes (Salines et al. 2011) and new equilibria resulting from an endogenous institutional response to the financial and sovereign debt crises (as explained by rational choice institutionalism), it is also congruent with the surge of a broader impetus for institutional reform that emerged during the crisis.

**The internalization and politicization of EMU at the domestic level**

Since the beginning of the crises, institutional change in the EU – specifically, the completion of EMU (of its economic pillar) with new governance mechanisms – has become the subject of ongoing multilevel political negotiation, allowing for greater participation by many different actors. This negotiation process takes place through a multitude of different channels, including intergovernmental treaties and the possibility of treaty changes (together with referenda and/or changes in national constitutions that might be necessary in some member states), as well as the ordinary legislative procedure (as in the case of most of the ‘six-pack’ and ‘two-pack’ legislation).

In fact, the crises revealed that some domestic policies were not only inconsistent with the stated objectives of the respective governments, but also unsustainable. The gravity of the crises demonstrated that this unsustainability was putting the very functioning of EMU at risk, as well as the respective welfare states and the quality of life for current and future generations.

Most EU countries had failed to internalize the established common objectives of fiscal (SGP) and economic and social governance (the Lisbon and Europe 2020 Strategies). The absence of market pressure – financial markets failed to differentiate between the sustainability of public debt and external imbalances among participants – and of binding and enforceable rules (in the Lisbon Strategy and in the SGP) contributed to the procrastination of some of these (economic and institutional) reforms. The same held true for the announced objectives (voted on in national and European elections on various occasions) to which various governments and political parties had subscribed but that were poorly implemented.

The new crisis-enacted EU governance mechanisms exert an important influence and conditionality (through the availability of financial funds) on the implementation of reforms – which, for the most part, member states’ political systems (governments, oppositions and even social partners) had agreed to in the 1990s and, via the Lisbon process, during the first decade of EMU.

With increasing market pressure, transparency in the domestic political and policy process has increased. The vague references to European restrictions in national political debates have been transformed into fairly concrete constraints that are better understood by citizens, reducing the opacity of domestic political and policy processes. Still, in the face of economic and political uncertainty and amidst the gradual but hesitant and/or insufficiently coordinated EU intergovernmental action, increased contestation at the national level, in spite of its merits of leading to more precise discussions and even to increased effectiveness of special policies (i.e., forward guidance), may lead to political and social disaggregation and conflict. One should therefore keep in mind the inability of national political systems to deal with many of the global challenges that they face, increasing the gap in output legitimacy.

Just as the challenges involved in the creation of EMU may have functioned as mechanisms for economic stabilization, the current challenge of completing the economic side of EMU could similarly foster structural reform and long-term development. A multilevel political negotiation process may also render policy-making more efficient by permitting the continuous
contestation of positions at various levels of government, enabling or facilitating convergence to an acceptable common position for all the levels concerned. On the other hand, by demonstrating that national political systems are unable to deal with the inherent coordination and reform challenges without sharing sovereignty, the current crises may also contribute to the debate on the democratic quality of EU governance at different levels, starting at the national level. Institutions and governments have become more unaccountable through the process of globalization and, in certain instances, also through the process of European integration, impacting the quality of democracy in the union.

De Wilde and Zürn (2012) suggest that the extent to which the level and scope of EU integration have led to greater politicization depends on the more or less conducive political opportunity structure. Some of the most salient elements of this structure in this regard are crises, such as the current sovereign debt crisis.

Furthermore, the conditionality attached to the adjustment programmes of countries receiving financial assistance reflects both supply-side preoccupations (that is, appropriate and legitimate incentives to induce reforms that sustain EMU and member states’ access to financial markets) and a demand aspect of the problem (as citizens increasingly call for ownership of the reforms that impact their everyday lives). These supply- and demand-side elements are associated with different timeframes – for fast (political) institutional change and for slow (cultural) change, respectively.

This contributes to the much higher degree of politicization of EU constraints, which may in turn influence EMU’s legitimacy and sustainability. This is because a wider and more participated debate within better informed (of the challenges in question) domestic electorates may lead to better internalization of nationally compatible objectives and better implementation of domestic reforms, many of which have been hindered by national political systems and cultures. In fact, since the beginning of the crises (fast) institutional change in the EU – the completion of EMU’s economic pillar with new governance mechanisms – has played a role in shaping new common objectives.

Furthermore, access to all these new common mechanisms and institutions has been accompanied by the (at times, hesitant) pursuit of institutional reform and the achievement of the objectives of the Union as laid out in Article 3 of the Treaty on European Union, namely sustainable development based on balanced economic growth and price stability, a competitive social market economy aimed at full employment and social progress, and a high level of protection and improvement of the quality of the environment. Values, beliefs and social norms form the foundation for common rules; at the same time, the multilevel debate opens up the possibility of increased ownership of structural reforms and new institutions by the public. From this perspective, a higher degree of politicization of EU constraints through increased democratic contestation of EU issues within national boundaries can also contribute to resolving the problem of sequential decision-making (Collignon 2010), since multilevel governance may help structure national debates towards common-interest European public goods. These frictions therefore constitute an opportunity for the EU – as various demoi or ‘multiple but connected national politics’ (Nicolaïdis 2013: 352) and/or as a demos in the making – to collectively address its current institutional fragilities.

Conclusion

The steps that have been or will be taken in favour of enhanced governance allowing completion of the economic side of EMU are an open-ended process. As such, they are compatible with the idea of incremental changes and new equilibria resulting from an endogenous institutional
response to the financial and sovereign debt crises. However, the current response may well have reached the limits of its institutional framework with respect to the level of policy interdependence. As a consequence, in theory EMU could potentially disintegrate, should the financial and sovereign debt crisis transform into (and remain) a crisis of democratic governance (Zielonka 2012 and 2014). Alternatively, the crisis could trigger substantially increased economic and political integration, an option that national governments may choose as the less costly and the only effective way to deal with the current challenges.

The role of the ECB in sustaining EMU during the crisis will remain crucial. As a supranational independent institution operating within a changing framework (as EMU is still an incomplete and open-ended mechanism), the ECB will continue to act strategically, pushing for the necessary compromises within the Council. Its role is particularly relevant in the transition to a new steady state in the process of EMU compaction. Such strategic behaviour is not without risks and therefore the ECB has a strong interest in finding ways to be perceived as responsive (within a wider EMU cum EU governance system) and as acting effectively on behalf of the interests of Eurozone citizens. In this sense, the Monetary Dialogue is a very useful platform and can certainly be further enhanced by both the EP and the ECB.

Depending on the path of institutional reforms – ranging from minor adjustments addressing improvements in surveillance and enforcement mechanisms to a re-founding of EMU as a functioning banking union equipped with the necessary fiscal provisions (if and when the Eurozone will get to a real banking union) – the sovereign debt crisis could become a source of new legitimacy for the EU integration process.

The jury is still out as to whether the severity of the current crisis has definitely rendered multilevel governance politically dysfunctional, or whether it may actually be contributing to the resolution of the crisis by addressing long overdue national and EU democratic failures and burden-sharing issues. With the onset of the crisis, the EU agenda has become increasingly politically salient, and the EU debate has been politicized as never before in national elections. These elections have become to a varying extent characterized by high democratic contestation of EU issues. This contestation will also most likely be a feature of the forthcoming European elections, which might provide more political visibility and import to the European Parliament. The real question is then whether this increased politicization will help structure national and European debates towards common-interest European public goods, leading to a convergence of preferences that will allow the EU to collectively (in its diversity) address its institutional fragilities in a more sustainable way.

Acknowledgements

I would like to thank Paul De Gawe, Russell Kinkaid, José Magone, Kalypso Nicolaïdis and Max Watson for very fruitful discussions and suggestions.

Notes

1 This reluctance surfaced again with the sovereign debt crisis and the non-conventional (arguably quasi-fiscal) measures adopted by the European Central Bank.
2 This ruling conditioned the German stance on the creation and expansion of the various rescue packages and financial support mechanisms throughout the Eurozone sovereign debt crisis. It was followed by Bundesverfassungsgericht rulings on the Lisbon Treaty on 30 June 2009, on the rescue packages on 7 September 2011 and on the European Stability Mechanism (ESM) and the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG, also known as the Fiscal Compact) on 12 September 2012. This last ruling opened the door to Germany’s ratification of the ESM Treaty and the TSCG with additional conditions, notably reinforcing the rights of the national parliament. A ruling on the ECB’s Outright Monetary Transactions (OMT) is expected in 2014.
According to Thygesen (2013: 133), who was himself a member of the Delors Committee in his academic capacity, the ECB's very limited responsibilities with regard to financial stability reflected the preferences of the central bankers, who were directly involved in the drafting of its statutes and sought to shelter it from any responsibilities other than the objective of price stability, as well as those of European political leaders, who did not want the institution to become too powerful. However, in the course of the financial crisis (and as far as the banking sector is concerned) the provision of liquidity support to financial markets made the ECB a 'full-scale central bank', although the same support did not materialize in the sovereign debt markets. As stressed by the ECB during the crisis (e.g. Bini-Smagni 2011), solvency support should be provided by national governments in order not to blur the distinction between monetary and fiscal policy and to safeguard the ECB's independence.

See Dyson and Quaglia (2010: 346). In accordance with various studies and reports at the time, the European Commission had stressed the need for policy coordination. See, for instance, Emerson et al. (1992).


The Treaties of Maastricht and Amsterdam did not provide a clear ex-ante specification of the rules of Economic and Monetary Union. See Eichengreen and Ghironi, De Grauwe, Gros, Giovannetti and Marimon in Torres (1996) for a discussion of possible ex-ante specifications of EMU rules concerning, among other things, enforcement mechanisms.

Looking back at the first years of EMU, which featured increasing competitiveness and fiscal imbalances that became particularly acute with the onset of the financial and sovereign debt crises, these unsolved sustainability-related issues included banking, financial, product and labour-market regulation, social policy, competitiveness and other structural policies.

Dyson (2013) describes the situation as a state of supreme emergency, discussing the difficulties of contingent commitments to take exceptional measures at the supranational level.

With the crisis, economic mechanisms (labour mobility, wage flexibility), political/institutional adjustment mechanisms (public insurance mechanisms) and/or the coordination of a number of policies (such as social policy) have been evolving in the direction of greater integration.

See Darvas and Merler (2013) for a thorough account of the ECB's extended roles beyond price stability, its main constraints (fiscal dominance, financial repercussions and regional divergences) and some of the conflicts inherent in its participation in financial assistance programmes and its introduction of the concept of monetary policy under conditionality (in the case of OMT).

In the process, the Lisbon Strategy lost its transitional character, with economic coordination continuing under the Integrated Guidelines (IG) and the Europe 2020 Strategy from 2010 onwards.

For an updated description of those new institutions and mechanisms, see http://ec.europa.eu/economy_finance/economic_governance/index_en.htm.

Financial assistance facilities have included the European Financial Stabilization Mechanism (EFSM, an EU mechanism), the European Financial Stabilization Facility (EFSF, a private company owned by Eurozone countries) and the ESM (an intergovernmental organization).


Besides its monetary dialogue with the ECB, with the adoption of the ‘six-pack’, the European Parliament has engaged in an economic dialogue with the Council, the European Council, the Eurogroup and the European Commission. It has also significantly influenced the development of the ‘six-pack’, the ‘two-pack’ and the SSM. See Torres (2013) and De Schouthete and Micossi (2013).

The global financial crisis and the sovereign debt crisis have shed light on the changing role of most relevant central banks (see Buiter 2012; Torres 2013).
This interpretation contrasts with Dyson’s (2013) view and has potentially different implications for EMU’s legitimacy. Dyson (2013: 221) highlights the risks of ‘abandoning the ground-floor principles of the Maastricht treaty’, with ‘the ECB being drawn into filling a political vacuum’, whereas Torres (2013: 293) stresses the incomplete contract that the ECB is filling in in the new EMU construct.

Both market pressure and peer pressure rose with the transformation of the global financial and economic crisis into the sovereign debt crisis. This implies that the Europe 2020 Strategy (and any extensions of it for the Eurozone and some other EU member states, such as the Euro Plus Pact), although continuing under the same soft method of coordination, will bring about different results. For Schmieding et al. (2013: 3), in 2014 ‘the Eurozone could begin to reap the rewards of reform amid a firming cyclical recovery’, with the combined twin deficits of the four former cohesion countries that were granted external assistance practically disappearing and Germany’s trade surplus diminishing.

National political processes seem incapable of internalizing the consequences of interdependence or providing adequate political incentives in that context (Maduro 2012).

This hypothesis parallels previous analyses of the efficiency of the co-decision procedure (see Torres 2006).

See Rodrik (2011), whose main thesis is that it is impossible for democracy, national sovereignty and economic globalization to occur simultaneously.

According to Roland (2004), ‘culture’, which includes values, beliefs and social norms (such as technology), evolves slowly and continuously and is definitely a determinant of economic growth.

For Tsoukalis (2012: 50), the crisis has generated a lively public debate about the proper method of dealing with it at the European level. This is not merely a juxtaposition of national debates limited to a small number of opinosenti; rather, it involves ordinary citizens.

See Follesdal and Hix (2006), who argue that increased politicization may enhance legitimacy, since a democratic polity such as the EU requires contestation over political leadership and debate over policies. The authors claim that ‘all that may be needed is for the political elites to make a commitment to open the door to more politicization of the EU agenda’ (Follesdal and Hix 2006: 557). The current crisis has had precisely that side-effect, irrespective of the political elites’ stance.

Nicolaïdis (2013: 353) defines ‘European Democracy’ as ‘a Union of peoples, understood both as states and as citizens, who govern together but not as one’, which is distinct from both national and supranational versions of single-demos polities.

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