Facts & Findings

Konrad Adenauer Stiftung

REFLECTIONS ON THE FUTURE OF EUROPE

NOVEMBER 2017
NO. 279

The future of the Economic and Monetary Union (II) – pressure to join?

Proposals of the European Commission for the reform of the Monetary Union and the perspective of the non-euro states from Central and Eastern Europe

Sebastian Płóciennik

Key Points

- The EU member states that do not belong to the eurozone are not only expecting positive results from the currently debated reforms of the Economic and Monetary Union.
- They see a risk of political and economic marginalisation if they do not opt for a rapid path towards membership in the eurozone.
- The latest proposals of the European Commission within the framework of the Reflection Paper on the consolidation of the EMU only partly confirm this perspective.
- The consequences of such a deepening of the eurozone could be far-reaching and very diverse: from a wave of rapid accessions to the eurozone to a wider division within the EU.

CONTENTS

Consolidation of the eurozone: the perspective of non-members

On 31 May the European Commission published a "Reflection Paper", containing its proposals for reform and finalization of the Economic and Monetary Union. The proposals are important not only for the 19 eurozone members, which have a clear interest in a better, more resilient Union, but also for the EU countries that are not part of the Monetary Union. Among them a special group are countries from Central Europe, which joined the EU in 2004: Bulgaria, Croatia, Poland, Romania, Hungary, the Czech Republic. Three things are crucial from their perspective:

Foremost is the success of the eurozone because of the mutual, very intensive trade relations and capital ties. A stronger eurozone would signify better chances for rapid economic growth, even for the non-euro countries. If the core of integration into Europe functions well, the risk of a collapse of the EU would also be greatly reduced.

Secondly, non-euro countries are interested in the thrust of the reforms, not least because of the potential impact on their own institutional systems. After all, they are obliged by accession treaties to introduce the euro and thus adopt the rules created for the eurozone once the accession criteria have been met.

Thirdly, these states are somewhat concerned about the reform plans. They fear that EMU consolidation will entail their own political and economic marginalisation and that the eurozone will become an overpowering core. Gradually, the eurozone would be able to force the other countries to adopt its rules, transforming these states into simple rule-takers.

Marginalisation fears in the foreground

If you follow the debate in the CEE non-euro countries it becomes obvious that their perspective is mainly focused on the third area, i.e. fear of marginalisation

Brexit weakens the non-euro platform

Several reasons exist for this: Brexit, of course, has a great impact here, significantly weakening the "no-euro platform" within the EU. Also important is the increasingly intense debate about a "Europe of different speeds", which was heightened, for instance, through the quadripartite summit of Germany, France, Italy and Spain in March in Versailles and is inevitably associated with the debate on eurozone reform. In addition, there is a conviction among the non-euro countries that the currently functioning structure of the EU, which is in principle based on unity and consensus within the EU-27 framework, secures their interests relatively well and could be jeopardized by eurozone consolidation.

For the above reasons, discussions about the future of the Economic and Monetary Union quickly become associated with a series of detailed questions, which can be formulated as follows:

- Will the consolidation of the eurozone lead to the closure of the institutional structure and the emergence of a hard core with high hurdles to accession?
- Will the consolidation and expansion of the eurozone – which at any rate will determine the direction of the entire integration – be carried out **without consultation and the collaboration of all EU countries?** Will at least the countries that are required to become members be involved in the reform process?

- Does the reform of the eurozone mean that **new, separate political institutions will emerge (a union within the Union)** and EU members outside the eurozone will be marginalized?
- Does consolidation also signify the **creation of a separate budget for the countries of the eurozone** or at least a reorientation of the current spending - with negative effects for the non-members?
- Will the consolidation of the eurozone jeopardize the common single market, e.g. through **restrictions on countries that have an "unfair" advantage through their capacity to devaluate their own currencies?** At first glance, this point may seem exaggerated but given the recent intervention in the rules on employee secondment within the EU, it is no longer considered outlandish by Central Europeans.

The text below discusses the Reflection Paper of the European Commission with regard to the above questions.

A closed core?

The EMU is to remain open for all member states.

Reassuring from the perspective of the non-euro countries are the so-called "guiding principles" of reform, according to which "both the reform of the EMU and its final form" are to remain open to all member states. The core of integration may therefore not be closed. Thus, the idea of establishing a "Europe of different speeds" as a final form of integration appears to be off the table.

Moreover, statements in the Paper demonstrate that the still existing differentiation need not be a ground for open criticism. In the foreword, EU Commissioners Valdis Dombrovskis and Pierre Moscovici agree that the eurozone "was conceived as a promise of prosperity" but that this promise has currently not been completely fulfilled. They thus show their understanding for the procrastination on the part of many non-eurozone members in adhering to the exemption rules and delaying their accession.

Reforms without including the non-euro countries

From the viewpoint of the non-euro countries, the European Commission's proposals regarding the procedures to carry out the reform and finalisation are not very encouraging. The "golden path", of course, would be to amend the Treaty. But if this is not possible, the Commission suggests eurozone countries should coordinate their action outside the treaties, using an intergovernmental approach. This could be construed as a signal to non-members that blockade attempts can be easily circumvented. This method of promoting integration is not new, and has been implemented several times successfully in the past.

Concerns about the tight schedule for eurozone reform

A further concern is the tight schedule for eurozone reform. The first wave of reforms is to be carried out by 2019, the second final wave by 2025. This means that any non-euro country has to seek accession relatively quickly if it still wants to influence the direction of reforms.

Creation of separate institutions

Rapid emancipation of the eurozone from the rest of the EU

With regard to institutional reform, the European Commission points out that many voices exist within the Eurogroup to close access to the decision-making process for non-euro members. The EU Commission only partially counters this demand with the postulate that decisions within the Eurogroup should nevertheless be made "transparently" for the countries outside the eurozone. The conclusion is clear, however: the eurozone will emancipate itself politically from the rest of the EU - and quickly. One indication of this direction, for instance, is the proposal to create a full-time permanent chair of the Eurogroup, whose functions could be merged with those of the commissioner for the EMU. This would mean that a core area of economic policy, for which the Commission had previously been responsible for EU as a whole, would be separated and subordinated to the interests of the eurozone.

In a further step, the gap between the eurozone and the rest of the EU is to be increased through a "treasury". The idea is to consolidate competences now distributed among various institutional levels, including supervision of public finances and economic reforms as well as new areas dealing with possible common European "safe assets" and the capacity for macroeconomic stabilisation. Such an institution would be led by an "EU Finance Minister", who would also be chair of the Eurogroup / ECOFIN and whose activities would be controlled by the European Parliament.

It is not completely clear why the Commission employs the term "EU Finance Minister" and not "Euro Finance Minister". The most likely explanation is that the authors assumed that all EU member states will belong to the eurozone by that time.

A separate budget for the eurozone

The European Commission does not foresee a separate budget for the eurozone in the near future. One proposal in the Reflection Paper, however, is to develop a so-called "macroeconomic stabilisation function", which could lead to a redeployment of spending under the future financial framework, basically cushioning economic shocks. In the longer term, the Commission plans to support public investment and unemployment insurance in crisis countries from a common pool. The Paper does not explain, however, how this mechanism is to be financed. One option would be to include these measures in the next multiannual financial framework. Another option gives priority to separate sources of financing.

Macroeconomic stabilisation function: non-euro countries fear for their shares in the EU budget

As the biggest beneficiaries of the current budgetary structure, this development would be problematic for the non-euro CEE-countries for several reasons. Firstly, in view of these new objectives, the eurozone net payers will be less willing to maintain the current share of the structural funds – the main benefits of EU-membership for poorer members – in the total budget. Secondly, while the macroeconomic stabilization function is foreseen for the entire EU, it is primarily geared towards the needs of eurozone members. Their ability to respond anti-cyclically at the national level is limited through the common currency. This is not the case for the countries with their own currencies.

Little enthusiasm for reform conditionality

Candidates also view the Commission's proposal to make access to EU funds contingent on the implementation of the recommended reforms with little enthusiasm. In the worst case, this mechanism could become an instrument of political pressure, restricting access to financial resources for countries outside the eurozone.

Cohesion of the common market

Positive: Commitment to the integrity of the single market

In the guidelines on the reform project, the authors write that "the integrity of the single market must be preserved" – throughout the EU. The single market must be oriented on the free movement of goods, services, capital and people. The fear that non-membership alone could become a ground for discrimination thus does not appear well-founded. A second point that might be reassuring for non-euro states is the Commission's clear commitment to accelerate convergence, not just in the eurozone but throughout the EU. The authors underscore that this is about creating "resilient economic structures" and not about the "harmonisation of policies or situations across the board" or a "one-size-fits-all" method. It can be concluded that strengthening the free market and competition – and not interventionism - should remain the key convergence mechanism.

Problematic: Some proposals could negatively affect competitiveness.

Some passages in other parts of the text, however, sound more problematic, especially for the Central European countries that still base their competitiveness on relatively low costs. The Commission writes that "better working and living conditions" are to be included in economic policy coordination and that the "European Pillar of Social Rights" will provide a "renewed compass" for further coordination measures. This entails, for instance, aligning member states' business taxation frameworks. The document invokes an earlier proposal (from the Five Presidents' Report of 22 June 2015) envisaging a formalised, more binding convergence process based on agreed standards, including social standards. In the view of Central Europeans, this proposal could easily be used to intervene against the less expensive and therefore annoying competition from Central Europe.

In the context of the single market cohesion the Commission makes another proposal to strengthen the link between the use of EU funds and implementation of reforms on national level. Of course, the question remains whether this vague idea will not become a gateway to aspirations that focus on common standards rather than competition. This is all-the-more evident in that the report addresses issues of competitiveness rather marginally.

Conclusions

After reading the document of the European Commission, it can be concluded that the eurozone is indeed facing a major restructuring and could soon emancipate itself from the current EU, notably through the introduction of new political decision-making bodies, a revision of spending priorities in the common budget and ambitious convergence measures.

Non-euro countries as passive 'rule-takers'?

This would transform current non-euro EU membership into a passive "rule-taker" status in the future, with rules being determined more by EMU countries than by the EU as a whole. The report also makes clear that this restructuring can also be initiated outside the EU treaties, if necessary. The impression again arises that the EU-wide perspective is rather secondary.

Commission is assuming further accessions to the euro area

The European Commission avoids the politically awkward question of the situation of the non-euro countries and their very possible marginalisation by assuming that this problem will resolve itself through further accessions. The Commission obviously assumes that the consolidation of the eurozone entailed with creating a political core of integration will be enough to initiate a wave of expansion. For this reason as well, the EU Commission does not provide either for "punitive mechanisms" for euro "procrastinators" who have not fulfilled their obligations or for any special incentives to accelerate preparations for accession.

There are good reasons for this calculus. Rapid accessions may in fact occur, particularly by small, open economies with strong ties to the eurozone and no problem transferring their economic sovereignty to a supranational level. Other countries who for various political or economic reasons do not (or do not want to) meet the accession criteria will face a troubling dilemma: either they must accept their rule-taker role or they must push for more say and influence over the decisions of the eurozone and/or seek a more pared-down form of EU membership guaranteeing a place in the single market while maintaining more scope for action in economic policy. The last two options signify that new disputes and a further division in the current integration structure cannot be ruled out.

Author

Dr. Sebastian Płóciennik *is Head of the Weimar Triangle Programme at the Polish Institute of International Affairs (PISM).*

Konrad-Adenauer-Stiftung e.V.

Contact:
Olaf Wientzek
Coordinator for European Policy
European and International Cooperation
Phone: +49(0)30/26996-3509
E-Mail: olaf.wientzek@kas.de

Postal address: Konrad-Adenauer-Stiftung, 10907 Berlin

ISBN: 978-3-95721-392-1

www.kas.de