Future prospects
Has the European Social Model really 'gone'?

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Recent events at EU level have led some analysts to discover a 'new' reality. European integration has always been a complex process, consisting of lengthy compromises, ambiguous deals, references to many principles and ideas that each actor then tries to align with her/his own interests and viewpoints. Yet the past few months have seen more unilateral action, consistent with increased conflicts.

For years, the key traits of the European governance – see the Lisbon Strategy in the past and Europe 2020 nowadays – have been defined by and justified through different normative perspectives: neo-liberals have seen the attempt to reinvigorate economic growth and competitiveness according to the free-market principles at the basis of the European project. Social democrats, and 'third way' representatives, have seen new ideas and perspectives (activation, flexicurity, social investments, etc.) taken seriously by EU policymakers. Christian democrats have recognised the traditional principles of subsidiarity and social market economy in the decisions made. Everybody had reason to believe the EU would implement at least part of her/his agenda (see Pochet, 2006 for an overview of the political coalitions supporting the EU project).

2011 did in many respects end the dynamics of the past. Ambiguous deals – originated by the synthesis between different political, ideological and programmatic positions – have been substituted by more ideologically oriented and unilateral interventions. Key official documents (like the Annual Growth Survey or the recent White Paper on Pensions) are more likely to pressurise Member States into introducing austerity measures without any major 'trade-off' with solidarity and growth-oriented measures. And official statements from EU leaders seem to be confirming the new trends. In the following, we take the very recent interview given by the president of the European Central Bank (ECB) to the *Wall Street*

Journal as a sign of the end of the logic of mediation. Mario Draghi was extremely clear about the state of Europe: 'The European Social Model has already gone!' (Blackstone *et al.*, 2012).

That interview did, in many ways, illustrate the very recent evolution of EU discourse about the present and future of the integration process. The following pages focus on three main issues. First we start with an analysis of the supposed death of the European Social Model (ESM). Section two then looks at the actual problem in balancing the ESM with European integration. Section three provides some tempting answers about the need for the EU to further develop its social dimension: while many have interpreted this social dimension as the origin of the European disease, others (including ourselves) stress that it is the most promising step to exit the crisis. We consider this a fundamental element to provide more legitimacy to the European project and to make the European economy grow again. Section four offers some conclusions.

1. The European Social Model is already gone... said Mario Draghi

As shown by the chapters in this book, in the last year the European economic and social context has worsened. The *Great Recession* of 2008-2009 led to the fundamental crisis of the EU project. The EU's incapacity to find a solution to the Greek challenge has put the entire euro zone in danger. Many countries are now coming under pressure from the international financial markets that distrust both EU and national policymakers. Fears expressed by European public opinion have been paralleled and reinforced by the persisting economic problems. And the political debate still seems dominated by the neo-liberal reading.

In *The Wall Street Journal* on Friday February 24 2012, European Central Bank (ECB) President Mario Draghi put forward his ideas on the future of the European social model: it is already dead! For Draghi there is no alternative to tough austerity measures in all of the over-indebted countries; and this will necessarily involve giving up a social model based on job security and generous social benefits. Draghi quoted Rudi Dornbusch: his famous provocative phrase – 'the Europeans are so rich they can afford to pay everybody for not working' – stating that it no longer applies.

While this message from the ECB can be interpreted in terms of a tactic and 'role-shaped' declaration – the 'bad cop' trying to calm international financial markets, confirming that the ECB will control public spending and the implementation of structural reforms across Europe – this appears as further confirmation of the strategy EU institutions are pursuing. The ECB, its allies in Brussels and in some Member States, are using the crisis to finally push through their neo-liberal programme of deregulation and flexibilisation (Leschke *et al.*, 2012). The argument goes like this: Europeans cannot afford the costs of an expensive welfare state and social entitlements that are increasingly outmoded in a global context marked by increased competition from emerging economies whose social standards are much weaker. In the literature the label 'Frankfurt-Brussels consensus' is often used to represent this paradigm. We use it to represent any set of policies that follow three basic principles (see De Grauwe, 2006). First, the way to deal with asymmetric shocks is to increase flexibility. An increase in flexibility and structural reforms raises the sustainability of a monetary union. Second, the Stability and Growth Pact (SGP) provides all the needs for countries to use national fiscal policies as an instrument for dealing with asymmetric shocks that have a cyclical (temporary) component.[1] Third, there is no need to have a Europe-wide budgetary policy to stabilise the business cycle. ECB monetary policy is perfectly equipped to provide for macroeconomic stability. By focusing on price stability the central bank does all that can be done to stabilise output movements.

The EU reflects the neo-liberal doctrine that prevailed in the early 1990s, whereby the areas of competition and macroeconomic policies have to be seen largely as substitutes (Fitoussi and Saraceno, 2004). This is consistent with the reduction in the governments' role in the economy; at the same time the freed resources should be used to increase competition by means of structural reforms. This is why macroeconomic policy in the European institutional setting is not at the centre of the stage; furthermore, it is in the hands of technical bodies like the ECB and constrained within the limits of inflexible rules like the Stability and Growth Pact (Fitoussi and Saraceno, 2004: 8). This fundamentalism

1. By following the SGP prescription of a balanced budget in the medium run, countries have enough flexibility to allow their budget deficit to increase up to 3% during an economic downturn.

is then further aggravated by the objective difficulties of a currency area that is far from optimal (De Grauwe, 2011). The low labour mobility creates a rigidity in the system, for which the solution would be price and wage flexibility. However, in the form required by the theory this has not been experienced anywhere, as it would be socially unbearable. The only way out of this impasse, consistent with the neo-liberal doctrine that permeates the European institutions, is a form of indirect 'flexibilisation', cost containment through fiscal competition and the progressive rationalisation of the welfare state.

The words of the ECB President tally with this perspective. The sacrifice of the European Social Model, through austerity measures plus flexibility and the reduction of social standards, seems to be the only strategy left in order to save the EU.

2. The European Social Model and the difficult balance between economic integration and social cohesion

But what precisely is the European Social Model? And what have been the conditions making it work for so many years in Europe? We refer below to the basic elements of the ESM and the division of labour between EU and national competencies that were supposed to defend it.

The basic idea of the ESM is that economic and social progress must go hand in hand; economic growth, in other words, is to be combined with social cohesion. Jepsen and Serrano Pasqual (2008) see the 'identity marks' of the ESM as generous welfare-state transfers and services together with social regulation of the economy. These translate into the provision of social assistance to the needy, universal provision of education (primary and secondary) and health care, a complex nexus of social insurance and social services, as well as an elaborate system of industrial relations (for a subtler comparison between the European and American models see Alber, 2010).

The past few months have shown the increased pressure on the ESM. As stressed by many contributors in the previous chapters, last year saw an impressive acceleration of European integration, especially in three areas: the attempt to address the sovereign debt crisis; reinforcement of economic governance and stricter EU control over members' public finances. This is full of consequences for the safeguarding of the ESM. The latter is at risk, not just because Europeans seem unable to afford its costs. The mismatch between economic integration and support for social conditions is a further challenge (see also Lehndorff, 2012).

The ESM is at risk because of a changing economic and political context, where the supposed balance between the EU's economic and social dimensions (especially in its new configuration) is difficult to sustain. In the words of Ferrera (2008), when it was launched in the 1950s the EU project was not intended to challenge the national welfare state that is at the core of the so-called European Social Model. By contrast, the founding fathers conceived a virtuous interaction between the Member States' open and integrating economy and the closed space of solidarity defined at the national level. The idea was akin to the division of labour exemplified by the famous *'Keynes at home, Smith abroad'* (Gilpin, 1987). The integration project was meant to favour the Member States' economic competitiveness, through the concrete implementation of the four fundamental freedoms to actually support the completion of the single market. The benefit of this increased economic growth and wellbeing was expected to help reinforce the national roots of the welfare state. And this did happen, at least until the 1970s. Ongoing economic growth granted increased legitimacy to the European project, while it provided the resources the national welfare states required to further integrate European societies.

The virtuous interaction between economic integration at European level and the welfare state at national level culminated in the 1970s (at the end of the 'golden age' of welfare). Afterwards, such an interaction has become much more complicated and hard to fix. In the 1980s, the need to relaunch the European project while safeguarding the national domain of social policies gave scope for a new ambitious project: to complete the single market and then to reach a higher degree of unity through the EMU. At that time, the idea was to revise (not to destabilise) the old compromise between economic integration and social cohesion. The more marked protection under the four fundamental freedoms and the stricter control of budgetary and macro- and micro-economic policies should have been paralleled by the new impetus on the definition of the minimum social 'floor' and the launch of European social dialogue (see Pochet, 2005 for a broad review of the integration of social and economic policies at EU level).

Unfortunately, the supposed balance between the economic and social dimensions has not materialised. Despite all the attempts made, the European social dialogue has seen both advances and setbacks, EU social legislation has not advanced very much, while the attempt to achieve soft coordination through new modes of governance has been partially successful (see Peña-Casas in this issue, and de la Porte and Jacobsson, 2011). What has become increasingly evident (especially after the *Great Recession*) is the different pace of integration in the two economic and social dimensions, and the predominance of the neo-liberal orthodoxy in EU policymaking. As proved by Degryse and Pochet in this issue, economic integration (through the single currency) and especially the coordination of budgetary, macro- and micro-economic policies have largely advanced (see the recent Euro Plus Pact and the European Semester). By contrast, social policy coordination has evidenced more limited steps forward.

The hypothesis outlined below is that the ESM is one part of EU integration and that what is required for more austerity measures is not a more competitive economy. Rather, we need a new articulation of economic growth and social cohesion imperatives.

3. How the European Union can save the ESM: competition, cooperation and solidarity

Starting from our reading so far of the main shortcomings of the strategy pursued, we look here at the more promising ideas proposed by some authors, scholars and think tanks in order to revive the European project (see Bertoncini, 2012; Vignon, 2012, and to some extent Vandenbroucke *et al*., 2011). We focus first on the substantive steps EU policymakers should take to address the main shortcomings of the integration project. We then look at the more political issues, related to the need to revise the strategic game social groups (primarily the trade union movement) must define.

How to save the EU: the substantive dimension

As stressed by contributors to this volume, what marked the year 2011 was the fact that the EU's focus shifted further from the broad socio-economic challenges for smart, sustainable and inclusive growth, to the unidimensional austerity plans for increasing the financial sustainability of public budgets. Despite all this, the economic crisis did not stop, and the EU's political legitimacy declined. 'Balanced budget fundamentalism' (to quote De Grauwe, 2011) therefore seems an inadequate term for a number of reasons. The first has to do with the actual reinforcement of a deflationary bias, where the current priority in Europe ought to be growth and jobs. Targeting public sector deficits entails a continuing emphasis on austerity programmes which risks prolonged stagnation. The second problem and incoherence has to do with the need for adequate and diversified responses to the economic imbalances of individual Member States (Collignon, 2011). The third limit flows from the incapacity to link the new coordination arrangements with the question of financial regulation (Leschke *et al.*, 2012).

A more fundamental criticism relates to the normative place of solidarity in the building of the EU. A number of contributions have recently focused on that issue. While the European integration process is basically keen to develop economic integration through completion of the single market, solidarity has always been present in European discourse and policy decisions since the Treaty of Rome. Since the beginning, as stated by Bertoncini (2012), the ambitious goal of creating a common market and a customs union was set up together with the engagement of the Member States to support farm production. Agriculture solidarity was the first example of solidaristic traits of the integration project. This first step was thereafter complemented by territorial solidarity (through structural funds aimed at promoting financial transfers between countries and territories) and solidarity towards workers through the European Social Fund – to finance workers' training and retraining – and the more recent European Globalisation Adjustment Fund to compensate workers who are victims in the event of company relocations).[2]

In the words of Fabry (2012: 7), solidarity in the EU is not 'an asymmetric mechanism but rather a component in a network of interlocking interests where each party gains something'. Solidarity mechanisms are a natural complement of economic integration and development. Each milestone in the integration process has marked a (renewed) 'solidarity

2. Further solidarity tools relate to the Schengen area and the strategy to deal with natural disasters (see Bertoncini, 2012).

deal' between the Member States to redistribute risks and opportunities. As Delors stressed some decades ago, the EU is based on three key elements: competition, cooperation and solidarity (Vignon, 2012).

If this is the normative starting point of the European project, and the old division of labour between national and supra-national authorities does not work anymore, we need a new balance between the economic and social dimensions. On the basis of what Amato and Mény on the one hand, and Diamond and Liddle on the other, have stressed in their chapters, it is evident that the 'solidarity angle' is now missing. Actually the European Union has tried to implement a new form of solidarity through the stability mechanisms set up after the Greek crisis. But these mechanisms have proved ineffective both from a political and an economic point of view. Europeans are thus in need of more effective solidarity (see Leschke *et al.*, 2012 for a similar analysis). In the literature and the political debate some proposals have been put forward. Here we refer to four of them:

— The financial stabilisation mechanism is for the moment incapable of inverting the negative trends in the financial/bond markets. For some authors this has to do with the curative and emergency nature of the tools set up by the Member States. The same toolkit could be used in line with a different logic: preventing further crises, using resources to boost economic competitiveness and growth through investments, rather than paying national debts (Fabry, 2012);

— The ECB should protect indebted Member States. Highly indebted countries cannot survive attacks from the financial markets without protection from Europe. Their debts exist and cannot be reabsorbed in the short term. The simplest option from an economic point of view is to give the ECB the mandate to intervene to purchase the public debt of the countries under attack. Alternatively, and probably with no need to change the Treaty, the European Financial Stability Facility (EFSF) could be instructed to play this role without any prior political approval. In the latter case, the EFSF should receive financial assistance from the ECB, with practically unlimited resources (Tabellini, 2011; Terzi, 2011).

— Implementing the Lisbon Treaty and the principle of the social market economy. In a more long-term perspective, a growth-enhancing strategy should be pursued by the EU. In line with Articles 3 and 14 of the Treaty of Lisbon, economic services of general interest are a pillar of the social market economy and could be a source of new economic dynamism. Health care, education and training services, and social housing are all instruments that could be at the core of a broad EU strategy to reinforce (rather than destabilise) the social market economy. This could be encompassed in the social investment pact proposed by Vandenbroucke *et al.* (2011) and being paralleled by the revision of the Stability and Growth Pact (SGP) with explicit exemption of 'social investment' spending from the strict budgetary rules. The limited progress made in the social dimension of Europe 2020 (as stressed by Peña-Casas in this issue) could benefit from these new efforts (see also Vignon, 2012);

— Launching a broad project for a truly European public policy solidarity. As stressed by Vignon (2012), Article 194 refers to the solidarity spirit Member States can implement. The energy and climate change policies may represent the perfect field where shared interests could be identified and then pursued. Another field of shared interest could be the military one. Security policy through defence spending is clearly a burden on national budgets, whereas a coordinated EU effort could be the source of decisive economies of scale.

How to save the EU: the political dimension

As stressed by Natali and Vanhercke in the foreword, one of the major effects of the recent trends in European integration has been the growing tension between different political and social actors. This is the result of the more unilateral strategy proposed and pursued by the European Union. Balanced budget fundamentalism implies the more unilateral definition of the EU's political economy and of its economic and social strategy.

Some years ago Pochet (2006) provided an interesting picture of the key coalitions struggling to shape the European economic and social paradigm. Neo-liberals, endogenous-growth theorists, neo-Keynesians and the moderate left represented the four advocacy groups that participated in revising the European political economy. They interacted with each other, influencing the emergence and development of the socio-economic strategy: from Maastricht to Lisbon and beyond. The last few years – especially the transition from the first years of the Lisbon Strategy to its revision and then the emergence of Europe 2020 - have marked the growing role of neo-liberalists ('mainstream economists' in the words of Pochet). Their power has been reinforced through the *Great Recession* and now they seem to dominate the political game in Brussels. As a consequence, the compromise between 'endogenous-growth' theorists and the moderate left (at the basis of the Lisbon Strategy) evaporated.

This has led to the marginalisation of both moderate leftists, leaving neo-Keynesians and the economists more open to a demand-side perspective isolated. While much more research is needed to better understand the political games between different advocacy coalitions, some elements seem already clear.

Orthodox liberalism is now dominating both EU discourse and national policymaking. While DG Ecfin and other economic-oriented actors dominate the scene in Brussels, a new season of technocrats is now taking the lead in some Member States (see the case of Greece and Italy). The left is becoming ever weaker, lacking a real alternative policy proposal. The labour unions (both at European and national level) have reacted but find themselves between a rock and a hard place: the dialogue with liberals seems tense while the interaction with the far left seems unproductive.

Beyond the advocacy coalitions mentioned by Pochet, the role of interest groups seems important here. The alternating interplay between these groups and their resources may alter the political game (see Pierson, 2011). As stressed above, we could interpret last year's innovations as the result of a changing 'balance of power' between different coalitions operating at EU level. If this is the case, the labour movement should question its strategy. The alternative seems to be between once again trying out new compromises with neo-liberals and the endogenous-growth theorists (maybe through a social investment strategy at EU level); and a new attempt to a leftist coalition to reverse the actual paradigm.

4. Prospects and risks for the European Social Model and the EU's social dimension

As shown above, the austerity paradigm is risky and represents a challenge for Europe and its social dimension. While many commentators and policymakers stress that the European Social Model is gone, the policy mix proposed by the EU seems largely ineffective. The countries most at risk are especially incapable of sorting out the vicious circle represented by the reduction in public spending, the freezing of wages, the decentralisation of collective bargaining and the consequent reinforcement of both inequality and economic stagnation.

While many have interpreted the crisis as a challenge to Europe's competitiveness in the global market, a more pressing issue affects the integration process and the ability to renew the balance between economic integration and social cohesion. The old compromise – solidarity within national boundaries, and liberal economic integration in the supra-national context – (as Gilpin put it, '*Keynes at home, Smith abroad*') has disappeared. And the feasibility of the austerity paradigm (a sort of '*Smith both abroad and at home*') is doubtful.

In our opinion, the EU thus requires a new political economy to be supported by a new coalition of interests and ideas. In other words, a new compromise is needed to exit the crisis and provide new legitimacy to the European project. Above, we have put forward some initial ideas for a new EU growth and solidarity-oriented strategy: the development of truly EU policies (e.g. environmental, energy and defence policies), the renewal of solidarity at EU level (new tasks for the European stability mechanism, a more active ECB), and the coordination of national socio-economic policies in line with the 'social investment' paradigm) seem promising.

Nevertheless, to implement a new compromise, political conditions have to change. In the next few months some political events (e.g. the French presidential elections, then the German and Italian elections) could subvert the actual balance of power between the EU and national actors. In such a context two risks seem alarming. On the one hand, the EU's misguided policy strategy is putting the Community's entire economic growth and European integration at risk. On the other, the balance between economic and social groups is particularly negative for the labour movement. Trade unions must react to the actual state of affairs, but they need a clear vision of what alliances and coalitions to build in the near future. All these questions will need to be addressed in the near future.

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