The new European economic governance

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Introduction

In the wake of the financial crisis of 2008 and of the economic crisis which followed from 2009, the member states of the European Union (EU) – and in particular those of the Eurozone – have been confronted, since 2010–2011, by a public debt crisis unprecedented in the – admittedly relatively short – history of the Economic and Monetary Union. The bailout of the financial industry as well as support for the economy and jobs in order to avoid a Great Depression like the one in the 1930s have set in motion a surge in budget deficits and public debt in almost all the EU member states.

Throughout 2011 and in the first half of 2012 the European institutions and the member states were engaged in a veritable head-to head with the financial markets, which appear to have believed that the Eurozone would not withstand this debt crisis and demanded ever higher risk premiums in exchange for financing the public budgets of Greece, Ireland, Portugal, Spain, Italy and others.

Fearing a Greek default and an extension of the crisis to other countries, ultimately risking an implosion of the most ambitious and symbolic EU project, the European Commission, the European Central Bank (ECB) and the member states, in various formations – Ecofin, the European Council, the Euro Group, the Euro Summit – have in various ways sustained the public finances of countries in difficulty: some – the ECB – by the redemption of sovereign obligations on secondary markets (Greece, Ireland, Portugal), some by means of assistance with their balance of payments (Hungary, Lithuania, Romania), some via the European Stability Facility established in 2010 (Ireland, Portugal) and others with bilateral loans (Greece). And this does not even include the ECB's action aimed at providing the banks with cheap liquidity (amounting to around 1,000 billion euros between December 2011 and February 2012).

Some of these bailout measures have been deemed contrary to the European treaties: government aid to banks and, above all, the activities of the ECB on secondary markets, which are considered to constitute an indirect bailout of member states' public finances, which is formally excluded from the ECB's tasks by the treaties (no bailout clause). All the arts of casuistry were needed to get authorisation for these actions (which led to the resignation of Bundesbank president Alex Weber in February 2011, then that of the ECB's chief economist, Jürgen Stark, in September of the same year).

Thus and most importantly the EU and its member states have put in place, amidst some confusion and under pressure from the financial markets, a new set of regulations, procedures and institutions now known as 'new European economic governance'. This new governance[1] is aimed principally, according to its designers, at reinforcing the stability of the Eurozone by putting in place new mechanisms for monitoring, sanctions and coordination, as well as – perhaps in future – solidarity.

The present report will devote Section 1 to an analysis of the weaknesses of the architecture of the Economic and Monetary Union (EMU) as conceived in the Maastricht Treaty signed in 1992. It has been possible more or less to conceal these weaknesses for a dozen years but they were exposed by the crisis that started in 2008. In Section 2 we shall examine, as the crisis continues, the reasons for putting in place the new European economic governance and its ongoing implementation: the strengthening of the Stability and Growth Pact, widening of the field of multilateral surveillance, new treaties (Euro-Plus Pact, Fiscal Compact) and new instruments (European Financial Stability Facility, European Stability Mechanism and so on). This section will also contain a detailed chronology of the principal events at the heart of the Euro crisis – from January 2010 to June 2012 – and which allow us to better understand the political and economic context.[2] Although it may at times appear somewhat tedious this chronology will shed light on the veritable vicious circle that has established itself, with all its recurrent elements: recession, downgrading of credit ratings and commercial banks by the rating agencies, consolidation of budgetary discipline, austerity plans, loss of purchasing power, unemployment, crisis, recession, new credit rating downgrades and so on. In Section 3 we reflect on the direction taken by this new governance, as well as alternative options that have been discussed during the crisis.

Since the present analysis was written when the crisis was culminating – when it could not be ruled out that Greece might exit from the Eurozone – it is difficult to draw a general conclusion: since the actors are, it seems, more than ever immersed in their efforts in this summer of 2012 we recognise that it would not be right to draw conclusions concerning a 'sequence' of the crisis without knowing the outcome or the aftermath. This sequence ends with the Eurozone summit and the European Council of 28–29 June 2012.

1. The reason the European Union generally uses the term 'governance' and not 'government' can be explained by the fact that the EU produces regulations, norms and laws. Although it is not ruled by a European government it exercises political power and thus, in a fashion, governs.
2. This chronology is not intended to be exhaustive, which would be impossible.

1. The defects of the Economic and Monetary Union

Since 2008 the successive financial, economic and public debt crises have revealed the weaknesses and defects of the general architecture of the Economic and Monetary Union, as established in the Maastricht Treaty of 1992. In order to understand the consequences of the crisis for the Eurozone and the remedies applied we have to go back 20 years.

The Maastricht Treaty, signed in 1992 by the heads of state and government of the EU12,[3] launched the project of Economic and Monetary Union (EMU).[4] The creation of a single European currency was a radical political change for the participating countries. It offers benefits such as a reduction in transaction costs, the elimination of exchange rate risks and greater transparency of prices. However, these benefits are accompanied by constraints and disadvantages, including the establishment of a single monetary policy for the entire Eurozone, with monetary policy choices – interest rates, level of inflation and so on – that do not necessarily a priori suit all the participating member states in the same way and at the same time.

Another disadvantage is even more apparent. On entering the Eurozone the member states agree to renounce one of the principal levers of economic policy, namely the national exchange rate, with the irrevocable fixing of exchange rate parities between them. This is the other side of the elimination of exchange rate risk. It is important to understand the importance of this renunciation. In a system of competing markets in the absence of efforts towards convergence of levels of economic development in the countries of the future Eurozone and of a true European ‘economic government’ that would have the means – political and budgetary – to ensure this convergence, renouncing the exchange rate instrument means that the adjustment between national economies at the heart of the Eurozone in the event of crises or asymmetric shocks[5] must be brought about by other variables, such as *internal* devaluation (of which Greece currently offers a striking example) and mobility of labour.[6]

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3. The European Economic Community had 12 member states at the time: the six founders (Germany, Belgium, France, Italy, Luxembourg, The Netherlands), the three ‘Northern’ countries that joined in the 1970s (Denmark, Ireland, United Kingdom) and the three ‘Mediterranean’ countries that joined in the 1980s (Spain, Greece, Portugal).

4. Or rather, relaunched. The project of a single European currency had been formulated for the first time in 1969 (at the La Haye conference, that resulted in the adoption of the Werner report in 1970) (European Commission 1970).

5. In other words, only affecting some members of the Eurozone.

6. Since 2011–2012 waves of emigration have been seen from Greece, Spain, Portugal and Ireland to, chiefly, Germany, the United States and Australia.

Deprived of the instrument of monetary devaluation, how will the countries of the Eurozone, which are undergoing a significant economic crisis and a prolonged recession, be able to maintain or strengthen their competitiveness? It must be underlined here that the renunciation of the exchange rate instrument is accompanied, according to the provisions of the Maastricht Treaty, by a 'no bail out' clause:[7] the European Union or the Eurozone cannot come to the aid of a country in budget difficulties, the Treaty affirms. The principal aim of this clause is to encourage the members of the Eurozone to self-discipline and to avoid moral hazard.[8]

Even before the signing of the Maastricht Treaty there was a debate on the question of whether the real convergence of economies – in other words, convergence of growth, productivity, competitiveness and employment – will occur automatically on entrance to EMU or whether it is necessary to set up a form of European economic government for this purpose. There is every reason to think that if this convergence is effective – and if the economies of the member states become more and more interdependent, the risks of asymmetrical shock will diminish.

At the time, monetarists took the view that monetary union would have an integrative effect: it would compel the convergence of economic policies. According to the neoclassical model of general equilibrium, by letting market mechanisms operate freely they will ensure the optimal development of the Eurozone economies. The monetarists therefore reject the idea of harmonisation of economic policies or of a European 'economic government'. In contrast, Keynesian economists take the view that the process of monetary integration will demand more intensive coordination of economic policies in order to bring about convergence of global demand, prices and production costs.

The Maastricht Treaty, signed in 1992, was inspired more by monetarist than by Keynesian thinking. It put in place a true monetary union, with a federal institution to implement monetary policy – the ECB – but did not provide for an equivalent with regard to economic union. The provision introduced was merely for 'coordination' of national economic policies (Article 121 TEU).

Since 1995 observers have noted that 'many criticisms have been pronounced on the inadequacy of the approach taken [in the Maastricht Treaty] because a large number of problems are yet to be solved. Some concern the asymmetry between a centralised monetary union and an economic union that is at best

7. 'The Union shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of any Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project. A Member State shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of another Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project.' (Article 125.1 du TFUE).

8. In other words, the risk of changes in behaviour – in the sense of a diminution of responsibility – on the part of a government that could in all circumstances count on the possibility of a European rescue.

coordinated. Budgetary policies are subject to a number of uncertainties: a first level concerns the articulation of monetary and budgetary policies and a second is related to the articulation of budgetary policies between themselves. Furthermore, the political dimension of the Union is particularly weak ... The absence of social criteria has also been raised. Moreover, it seems scarcely credible to have a monetary union without the convergence of collective bargaining systems' (OSE 1995).

On this last point the risks of inadequate preparation on the part of the European trade unions with regard to the 'radical' changes expected concerning wages in the monetary union have been emphasised since 1995, in particular by Klaus Busch (1995): 'The unspoken aim of the Maastricht Treaty, in other words, putting in place the necessary wage and price flexibility via the subsidiarity principle applied to wage policy and, consequently, the neoclassical dream of dissolving the trade union cartel with regard to wages, could become a reality'.

More generally, Philippe Pochet (ETUI) (Pochet and Vanhercke 1998: 70) shows that since 1998 the actors have had a very clear view of the social stakes of the Economic and Monetary Union: in theory, it can lead either to economic convergence 'via the market' – in other words, by putting national social systems in competition with one another – or via 'guided' economic convergence.

Almost 20 years later the Euro crisis has revealed the pertinence of these analyses. Of the three letters that make up 'EMU' only the second and third have been realised, leaving economic union in the care of a number of procedures that could, in reality, be reduced – at least before the crisis – to the 'Broad Economic Policy Guidelines' (BEPG), on one hand, and the Stability and Growth Pact (SGP), on the other. Up to 2008 these formal procedures and instruments suggested that this minimum would suffice for the euro as regards 'economic governance'. It was thus essentially the monetarist view that prevailed: even though the question arises of whether or not the Eurozone, in the course of its creation, constitutes an optimum currency area,[9] the instruments for coordinating fiscal policies, wage policies, investment and public borrowing policies are entirely lacking, as we shall see in what follows.

1.1. Broad Economic Policy Guidelines (BEPG)

As implemented by the Maastricht Treaty, the Broad Economic Policy Guidelines (BEPG) are the historical result of the protracted development of the coordination of national economic policies. Originally, the 1957 Treaty of Rome, instituting the European Economic Community, only grants limited

9. Robert Mundell's theory of 'optimum currency areas' (Mundell 1961) – a controversial theory at the time EMU was launched – postulates, in a nutshell, that the criteria and conditions must be respected if calculations of the costs and benefits of a monetary union (costs: loss of exchange rate flexibility; benefits: gains from a single monetary policy, abolition of monetary fluctuations, etc.) are to be optimal in a given area. Cf. for an update of this interesting debate: Krugman 2012.

room for mutual 'consultation' on economic policies between the member states. A brief chapter on 'conjunctural policies' provides that 'Member States shall regard their conjunctural policies as a matter of common concern. They shall consult each other and the Commission on the measures to be taken in the light of the prevailing circumstances' (Article 103 of the Treaty of Rome). In the 1960s three committees were established to this end: the Short-term Economic Policy Committee (1960), the Budgetary Policy Committee (1964) and the Medium-Term Economic Policy Committee (1964). In 1974 these three committees were merged to form the Economic Policy Committee.

In 1986, the Single European Act, which revises the Treaty of Rome, emphasised the 'convergence of economic and monetary policies which is necessary for the further development of the Community' (Article 102A as inserted by the Single European Act). In effect, the prospect of completing the internal market in 1993, followed by the prospect of an economic and monetary union, requires, according to the authors of the Treaty, increased efforts with regard to the 'coordination' of economic policies. The Maastricht Treaty of 1992, which launched the EMU process, modifies Article 103 of the Treaty of Rome (today Article 121 TFEU) in order to instigate an *a minima* process of coordination and surveillance of member states' economic policies via the Broad Economic Policy Guidelines.

The Treaty defines the BEPG procedure as follows (Article 121 TFEU):

1. 'Member States shall regard their economic policies as a matter of common concern and shall coordinate them within the Council …

2. The Council shall, on a recommendation from the Commission, formulate a draft for the broad guidelines of the economic policies of the Member States and of the Union, and shall report its findings to the European Council.

   The European Council shall, acting on the basis of the report from the Council, discuss a conclusion on the broad guidelines of the economic policies of the Member States and of the Union.

   On the basis of this conclusion, the Council shall adopt a recommendation setting out these broad guidelines. The Council shall inform the European Parliament of its recommendation.

3. In order to ensure closer coordination of economic policies and sustained convergence of the economic performances of the Member States, the Council shall, on the basis of reports submitted by the Commission, monitor economic developments in each of the Member States and in the Union as well as the consistency of economic policies with the broad guidelines referred to in paragraph 2, and regularly carry out an overall assessment.

   For the purpose of this multilateral surveillance, Member States shall forward information to the Commission about important measures taken by them in the field of their economic policy and such other information as they deem necessary. '

Although the BEPG are 'recommendations' – in other words, from a legal point of view, legislative acts that suggest a course of action to the member states but without establishing legal obligations in that regard – the member states commit themselves to following these recommendations or, if not, to publically explain why they have not followed them.

The political importance – including domestically – of the BEPG cannot be underestimated, particularly because the European Commission can issue a 'warning' to a member state whose economic policies do not conform with the BEPG, which can result in the adoption (and publication) by the Council of a specific recommendation in this regard. We shall come to this below, but we may note at this point that other procedures, this time with possible sanctions, can be instigated against a country that persistently fails to heed the recommendations made to it (excessive deficit procedures and, since 2011, for macroeconomic imbalances). Finally, we may also note the minimal involvement of the European Parliament in the process: the Parliament is only 'informed' of the Council recommendation determining the BEPG.

Adopted annually since 1993 (and every three years since 2003) the BEPG are thus supposed to ensure closer coordination of economic policies and a 'sustained convergence' of economic performance. By way of illustration, six guidelines were adopted for the period 2005–2008 – that is, just before the financial crisis – which can be summarised as follows (Council of the European Union 2005c):

— Guideline 1: 'To secure economic stability to raise employment and growth potential': compliance with budgetary objectives, correction of excessive deficits, resolution of current account deficits.

— Guideline 2: 'To safeguard long-term economic sustainability in the light of Europe's ageing population': reduction of public debt, reform of pension and health care systems, increasing labour market participation.

— Guideline 3: 'To promote a growth, employment orientated and efficient allocation of resources': reorientation of public spending towards growth, adaptation of fiscal structures.

— Guideline 4: 'To ensure that wage developments contribute to growth and stability and complement structural reforms': appropriate regulation of wage negotiation systems so that the development of nominal wages and labour costs remain compatible with price stability and productivity development.

— Guideline 5: 'To promote greater coherence between macroeconomic, structural and employment policies': implement labour and product market reforms, establish incentives to make work financially worthwhile, flexibilisation and security of employment ('flexicurity'), improving employability.

— Guideline 6: 'To contribute to a dynamic and well-functioning EMU': compliance with the Stability and Growth Pact (see below), an economic policy mix to sustain the economic recovery, while contributing to price stability, continuing structural reforms, consolidating the influence of the Eurozone on the global economy.

The BEPG serve as a common frame of reference in the conduct of national policies; they cover macroeconomic policies, but also microeconomic (Cardiff Process: research and development, innovation, entrepreneurial spirit and so on) and structural policies. As part of the Europe 2020 Strategy they are accompanied by four other guidelines concerning the coordination of employment policies, the fight against poverty and education.

But as we can see, the BEPG and other guidelines are principally directed towards forms of self-discipline: the member states commit themselves to endeavouring, generally speaking, to maintain price stability, robust and sustainable public finances over the long term and structural reforms for the sake of economic growth and employment. Based on a number of common orientations that each member state is committed to comply with, this self-discipline in principle makes it possible to do without economic government. 'In principle', because three weaknesses can be discerned in this process: the first concerns the real effectiveness of the BEPG at national level, the second is related to the strict limitation of the area of coordination of economic policies being implemented and the third has to do with what one might call the myopia of the authors of these recommendations.

In practice, this instrument was rapidly revealed to be ineffective. 'If the BEPG are having a growing impact on national budgetary policies ... they are having less impact on so-called structural policies concerning markets for goods, services, capital and labour. The reality of the impact of the latter aspects on national policies remains a matter for debate, just like the recommendations made within the framework of the European Employment Strategy.' (Math 2002)

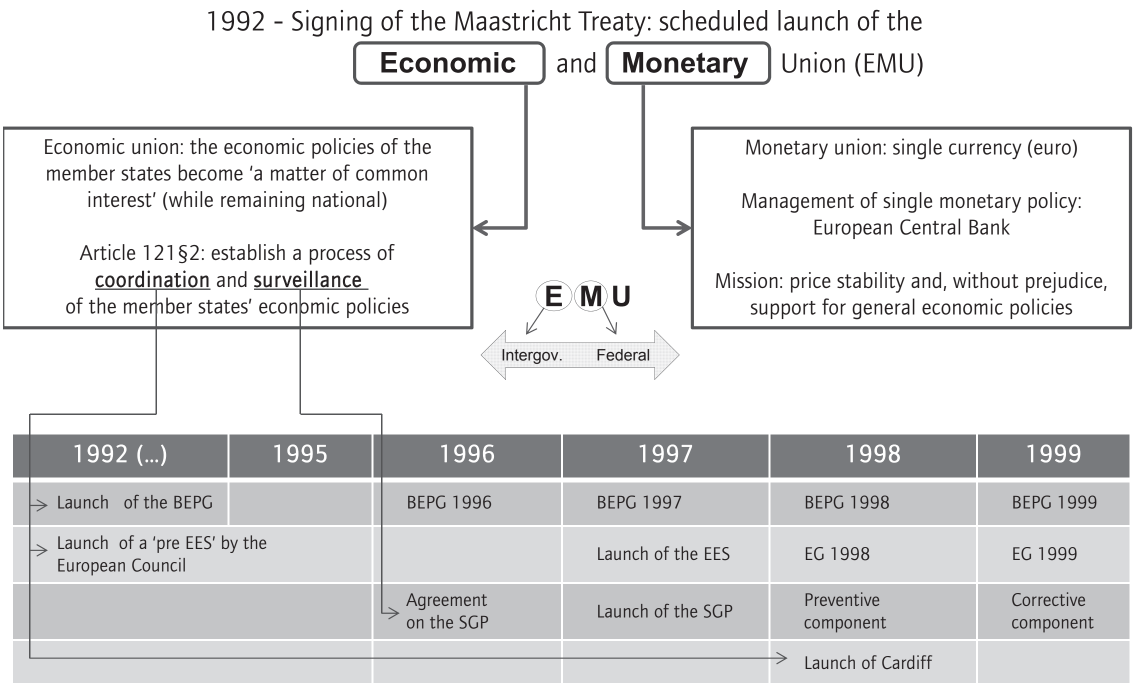
Furthermore, the instrument of the BEPG has from the beginning been focused on price stability, public finances and so-called structural reforms. It has not been used for the convergence or harmonisation of company taxation, wage coordination, progressive convergence of working conditions nor coordination of investment policy. These are all elements that would make it possible for the Eurozone member states or the regions within these member states to avoid basing their competitiveness on fiscal and social competition and on the deterioration of the living standards and working conditions of their populations.

Finally, it should be noted, with regard to their surveillance component based on Commission reports, that the BEPG did not see the financial crisis of 2008 coming. The guidelines adopted in May of that year – in other words, four months before the fall of Lehman Brothers, which marked the outbreak of the crisis – refer to 'effective surveillance of the financial sector' (a sector then in the process of deregulation) designating as priority risk the 'rising spending on pensions, social insurance, health and long-term care systems' and thus calling in particular for budgetary austerity. This discrepancy between an absolute confidence in the functioning of markets and an equally absolute distrust with regard to solidarity mechanisms had a dire effect on the foresight and discernment of the authors of the recommendations.

1.2. The Stability and Growth Pact (SGP)

Besides the BEPG as a mechanism of economic policy coordination – as lax as we have seen it to be – the member states also set up a system of reciprocal surveillance of their respective budgetary policies. This system took the form, in 1997, of the Stability and Growth Pact (SGP). This Pact was cast as two regulations, one preventive and the other corrective. This time the chosen legislative instrument – the regulation – not only exercises legal constraints but is also directly applicable to the member states. This hierarchy of norms seems to indicate that, in the eyes of European legislators, budgetary discipline (regulations) counts more than coordination of economic policies (recommendations).

Figure 1 **On the origins of European economic governance, 1992–1999**



Source: ©Christophe Degryse, 2012
Notes: BEPG: Broad economic policy guidelines
SGP: Stability and Growth Pact
EES: European Employment Strategy
EG: Employment Guidelines
Cardiff: Microeconomic reforms

In summary, the Stability and Growth Pact imposes the following on the Eurozone: control of budget deficits, which must remain below the threshold of 3 per cent of GDP; control of public debt, below the threshold of 60 per cent of GDP; and control of the level of inflation (price stability).

To ensure compliance with this Pact a control system was set up, known as 'multilateral surveillance'. Every year, in April-May, the EU member states submit to the European Commission and the Council a report in which they lay out their budgetary commitments for the year. These reports are called 'stability programmes' (for the countries of the Eurozone) and 'convergence programmes' (for the countries outside the Eurozone). This is the preventive component of the Pact. If a country does not comply with its commitments a sanctions procedure may be launched against it by the Commission and the Council. This procedure can result in the payment of fines. This is the corrective component.

1.3. Euro-confidence (1999–2008)?

The launch of monetary union in 1999 by the irrevocable fixing of exchange rates in relation to one another seems to have generated a climate of 'euro-confidence', reflected in particular in the launch of the Lisbon Strategy in 2000. In March 2000 the EU heads of state and government declared that they wanted to make Europe 'the most competitive and dynamic knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion'.[10]

The Lisbon Strategy constitutes a medium-term programme aimed at reconciling three requirements: economic competitiveness, more and better jobs and sustainable development (component added in 2001 at the European Council meeting in Gothenburg).

These ambitious objectives were to be pursued by means of a new approach known as the 'open method of coordination' (OMC). This has been applied progressively to policies on employment, the fight against social exclusion and poverty, pensions, education and public health. The EU believes it has found, with the OMC, a new instrument for unleashing a process of enhanced policy coordination, although the method's distinguishing feature is that it is not legally binding.

In the context of the fledgling euro, the Lisbon Strategy and impending enlargement to include Central and Eastern European countries the EU seems to have been concerned with reinforcing its unity. This was also the period in which the project of a European constitution was under preparation, reflecting this political ambition of reinforced unity.

10. Lisbon European Council, 23–24 March 2000: Presidency Conclusions.

Figure 2 **Development of policy coordination, 2000–2004**

2000 - Launch of the Lisbon Strategy

'Open coordination' of national policies covers the areas of employment, poverty, pensions, health and education.
A sustainable development strategy has been launched.

	2000	2001	2002	2003	2004
SGP	→	→	→	Suspension of the SGP	
BEPG	BEPG 2000	BEPG 2001	BEPG 2002	BEPG 2003-2005	→
Cardiff	→	→	→	→	→
EES	EG 2000	EG 2001	EG 2002	EES 2003-2005	
Poverty		Launch of the OMC	→	→	→
Pensions		Launch of the OMC	→	→	→
Health					Launch of the OMC
Education		Launch of the OMC	→	→	→
Sustainable Development		SDS 2001-2005	→	→	→

Source: ©Christophe Degryse, 2012
Notes: BEPG: Broad economic policy guidelines
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But as far as the governance of the euro is concerned, the debates are far from over. Since 2002 the Stability and Growth Pact has split member states, the Commission and, more unobtrusively, the European Central Bank. The merits of the criteria adopted for multilateral surveillance have not been universally accepted. Four member states are under threat of sanctions for excessive deficits: Germany, France, Italy and Portugal. More fundamentally, however, in this period of economic crisis – a mere 0.8 per cent GDP growth in the Eurozone – the relevance of the Stability and Growth Pact has polarised opinion, as illustrated by the words of Commission President Romano Prodi in October 2002, who labelled the Stability and Growth Pact 'stupid'.[11]

The early warning mechanism issued by the European Commission against Germany's excessive deficit was rescinded by a decision of the Eurogroup finance ministers. In November 2003 the Commission revived proceedings against the excessive deficits – more than 3 per cent of GDP – being run by Germany and France. On 25 November 2003 the finance ministers decided to suspend these proceedings. It was the Stability and Growth Pact itself that was de facto suspended.

11. In an interview with *Le Monde*, 18 October 2002.

Following this case that set the Commission, the Court of Justice (2004) and the EU Council (2005a; b) against one another a reform of the Stability and Growth Pact was launched that resulted in the entry into force of a 'new' Pact in August 2005. The key new feature concerns the introduction of a certain margin of interpretation with regard to the Stability and Growth Pact criteria. Thus in future the costs of certain major structural reforms – such as pension reform – a serious economic recession or other relevant factors can be taken into account. Likewise, the time period granted to member states with excessive deficits to correct the problem was increased from four to six months. Does this render the Stability and Growth Pact less 'stupid'?

In parallel with this reform of the Stability and Growth Pact two other elements were also involved in 2004–2005: on one hand, the arrival of José Manuel Barroso as President of the European Commission (2004), which meant a strong desire to 'rationalise' the various policy coordination procedures in the wake of the Kok Report (2004); and on the other hand, the signing of the draft Constitutional Treaty by the heads of state and government (2004), followed by its rejection in referendums in France and the Netherlands (2005).

The year 2005 saw Europe plunge into uncertainty and hesitation. The consolidation of political unity – and thus also of coordination of economic and social policies – was no longer on the agenda. The Commission proposed to refocus the Lisbon Strategy, on one hand, on a programme of deregulation and liberalisation[12] and, on the other, a rationalisation of policy coordination procedures.

This 'rationalisation' led to major confusion: the various procedures put in place between 2000 and 2004 were, as the new Barroso Commission put it, 'streamlined'. In other words, the BEPG, the Cardiff Process and the European Employment Strategy (EES) were merged into 24 new 'integrated guidelines', six of which concern macroeconomic policy, 10 microeconomic policy and eight employment policy. Furthermore, the OMCs related to poverty, pensions and health were merged in an OMC related to social protection and inclusion, which lays down three aims in each of these areas.

This 'rationalisation' has transformed the 'open' method of coordination into a process that is more and more closed and technocratic, and in which the role of certain circles of experts has ended up being more important than that of political, economic and social actors.

12. Cf. Van den Abeele (2009). It should also be noted that the financial component of this Strategy – *via* the action plan on financial services and chiefly its aim of improving the prudential supervision rules — will utterly fail to prevent systemic risk. In a Commission Services working document, moreover, this is underlined 'with hindsight … it is evident that the Strategy would have been better structured and more focused on the basic elements comprising the origin of the crisis, such as strict surveillance and the systemic risks of the financial markets, speculative bubbles (such as in the housing markets) and credit-driven consumption' (European Commission 2010a:4-5).

Figure 3 **'Rationalisation' of policy coordination, 2005–2010**

The Commission decides to rationalise the Lisbon Strategy (II)

Macroeconomic (BEPG), microeconomic (Cardiff) and employment (EES) processes are merged.
Furthermore, the poverty, pensions and health processes are merged.

<table>
<tr><th></th><th>2005</th><th>2006</th><th>2007</th><th>2008</th><th>2009</th><th>2010</th></tr>
<tr><td>SGP</td><td>Reform of SGP</td><td></td><td></td><td></td><td></td><td></td></tr>
<tr><td>BEPG</td><td colspan="3" rowspan="3">Integrated guidelines 2005–2008:
6 BEPG, 10 Cardiff, 8 EES</td><td colspan="3" rowspan="3">Idem</td></tr>
<tr><td>Cardiff</td></tr>
<tr><td>EES</td></tr>
<tr><td>Poverty</td><td></td><td colspan="2" rowspan="3">Streamlining OMC social protection and social inclusion:
3 aims Poverty, 3 aims Pensions, 3 aims Health</td><td colspan="3" rowspan="3">Idem</td></tr>
<tr><td>Pensions</td><td></td></tr>
<tr><td>Health</td><td></td></tr>
<tr><td>Education</td><td></td><td></td><td></td><td></td><td>'Education and training' 2020</td><td></td></tr>
<tr><td>Sustainable development</td><td>SDS 2005-2010</td><td></td><td>'20-20-20' Goals</td><td>Energy and Climate Package</td><td></td><td></td></tr>
</table>

Source: ©Christophe Degryse, 2012
Notes: BEPG: Broad economic policy guidelines
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It is thus in a political context of deregulation – including financial deregulation – and equipped with instruments and weak (BEPG, Lisbon Strategy) and short-term or limited (Stability and Growth Pact) procedures of 'economic governance' that the Eurozone entered the crisis in 2008. The governance rules that do exist are blind: prohibition of budget deficits makes no distinction between good and bad public spending nor between investment and current expenditure; other indicators are not taken into account, such as private debt among companies and households, the current account balance or the trade balance.

Finally, as we have seen, neither the BEPG nor the Stability and Growth Pact put in place a true economic union between the Eurozone states, that is to say, involving real coordination of economic and public investment policies, financial regulation worthy of the name at the European level, harmonisation of fiscal policies and better coordination of member states' social policies in order to bring about a certain convergence of the member states' economies. As for the Lisbon Strategy, it laid down certain common objectives and guidelines, but without really managing to trigger a real dynamic of convergence since the instruments at its disposal – the OMCs – were too weak and its objectives too soft. The authors of the Maastricht Treaty of 1992 believed that this convergence would 'happen of its own accord': that the countries sharing the same currency would see their economies converge spontaneously. The crisis showed what a mistake this was.

Nevertheless, up to 2008 the euro was not significantly called into question, despite its defects, incomplete or inadequate rules and abovementioned policy failures (goals of the Lisbon Strategy). That can no doubt be explained by the global credit boom that coincided with the birth of the euro (Wolf 2012). As Michel Aglietta (2012) underlines, the euro, this incomplete currency, had up to then experienced 'calm weather'. Hendrik Enderlein indeed shows that the predictions of the 1990s and the beginning of the 2000s from both political science and economics with regard to the 'gloomy' future of the Economic and Monetary Union have not been borne out (Enderlein and Verdun 2009). Finally, it was against virtually all the odds that use of the euro was able to be extended, without major hindrance, to seventeen member states.

In 2008, however, the weather changed for the worse.

2. The crisis and its lessons

In the wake of the financial crisis that began in the United States in autumn 2008 and facing the systemic risk of the collapse of the European financial industry – a risk not anticipated by the regulatory authorities established within the framework of the completion of the single market for financial services and the probability of whose occurrence seems to have been beyond the purview of the authors of the BEPG – most European governments instigated rescue programmes or nationalisation of their banking sectors, as well as support for their economies. Since the governance of the euro is limited to a number of disciplinary and surveillance rules and these rules can no longer be complied with, all the conditions are in place for the outbreak of a crisis of the economic governance of the Eurozone.

Public debts and deficits are rising sharply in most of the member states. As a first step, the EU governments all became Keynesians: from the partial nationalisation of UK financial institutions announced by the government in October, to the creation of a special fund 'to support the funding of the financial system' in Madrid, besides gigantic rescue plans for the financial sector and industry in the United States, France, Germany and elsewhere, all governments have intervened – or resumed intervention – in the economy. We have seen an increase in public investment – for example, in energy efficiency and research and development – and in investment in infrastructure (for example, railways), plans to support certain kinds of company (in particular SMEs), specific sectoral measures (scrappage premiums in the car sector) and direct assistance to households (in particular the most vulnerable: expansion of social benefits).

Many economists and political figures expressed the view during 2009 that the financial and economic crisis would stimulate green growth (Watt 2009). This crisis is 'a golden opportunity to reorient our economy towards eco-efficiency', as the Swedish Presidency of the EU Council emphasised in July 2009. This 'climatic Keynesianism', to borrow an expression from Peter Newell and Matthew Paterson (2010), is oriented towards clean technologies and renewable energies for a decarbonised economy.

The European Commission – one of whose missions is to tackle state assistance and distortions of competition – has suddenly found itself in an awkward position. It must transform itself into a virtuoso of casuistry in order to endorse state rescue plans and assistance without regarding them as distortion of competition or public subsidy of lame ducks (including financial institutions that have become unviable but kept afloat by the public authorities). Furthermore, the economic recovery programmes presented by the EU member states mention significant increases of public deficits and public debts, mechanisms which, in normal times, would have been targeted by the European institutions in the name of the Stability and Growth Pact.

Admittedly, one might say, this development is temporary and in response to exceptional circumstances. Ultimately, however, the foundations of the theoretical edifice of EU economic policy have been undermined by the crisis: the rationality of economic actors, the efficiency of markets, deregulation, free competition, non-intervention by the state in the economy and so on. Beyond emergency plans, however, this earthquake has not given rise to any change in the economic paradigm since the causes remain open.

2.1. Lessons from the Greek crisis

Before Greece foundered and the threats to the Eurozone emerged three countries that are not members of the Eurozone were confronted, from autumn 2008, with significant balance of payments difficulties: first Hungary, then Lithuania and finally Romania. To help these countries the EU reinforced its Balance of Payments facility, endowed with 50 billion euros (Council of the European Union 2008). But in 2009 imbalances threatened the very heart of the EMU.

Many factors combined to put an end to ‘climatic Keynesianism’ from the second half of 2009 and refocus the European debate on reducing public deficits, budgetary austerity, competitiveness and economic growth (with the qualifier ‘green’ no longer in evidence).

These factors include, of course, the rapid increase in public debts and deficits in almost all EU member states due to the bailout of the financial industry and support measures directed towards the economy and employment. In the Eurozone, according to Eurostat, the government deficit to GDP ratio increased from 2 per cent in 2008 to 6.3 per cent in 2009 and in the EU27 from 2.3 per cent to 6.8 per cent. The government debt to GDP ratio increased from 69.4 per cent at the end of 2008 to 78.7 per cent at the end of 2009 in the Eurozone and from 61.6 per cent to 73.6 per cent in the EU27.

But there was also the ‘discovery’[13] of the Greek case following the PASOK victory in the parliamentary elections in October 2009 and the announcement by the new Prime Minister of the ‘true’ figures with regard to the government deficit, not 6 per cent but 15.4 per cent of GDP.

According to the media at the time, even if Greece has been singled out, every EU member state has used some form of accounting sleight of hand.

13. In fact, it was not really a discovery at all because in 2004 the new Greek Minister of Finance (conservative) had presented the results of an audit demonstrating that the figures of the outgoing socialist government were false.

In 2010 the French daily *Le Monde* conjured up a veritable hypocrites' ball: 'France has benefited from the exceptional dividends of France Télécom when the status of the operator changed. Germany did the same thing with the proceeds of operating licences under the mobile telephony standard UMTS and takes advantage of the separation of the federal and *Land* budgets ... With the Brussels Agreement, [Italy] has multiplied securitisation operations with regard to its debts: resold on the market in the form of financial securities its credit losses disappear from its deficit ... On behalf of Greece, Goldman Sachs enabled the country to 'erase' the equivalent of 1 billion euros from government debt in 2001. And the bank JP Morgan, one banker explained, 'did the same with Italy'.[14] This information sheds a particular light on the 'governance' of the Eurozone.

Nevertheless, the correction in the form of the addition of 9.6 per cent to the Greek deficit does not represent 'only' an extra 22 billion euros.[15] A substantial amount, undoubtedly, but tiny compared to the immense resources that the EU would have to mobilise in the following months and years.

In reality, even more than the falsification of the public accounts the EU 'discovered' that the Greek economy was adrift. Despite being part of the Eurozone Greece has been unable to achieve convergence of its economy, with almost no major export companies, an economic fabric comprising mainly SMEs, self-employed and craftsmen, an economy too dependent on a few sectors, such as tourism, productivity lagging behind and a balance of trade deficit. It also faces a wide range of problems, including ineffective administration, failure to collect taxes and clientism.

Ten years after its launch the Economic and Monetary Union has not had the expected effect of economic convergence. On the contrary, profound macroeconomic imbalances have developed at the very heart of the Eurozone, between its centre and its periphery, in terms of growth, productivity, balance of trade, employment and competitiveness. This is another theoretical failure by the monetarists who had argued that the Monetary Union would have an inherent integrative effect and would compel convergence of economic policies.

This economic divergence, as well as the weaknesses of EMU governance – weaknesses to which they had contributed by camouflaging the real accounts – caused the financial markets to lose confidence in the economies of the Eurozone. They were concerned about the robustness – and thus the solidarity – of this structure, and even more about the sustainability of the public finances of the member states: is it tenable that an economy such as Greece's should share the same currency as an economy like Germany's, the fourth strongest economy in the world?

14. 'Greece at the hypocrites' ball', *Le Monde*, 20 February 2010.
15. Making a Greek GDP of 232.920 billion euros in 2008 (Eurostat : http://europa.eu).

In December 2009, the three big rating agencies downgraded Greek debt and thus began Greece's long descent into hell, followed by Ireland, Portugal, Spain, Cyprus, Italy and the whole Eurozone.

The EU waited until May 2010 before announcing an aid plan for Greece, concocted by the Eurozone, the International Monetary Fund (IMF) and the European Central Bank. The latter for the first time departed from the role laid down for it in the Maastricht Treaty, buying Greek debt on secondary markets. This was revolutionary. But there would be a political price: from May 2010 to February 2012 the various elements of the new European 'economic governance' would be put in place, which some have described as punitive. In what follows we examine these elements in chronological order of appearance.

2.2. 2010: descent into hell

2.2.1. Initial stages of the crisis

Many observers believe a posteriori that if the European Union had not dithered on the subject of an aid plan for Greece the euro crisis would not have taken the turn that it did. However, besides the fact that at the beginning of 2010 no one could have imagined the magnitude that the crisis would assume it should be emphasised that the minimal solidarity laid down in the Maastricht Treaty provides, as we have seen, for a no bailout clause, in other words, no assistance for a country in payment default.

From January 2010, writes *Le Monde*, although 'Greece desperately sought external aid, which was a long time coming, the International Monetary Fund confined itself to technical assistance and the Chinese didn't seem particularly interested in acquiring bonds that every day looked more and more like junk bonds'. The other countries of the Eurozone are also reluctant. The news ... that the Europeans would discuss aid for Greece was immediately denied in Paris and Berlin. Of course there was an element of bluff in all this.'[16] In fact, it was the first round of a poker game: the member states of the Eurozone wanted to put the maximum pressure on the new government of Georgios Papandreou to take the measures needed to clean up the public finances. Greece's partners thus emphatically 'denied' that there is any prospect of an aid plan. But they also knew that they would not be able to let Greece default unless they saw that the Eurozone as a whole was threatened with contagion. The strategy for the Eurozone thus consisted of continuing as long as possible in denial and only giving in at the last moment.

But from February 2010, besides Greece, Spain and Portugal were also targeted by investors who were increasingly calling into question the ability of the Southern European countries to finance their government deficits, as well as the level of solidarity between Eurozone member states. Another

16. *Le Monde*, 29 January 2010.

poker game commenced, but this time between the Ecofin Council (The Council of EU ministers of finance) and the financial markets. Following an Ecofin meeting on 16 February 2010, in a message to the markets, the EU Council Presidency declared: 'If it proves necessary the members of the EU will provide Greece with aid … It is not necessary at this stage to give details on the form this will take', but if such a situation arises 'we have all the instruments' needed to act.[17]

There was talk of euro-bonds to mutualise part of public finances and also of the creation of a 'European Monetary Fund' to come to the aid of Eurozone countries that get into difficulties. The European Commission declared itself ready to propose the creation of such a fund, but the member states were divided on the subject and the ECB was firmly opposed.[18]

Although an aid 'mechanism' for Greece was still being considered behind the scenes Germany started to issue threats. After the declarations of German Minister of Finance Wolfgang Schäuble, calling in *The Financial Times Germany* for a suspension of the voting rights of any uncooperative member state German Chancellor Angela Merkel, in a speech to the Bundestag on 17 March 2010, underlined that the Eurozone needed to be able to exclude one of its members, as a last resort, if they did not comply with the conditions imposed by the Stability and Growth Pact. She questioned any idea of EU support for Greece. In response, the Greek Prime Minister did not rule out turning to the IMF, which was perceived as a disavowal of the Eurozone.

Discussions nevertheless commenced on the idea of a joint IMF–EU aid plan in conjunction with a visit to Brussels of the director general of the IMF, Dominique Strauss-Kahn, and meetings with, in particular, the President of the European Council Herman Van Rompuy, and the President of the European Commission, José Manuel Barroso. But this idea was very controversial. As far as ECB President Jean-Claude Trichet was concerned, IMF intervention – which was at the time applying pressure in the face of European procrastination – in the Eurozone would be positively 'humiliating', while others, including French President Nicolas Sarkozy, began to see a prospect of ducking out. For Angela Merkel, who began to distance herself from her government on this point, possible German aid could be envisaged – in the very last resort – only in connection with IMF intervention and the reinforcement of budgetary discipline within the EU.

This lack of a common vision helped to send the euro plummeting, while on 24 March 2010 the rating agency Fitch downgraded Portugal's long-term debt – from AA to AA– – lending weight to the scenario of Greek contagion.

The European Council meeting of 25 March 2010 was a first turning point in this regard. In conjunction with the Council the Eurozone heads of state

17. Bulletin de l'Agence Europe, 17 February 2010.
18. Bulletin de l'Agence Europe, 9 March 2010.

and government met in the form of a 'Euro Summit',[19] whose work unfolded under the strong guidance of the Merkel-Sarkozy duo. This summit adopted a declaration that essentially comprised three principal points: (i) 'As part of a package involving substantial International Monetary Fund financing and a majority of European financing, Euro area member states are ready to contribute to coordinated bilateral loans'; (ii) 'we commit to promote a strong coordination of economic policies in Europe. We consider that the European Council must improve the economic governance of the European Union and we propose to increase its role in economic coordination and the definition of the European Union growth strategy'; and (iii) 'For the future, surveillance of economic and budgetary risks and the instruments for their prevention, including the Excessive Deficit Procedure, must be strengthened. Moreover, we need a robust framework for crisis resolution respecting the principle of member states' own budgetary responsibility'[20] (this last point resulted in the establishment of Herman van Rompuy's high level group on economic governance). The first and third points mainly reflected Germany's worries and the second point those of France.

Given that at this point Greece had not yet formally requested financial assistance, no operational decision was taken to activate this mechanism of bilateral loans coordinated in combination with the IMF (activation which would only take place 'as a last resort').

2.2.2. First aid plan for Greece (2 May 2010)

In the days that followed the refinancing conditions pertaining to Greek debt deteriorated rapidly. At the beginning of April the rates charged by the financial markets attained the record level of 7.5 per cent, more than double that of Germany.

The activation of the aid plan for Greece became more and more probable. From 9 April the Eurozone countries worked on the specifics of putting it into operation. Since, according to Germany, the Netherlands and Austria, bilateral loans could not be considered 'subsidies',[21] they were to be subject to punitive interest rates of at least 5 per cent. On 9 April Fitch again downgraded Greek debt to BBB–, with a negative outlook. On Sunday 11 April the Eurogroup finance ministers announced the finalisation of the agreement: Europe was ready to make 30 billion euros available to Greece, in addition to IMF aid, making a total of 45 billion euros, intended to 'reassure the financial markets'.

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19. It is notable that the institutional formula 'euro summits', bringing together the heads of state and government of the countries participating in the single currency, was created ad hoc in the course of 2010. This 'institution' is not established in any European treaty, which inevitably raises a number of institutional issues.

20. 'Statement by the heads of state and government of the euro area', Brussels, 25 March 2010.

21. It should be remembered that at the time, 57 per cent of Germans declared themselves hostile to a rescue plan for Greece, according to a survey carried out by the German daily *Die Welt* and the French TV channel France 24.

Two weeks later, on 23 April 2010, Greece official requested activation of the EU–IMF rescue plan. On 28 April it was the turn of Spain's long-term government debt to be downgraded by Standard and Poor's, from AA+ to AA.

On 2 May the member states of the Eurozone announced the activation of the aid plan. In the end, it provided for 110 billion euros: 80 billion euros in bilateral loans and 30 billion from the IMF. This activation was not without a quid pro quo. The Commission, the ECB and the IMF demanded that the Greek government impose an unprecedented austerity plan, raise VAT from 21 to 23 per cent, raise taxes on fuel, alcohol and tobacco by 10 per cent, freeze wages and pensions in the public sector and raise the minimum retirement age. The climate in Athens became almost insurrectional.

If Greece seemed to have been rescued for the time being the whole Eurozone was thrown into turmoil: the crisis seemed to extend to Spain and Portugal; fears arose concerning Italy; the euro fell in relation to the dollar; there were fears of global contagion; and stock markets plunged throughout the world.

2.2.3. The European Financial Stability Mechanism and the European Financial Stability Facility (9–11 May 2010)

The aid plan for Greece thus seemed inadequate to restore calm on the financial markets. To date, EU aid to countries in difficulty has taken two specific forms: financial support mechanisms with regard to the balance of payments (Hungary, Lithuania, Romania – see above) in the amount of 50 billion euros and the EU–IMF Greek rescue plan in the amount of 110 billion euros (30 billion from the IMF). But the EU still does not have a specific mechanism, despite the fact this increasingly appears necessary in the face of the threats looming in a growing number of countries.

The establishment of such a specific mechanism, however, especially from the German standpoint, is confronted by the no bailout clause laid down in the Treaty (see above). It would thus be necessary that such a mechanism concerns solely the granting of reimbursable 'loans' with interest and not 'subsidies'.[22] Furthermore, the softening of Germany's position in this regard was possible only in exchange for substantial strengthening of budgetary surveillance in the Eurozone in the hope that such a situation would not recur. In a joint letter of 6 May 2010 which heralded the emergence of the famous 'Merkozy' (the Franco-German duo Angela Merkel and Nicolas Sarkozy) Berlin and Paris began to dictate the measures they wanted to see taken by the other countries of the Eurozone.[23] 'This crisis has demonstrated that every Member State is responsible for the stability of the Euro Area as a whole and strength of the single currency. For the success of the economic

22. Which, as we saw in 2012 in the case of Spain, led to a vicious circle between public debt and private bank debt.
23. Even though the high level group presided over by President of the European Council Herman Van Rompuy was working in parallel on the new governance.

and monetary union to continue, it is not enough to provide a solution to this crisis. We must … draw the lessons taking all necessary measures to avoid a repetition of this kind of crisis. We need first of all to strengthen the Euro Area's economic governance. … At our forthcoming summit, Euro Area heads of State and government will have to send the signal that they are ready to envisage for the Euro Area: stepping up budgetary surveillance in the Euro Area, including more effective sanctions for excessive deficit procedures and strengthening the consistency between national budgetary procedures and the Stability and Growth Pact; broadening surveillance to cover structural and competitiveness issues and imbalances, and enhancing the effectiveness of the European Union's economic policy recommendations; for the future, options for creating a robust framework for resolving crises respecting the principle of every Member State's budgetary responsibility.' From the start 'strengthen … economic governance' according to the French-German duo was limited mainly to strengthening and expanding surveillance of the member states.

From Sunday 7 May (Eurozone summit) to the small hours of 10 May (Ecofin Council),[24] just before the opening of the Asian markets and just after US President Barack Obama had twice called Chancellor Merkel to try to convince her of the gravity of the crisis, the Eurozone instigated its revolution: it established a European financial stabilisation mechanism (based on Article 122.2 TFEU[25] and an intergovernmental agreement in the Eurozone), by which the member states and the EU declared themselves ready to mobilise 750 billion euros to help governments that experience difficulties and to protect the single currency.[26]

Furthermore, the ECB engaged in active interventions to an exceptional degree, buying back sovereign bonds on the secondary market, interventions fraught with controversy, especially in Germany (see above). On the other hand, the Eurozone governments committed themselves to accelerating consolidation of their public finances, since this was the main perspective under which the reinforcement of governance was presented. This represents the second turning point in the euro crisis.

The regulation establishing the European Financial Stabilisation Mechanism was signed on 11 May 2010 (Council of the European Union 2010). This mechanism is a hybrid: it includes interventions at the EU level as such and at the level of member state governments; it can also have recourse to IMF

24. Conclusions of the Ecofin Council of 9 May 2010.
25. 'Where a Member State is in difficulties or is seriously threatened with severe difficulties caused by natural disasters or exceptional occurrences beyond its control, the Council, on a proposal from the Commission, may grant, under certain conditions, Union financial assistance to the Member State concerned. The President of the Council shall inform the European Parliament of the decision taken.'
26. This mechanism comprises a Community instrument endowed with 60 billion euros, an intergovernmental instrument (European Financial Stability Facility, EFSF), endowed with 440 billion euros' worth of national guarantees (calculated on the basis of the country's contribution to the ECB's capital) and an IMF contribution in the amount of 250 billion euros, making a total of 750 billion euros.

support and ECB assistance. Its mission is to come to the aid of countries that find themselves in budgetary difficulties that threaten the Eurozone. In order to be able to benefit from this mechanism in the form of a loan or a credit line the member state concerned has to present a financial and economic recovery programme precisely describing the measures it intends to take to re-establish financial stability. The European Commission and the ECB are tasked with regular verification of compliance with the aid conditions.

The agreement reached was also a message to the financial markets: the European Union and its member states are ready to mobilise up to 750 billion euros, if need be, to help a government that finds itself in difficulties and to defend the euro and they committed themselves to drastically reducing excessive public debt and deficits, which henceforth constitutes the unalterable priority.

On 7 June the countries of the Eurozone laid down the specific arrangements for the financial stabilisation plan of 9 May: a European Financial Stability Facility (EFSF) was created, endowed with an intervention capacity of 440 billion euros to come to the aid of Eurozone countries that have need of it.

Everything thus seemed in place to save the euro. The political price of all this remains to be paid, namely the launching of 'new economic governance' mainly intended to discipline the countries of the Eurozone. This price was demanded by Berlin in return for its three other big concessions: rescue of Greece, the establishment of a European Financial Stabilisation Mechanism and ECB intervention on the secondary markets.

In summer 2010 the whole of Europe plunged into a spiral of austerity.

Chronology I	**Between austerity spiral and downgrading of credit ratings (summer 2010)**
11 May	After the UK elections on 6 May Conservative David Cameron allies with the Liberal Democrats and succeeds Labour's Gordon Brown. He announces an emergency budget.
12 May	An austerity plan is adopted in Spain supplementing the austerity plan adopted on 29 January which provided for 50 billion euros in public spending cuts by 2013.
13 May	An austerity plan is announced in Portugal providing for tax rises (VAT rises from 20 per cent to 21 per cent, taxes on households and businesses are increased and public spending cut).
18 May	An unprecedented austerity plan is announced in Romania: the government intends to cut public wages by 25 per cent, lay off 10 per cent of public employees, raise VAT by 5 percentage points to 24 per cent and reduce pensions by 15 per cent.
21 May	First meeting of the economic governance task force under the presidency of President of the European Council Herman van Rompuy. Three days previously Germany had decided, alone and without consulting with its partners, to ban naked short-selling of securities and bearish gambles on government bonds.
25 May	Italy announces an austerity plan.

End of May	The first wide-ranging criticisms of austerity in Europe begin to be heard. According to the 2001 Nobel prize winner for economics Joseph Stiglitz 'austerity leads to disaster' and it is by means of solidarity and investment that Europe will exit the crisis.[27]
28 May	Rating agency Fitch downgrades Spain from AAA to AA+.
7 June	Angela Merkel announces an austerity plan for Germany.
8 June	Spanish public employees organise a strike against austerity.
14 June	Credit rating agency Moody's downgrades Greek debt to junk bond status.
16 June	The French government announces a pension reform.
16 June	The Spanish government adopts a labour law reform which includes, in particular, a reduction in redundancy payments.
17 June	At the European Council, the EU27 agree to tighten budgetary discipline.
18 June	US President Barack Obama calls on Europeans to prioritise economic recovery over budgetary austerity.
22 June	The UK Chancellor of the Exchequer (finance minister) announces annual cuts of 40 billion pounds.
2 July	In exchange for new IMF aid Romania steps up its austerity measures.
17 July	The European Commission announces that it is suspending consultations with Hungary on access to loans for its balance of payments, namely 1 billion euros out of a total of 6.5 billion euros. The issue was the lack of agreement between the IMF and EU delegations and Hungary's conservative government on the reform programme to reduce the public deficit.
1 September	The German government adopts an austerity plan which provides for around 80 billion euros of budgetary cuts over four years (2011–2014).
7 September	The Irish government prolongs the bank guarantee scheme. The EU begins to be concerned about the country's economic situation and the disarray of its banking sector.
29 September	A general strike is held in Spain and there is a trade union day of action in Brussels.

2.2.4. Launch of the 'Six Pack' (29 September 2010)

The agreement of 10 May on the rescue plan and financial stabilisation mechanism thus marks the starting point for the establishment of new governance instruments.

In a Communication of 12 May the Commission (2010b) announces its proposal to reform the Stability and Growth Pact and to implement a 'European semester' which would give the EU increased oversight over member states' budgets. It should be noted that while the announced reforms appear at first sight to be extremely restrictive on the member states, the European measures taken to address the roots of the financial crisis are ineffectual: one can be under no illusions about the credibility of the stress tests for European banks that took place in July 2010.[28] This reflects, moreover, an imbalance throughout

27. *Le Monde*, 23 May 2010.
28. A second, 'more exacting' stress-test took place in July 2011, which did not prevent the Spanish government from having to launch a – new – 'truth process' with regard to its entire banking sector in May 2012.

the crisis between the rapidity and severity of austerity measures imposed on public finances and the concessions and incessant reports of supervisory and regulatory measures with regard to private finance.[29]

Following its Communication of 12 May the European Commission elaborated more concrete proposals on 30 June to strengthen economic policy coordination. On 7 September the EU Council approved the principle of the 'European semester' which would be implemented early from January 2011 – even before its formal adoption – in order to ensure consistency ex ante between national budgets and commitments made at the European level.

Thus on 29 September 2010 the European Commission formally proposed the strengthening of the Stability and Growth Pact and new economic governance in the form of the so-called 'Six Pack'. This is a set of six legislative acts – five regulations and one directive – intended to make governance more rigorous within the EU. Four texts centre on budgetary questions and reform of the Stability and Growth Pact, while the two other texts are concerned with the process of identifying and correcting macroeconomic imbalances in the EU and the Eurozone.

— Preventive arm (European Parliament and Council 2011c): modification of the Stability and Growth Pact in order to better guarantee that the member states achieve the medium-term budgetary objective and stick to it. This modification relates to the provisions governing the content, presentation, examination and follow-up of 'stability programmes' and 'convergence programmes' within the framework of multilateral surveillance and the coordination of economic policies. This is the regulation that provides for implementation of a 'European semester'.

— Corrective arm (Council of the European Union 2011b): modification of the legislative basis of the corrective arm of the Stability and Growth Pact. This regulation determines the procedure concerning excessive deficits: the objective is to prevent the emergence of excessive public deficits and, if they emerge, to speed up their correction, compliance with budgetary discipline being examined on the basis of public deficit and public debt criteria (the main change consists of giving more importance to the development of public debt, which henceforth is put on the same footing as the development of the deficit). Member states whose debt exceeds 60 per cent of GDP must take measures to reduce it at the rate of one-twentieth of the difference from the 60 per cent threshold over the previous three years.

29. In the United States from 20 May 2010, the Senate approved the most ambitious financial reform since the 1930s: control of actors, control of systemic risk, control of rating agencies, derivatives, consumer protection and so on. In Europe, it was 2 June before the Commission proposed 'consultations' on the 'possible supervision' of rating agencies, short-selling, improving the corporate governance of financial institutions and so on.

— Sanctions (European Parliament and Council 2011a): this regulation establishes a system of graduated sanctions aimed at enforcing respect for the preventive and corrective arms of the Stability and Growth Pact in the Eurozone. When the Council finds that a member state has not taken measures following a recommendation the Commission recommends the imposition on this state of an interest-bearing deposit amounting to 0.2 per cent of GDP. The Council can oppose this decision only by a qualified majority ('reversed qualified majority').[30] If this state persists in having an excessive deficit it will have to set up a non-interest bearing deposit in the amount of 0.2 per cent of GDP. This deposit is converted into a fine if the recommendations aimed at correcting the excessive deficit are not respected. Moreover, this regulation provides for sanctions in case of statistical manipulation on the part of the member state.

— Budgetary frameworks of the member states (Council of the European Union 2011a): definition of the requirements pertaining to the budgetary frameworks of the member states. This new directive defines the set of elements on which national budgetary governance must be based: accounting systems, statistics, forecasting practices, budgetary regulations, budgetary procedures and budgetary relations with other entities, such as local or regional authorities.

— Macroeconomic imbalances (European Parliament and Council 2011d): establishment of procedures for the detection, prevention and correction of macroeconomic imbalances. Besides surveillance of public finances (deficit, debts), this new regulation provides for regular evaluation of the risks of imbalances ('alert mechanisms'), based on a scoreboard of economic indicators. The member states presenting such serious macroeconomic imbalances will be issued with recommendations by the Council and procedures concerning excessive imbalances will be launched. A Eurozone member state that persistently fails to take corrective measures risks sanctions. The envisaged imbalances concern:

  — at the internal level: public and private indebtedness, the development of the financial markets and the active markets, including the real estate market, the development of the flow of credit in the private sector, the development of unemployment;

  — at the external level: the development of the current account and the net exterior positions of the member states, real effective exchange rates, export market shares, development of prices and costs, and of non-price competitiveness, taking into account the various components of productivity.

30. The 'reversed qualified majority' must be achieved not to *adopt* the decision but to *reject* it. This constitutes an 'innovation' in the European decision-making process which, at the very least, raises a question.

— Sanctions for excessive macroeconomic imbalances (European Parliament and Council 2011b): establishment of implementing measures with a view to remedying excessive macroeconomic imbalances in the Eurozone. This regulation provides for a sanction mechanism if a Eurozone member state persistently fails to follow up on recommendations issued by the Council within the framework of the excessive imbalance procedure. It provides for an interest bearing deposit of 0.1 of GDP if the member state has not taken corrective measures recommended by the Council and an annual fine of 0.1 per cent of GDP if it persistently fails to comply with the recommendations. This sanction is proposed by the Commission and is deemed adopted by the Council unless it rejects it by a qualified majority vote ('reversed qualified majority') with only the Eurozone countries participating in the vote.

This Six Pack was the object of long negotiations between the member states and the European institutions, the stumbling blocks relating to the methods for toughening up the Stability and Growth Pact and, above all, the automatic nature of financial sanctions on the member states that fail to respect its provisions. According to the press at the time the actors were divided into two camps: on one hand, the ECB, the Commission and countries such as Germany, the Netherlands and Austria in favour of automatic sanctions and France, Italy and Spain in favour of room for interpretation.

French President Nicolas Sarkozy used the Franco-German relationship with Chancellor Angela Merkel to try to find a compromise, which they managed on 18 October at their summit in Deauville. On the same day the task force on economic governance under President of the European Council Herman Van Rompuy adopted its final report, which reflects the position of the finance ministers on the Six Pack: a new surveillance framework to better detect macroeconomic imbalances (the future 'European semester') and stronger and more rapid sanctions.

Three days later the ECB, through Jean-Claude Trichet, made it known that it was opposed to the French-German compromise because it meant that sanctions would no longer be automatic. Likewise, it included a footnote in the task force report declaring 'the President of the ECB does not subscribe to all the elements of this report', again in relation to the watering down of the automaticity of the sanctions. The report provides that sanctions shall be deemed adopted unless the Council opposes them by a qualified majority.

At the European Council of 28 October the heads of state and government nevertheless reached two important agreements: they endorsed the report of the Van Rompuy task force on economic governance, thus progressively giving form to this 'new governance' proposed by the Six Pack, and they subscribed to the principle of limited revision of the Lisbon Treaty in order to make the European financial stabilisation mechanism permanent (although the form of this instrument – which remains intergovernmental – did not enjoy unanimity: some states demanded that this revision should not involve any substantial transfer of sovereignty to the EU and that ratification should not require a referendum in the member states).

For its part, the European Parliament began the arduous process of adopting the Six Pack. This process lasted a year and the house divided mainly into conservatives (PPE) and liberals (ALDE), on one hand, and social democrats (S&D) and environmentalists (Green), on the other.

During this period the economic and social situation continued to deteriorate in many member states. In particular, it was now Ireland and Portugal that found themselves in the eye of the storm, before Spain and then Italy. For their part, British, French and German banks appeared to be very exposed to Irish debt.

Chronology 2	**Europe plunges into crisis (autumn 2010)**
29 September	Portugal, confronted by a deterioration in its ability to refinance its public debt, announces a third austerity plan.
30 September	The Irish government announces a tripling of its public deficit for 2010. It increased from 11.6 per cent to 32 per cent of GDP because of a revision upwards of the cost of bailing out the banking sector. At the same time, Dublin launches new austerity measures.
4 October	Thousands of ruined Icelanders vandalise their national parliament. Living standards fell by 15.5 per cent in 2009.
20 October	The British government adopts an unprecedented austerity plan that provides for cuts in public spending of 81 billion pounds up to April 2015 and tax rises of 30 billion pounds.
22 October	In France, the Senate adopts a draft pension reform, despite very strong popular opposition (strikes, demonstrations and so on). This ends retirement at 60 years of age introduced in 1982.
15 November	The Portuguese minister of finance estimates that his country risks having to accept EU financial assistance.
16 November	Rating agency Standard and Poor's downgrades Cypriot debt from A+ to A.
18 November	The Greek government presents its draft budget for 2011, which provides for cuts in the amount of 14.3 billion euros. The cuts mostly concern spending in the public health service, a pensions freeze and the sale of public shareholdings in a number of public enterprises (railways, mines, defence, gambling).
24 November	Massive general strike in Portugal, the first since the revolution of 1974.
24 November	In the United Kingdom thousands of young people protest against the rise in university fees.
1 December	Again under pressure from the markets the Spanish government urgently announces new austerity measures (abolition of unemployment benefits when entitlement ceases), an airport privatisation plan and cuts in corporation tax.

2.2.5. Rescue package for Ireland

From 2008 Ireland's economic situation deteriorated rapidly. After experiencing years of exceptional growth since the end of the 1990s – the famous 'Irish miracle' or the 'Celtic tiger' – the country was the first in the Eurozone to enter recession. The day after US investment bank Lehman Brothers went bankrupt Brian Cowen's government set itself the task of rescuing the Irish banking system: it guaranteed all bank deposits in Ireland. At the end of 2008 it carried out a first capital injection in the amount of 7.5 billion euros, involving three banks: Allied Irish, the Bank of Ireland and the Anglo Irish Bank. In 2009 and 2010 the cost of this bailout – in particular that of the Anglo Irish Bank – exploded, leading to an upward revision of the public deficit.

At the end of September 2010, after the announcement of the tripling of the public deficit – from 11.6 per cent to 32 per cent of GDP – a new poker game began between the Irish government (according to which this new situation was manageable without help) and the financial markets, worried about the country's long-term solvency and increasing the interest rate spread on Irish debt in relation to German rates.

As was the case with Greece in May, the position of the Euro-group was initially extremely ambiguous. On 16 November the Eurozone finance ministers announced that financial assistance for Ireland had been approved in principle, but that it had not been activated because Dublin had not asked for it. The Irish government was concerned, on one hand, by the strict conditions imposed by the EU and the IMF in the event of assistance, and on the other by the threat that these conditions would pose to Ireland's tax system (in the form of a rise in corporation tax, whose very low level – 12.5 per cent – is considered unfair by many of Dublin's European partners).

Nevertheless, beyond the position of the Euro-group, which officially purported to be 'neutral' – in other words, to respect Irish sovereignty – the pressure remained very strong. In a striking declaration the President of the European Council affirmed that the Eurozone and the EU itself would not survive if the budgetary problems were not resolved. For its part, Germany seemed this time to be keen on European intervention – while officially claiming that it did not want to put pressure on Ireland – in stark contrast to its position at the beginning of the Greek crisis. The exposure of German banks revealed by the stress tests could be one explanation of this switch. What is more, Germany was increasingly demanding that the financial sector pay its share in the rescue of European countries finding themselves in difficulty. Finally, fearing that the crisis would spread to Portugal and Spain, the United States advised Europe to act 'very, very quickly'.[31]

31. Timothy Geithner, US Treasury Secretary, 16 November 2010.

On 18 November a joint mission involving the European Commission, the ECB and the IMF – also known as the 'troika' – went to Dublin to explore the arrangements with regard to budgetary assistance 'if required' and to negotiate a restructuring programme for the banking sector.

Three days later, on Sunday 21 November, the Irish government resolved to officially request the activation of European and IMF aid. The EU finance ministers welcomed this request in the hope that it would constitute a new firewall against probable contagion of Spain and Portugal. Domestically, however, the Irish government was subjected to a barrage of criticisms, being accused of sold out national sovereignty. The day after the request for activation, Monday 22 November, the dissolution of Parliament was announced for the beginning of January 2011 and the holding of early elections, although after the parliamentary vote on the austerity plan.

This austerity plan was presented on Wednesday 24 November: it provided for bringing the public deficit back below 3 per cent by 2014 (recall that it was 32 per cent in 2010). It was the IMF that called on Dublin to add another year, extending it to 2015. In order to achieve this the Irish government envisaged spending cuts in the amount of 10 billion euros (cut in the minimum wage, cuts in social benefits, reduction of public sector wages, cuts in public spending, increased tuition fees for university students) and revenue increases in the order of 5 billion euros (increase in VAT, introduction of a property tax), but without touching corporation tax, which remained at 12.5 per cent.

In exchange, the EU and IMF financial assistance was worth 85 billion euros over three years, repayable by 2020. This decision was formally adopted on 7 December by the Ecofin Council. This time Germany insisted that in future the private sector should be involved in the costs of restructuring public debt in case of a risk of default (haircuts[32]). The increasingly numerous declarations of high-ranking German – Minister of Finance Wolfgang Schäuble and Chancellor Angela Merkel – and French (Minister of the Economy and Finance Christine Lagarde) politicians along these lines were accused by their detractors, including the ECB, of being likely to increase the costs of refinancing the sovereign debts of Ireland, Portugal and Spain (because if the financial sector is involved in the cost of refinancing it demands an even more substantial risk premium). The ECB also opposed any form of restructuring of Greek debt, which would be considered a 'credit event' by the rating agencies. In that case, if the private sector was to be involved it could only be on a 'voluntary' basis.

2.2.6. Beyond the 'Six Pack'

The Irish crisis revealed two things in particular: on one hand, it showed that the stress tests of July 2010 were not credible – the Irish banks,

32. In finance, a *haircut* designates a reduction of a certain percentage in the market value of a security issued as collateral. The aim is to reduce the risk of loss in case of the default of the debtor (Sapient Global Markets, *Glossary of Financial Terms*, n.p. n.d.).

including Anglo Irish Bank, had passed them – and on the other hand, that the commitments made within the framework of the legislative package on economic governance, in the process of adoption (Six Pack), were not enough to restore the credibility of the Eurozone on the financial markets and thus its stability.

As regards the stress tests, on 25 November the Commission and the Committee of European Banking Supervisors (CEBS) declared that they were preparing the revision of their methodology. With regard to the Six Pack it suggested – according to the Commission, the ECB and some member states – excessive margins for interpretation, if not flaws: the sanctions procedure was not automatic enough, the period of six months granted to member states experiencing economic imbalance to take measures, possibility given to Ecofin to rule, by qualified majority, on the appropriate character of such measures (before the possible intervention of sanctions) and so on.

In the aftermath of the Irish crisis the conclusion was that it was necessary to take things even further in the strengthening of economic governance, budgetary surveillance and cleaning up public finances (in other words, austerity). At the same time, the threat to Portugal became clearer: the country's capacity to refinance its public debt deteriorated and the prospect of European financial assistance drew nearer.

As for calls to exit the crisis by means of solidarity, establishing euro-bonds – aimed at mutualising part of government borrowings, in other words, converting part of the national debt into European debt – they went unheeded. Although raised chiefly by the President of the Euro-group Jean-Claude Juncker and the Italian Minister of Finance Giulio Tremonti, and supported in one form or another by the European Parliament's Economic and Monetary Affairs Committee, but also by economists such as Joseph Stiglitz and Daniel Cohen, as well as the European Trade Union Confederation, the idea of such euro-bonds came up against the categorical refusal of the German government, based on two principal arguments: moral hazard[33] and the increase in German bond rates that would follow.

The end of 2010 was marked by a meeting of the European Council on 16 and 17 December. The heads of state and government decided to revise the Lisbon Treaty in order to make the European stabilisation mechanism permanent via the creation of the European Stability Mechanism. That would eventually replace the European Financial Stability Facility (EFSF) and the European Financial Stabilisation Mechanism (EFSM).

According to the editorialist of Agence Europe the euro was saved: 'One can write or say what one likes, highlight the partial cacophony between the member

33. A government that could be sure that the financing of its public debt would in any event be guaranteed by mutualised bonds at European level would behave less responsibly in the matter of public finances. Another example of moral hazard: a guarantee of state intervention in the banking system incentivises financial actors to take excessive risks.

states' positions and comment ironically on the ineffectiveness of the EU's institutional mechanisms, but future historians will cite 16 December 2010 as the day European integration took a significant step towards monetary stability and economic governance of the Eurozone, at least partly remedying the historical imbalance between the monetary arm and the economic arm of EMU. These results, which involve a minor modification of the Lisbon Treaty, must be developed and the legal details worked out, but politically it is a done deal.'[34]

On 17 December, one week after Fitch's downgrading of Irish debt, Moody's downgraded Ireland's rating by five notches, from Aa2 to Baa1, seemingly paying little attention to the European commitments.

2.3. 2011: Institutional innovations and exacerbation of the crisis

In what follows we shall begin by examining in detail the new procedures of the European semester, which are supposed to improve budgetary discipline and strengthen multilateral surveillance. After examining these procedures we shall look at the political, economic and social priorities of these procedures in 2011–2012, the first year of – early – implementation of the preventive arm of the Six Pack. We shall then resume the chronology of the crisis which will enable us to understand how and why the European semester has been supplemented by a 'Euro Plus Pact', then a 'Two Pack' supplementing the Six Pack, then the European Stability Mechanism, and then finally the 'Fiscal Compact' which is supposed to round off the architecture of the new economic governance of the Eurozone.[35]

2.3.1. New procedures of the European semester

The new procedure known as the 'European semester for economic policy coordination' is provided for in the Six Pack as a procedure for preventing excessive imbalances and the coordination of member states' economic policies.

It involves various elements, which can be summarised as follows (Article 2 of Regulation (EU) No. 1175/2011):

— economic policy coordination: the formulation of the BEPG and surveillance regarding their implementation at national level;

— employment policy: the formulation of employment policy guidelines (EEPG) and scrutiny of their implementation at national level;

34. Bulletin, Agence Europe, 18 December 2010.
35. Subject to any modifications that might be made or supplements that might be added to it in the aftermath of the presidential election in France and commitments made in this connection by new French President François Hollande.

— public finances: presentation and evaluation of 'stability programmes' (for the Eurozone countries) or 'convergence programmes' (for countries that are not in the Eurozone);

— structural reforms: presentation and evaluation of member states' 'national reform programmes' (NRP). These NRP must take account of the BEPG and the employment policy guidelines, as well as guidance issued by the European Commission and the March European Council in the Annual Growth Survey (AGS);[36]

— recommendations: the initiation of procedures to correct possible budgetary or structural imbalances. On the basis of Commission recommendations, the Council adopts 'country-specific recommendations' (CSR);[37]

— national budgets: the member states should take due account of the guidance given them for working out their economic, employment and budgetary policies before taking major decisions on their national budgets in the coming years. The Commission will monitor developments.

There is a link between the European semester and the 'Europe 2020' medium-term economic strategy, although the nature of the link is far from clear in official documents (and although the ambition of the Europe 2020 strategy has faded considerably due to the euro crisis; in 2012 it no longer seems a priority). Remember that the objectives of this strategy include issues totally ignored by the European semester, such as the fight against global warming and the fight against poverty:

— employment: an employment rate of 75 per cent among 20–64 year-olds;

— research and development: 3 per cent of GDP invested in research and development and also innovation;

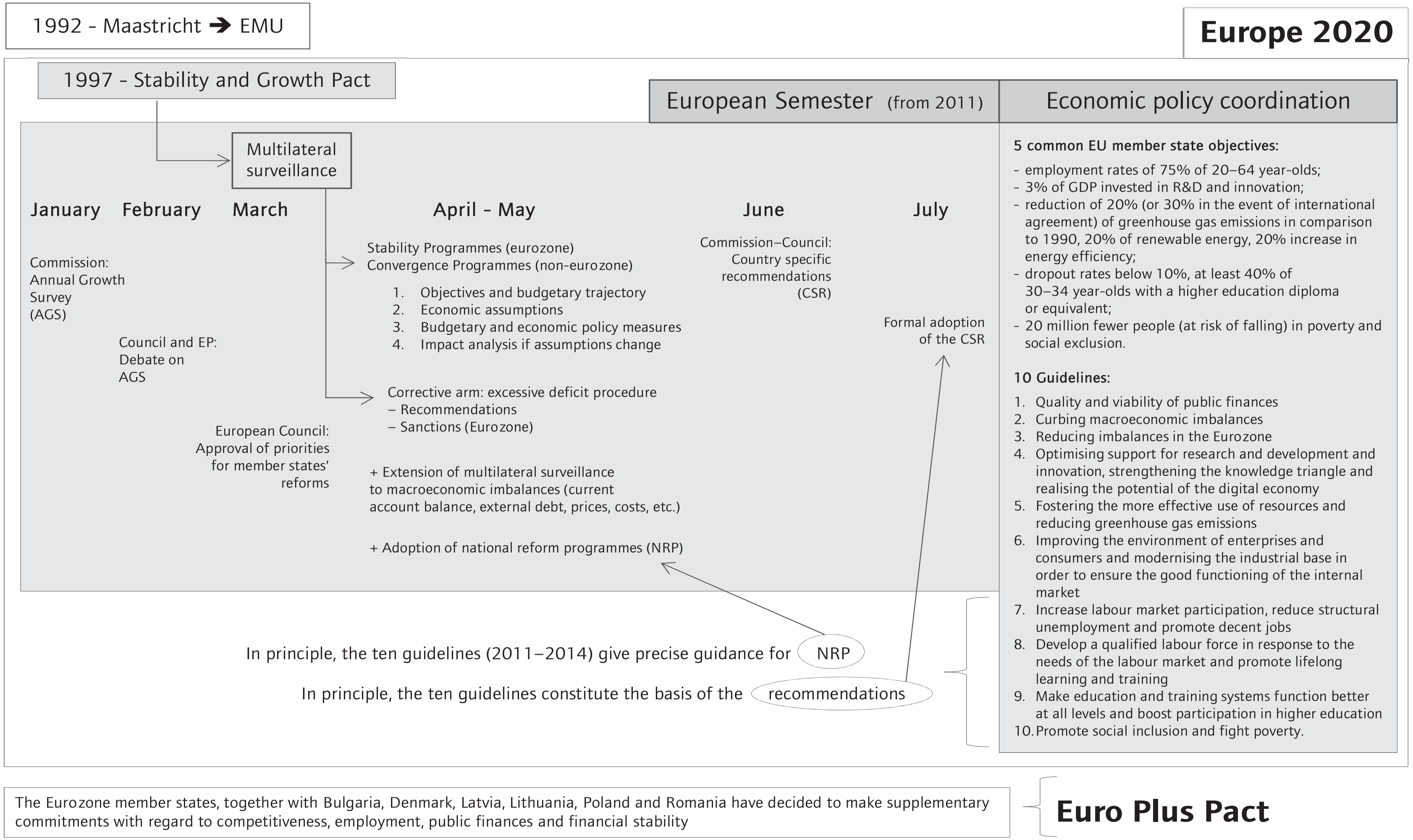
— climate: reduction of 20 per cent (or 30 per cent in the event of international agreement) of greenhouse gas emissions in comparison to 1990, 20 per cent of renewable energy and a 20 per cent increase in energy efficiency;

— education: dropout rates below 10 per cent, at least 40 per cent of 30–34 year-olds with a higher education diploma or equivalent;

— poverty: 20 million fewer people (at risk of falling) in poverty and social exclusion.

36. Cf. European Commission, http://ec.europa.eu.
37. Cf. European Commission, http://ec.europa.eu.

Figure 4 **The European semester**



Source: ©Christophe Degryse, 2012

The European semester is thus an annual cycle of ex ante economic policy coordination and budgetary surveillance of the member states; it provides a framework of guidance and surveillance before the member states set their final budgets for the following year (see Figure 4).

There are three main innovations of the European semester in comparison to the old procedures of the Stability and Growth Pact.

First, the field of surveillance and the prevention of imbalances is widened considerably: it is no longer only a matter of fiscal imbalances (public debt, public deficits), but also of global macroeconomic imbalances. Every member state is henceforth subject to close screening based on a 'scoreboard' of macroeconomic indicators: public and private debt, development of the financial markets and the active markets (including real estate), development of credit flows in the private sector, development of unemployment, development of the current account balance and member states' net external positions, development of real effective exchange rates, export market shares, development of prices and costs and non-price competitiveness, taking into account the various components of productivity.

There is also the strengthening of the binding character of this surveillance in the case of excessive fiscal or macroeconomic imbalances (sanctions in the form of interest-bearing or non-interest-bearing deposits which can be converted into fines). As already mentioned, these sanctions are not completely automatic, but the procedure of their adoption has been made considerably easier in comparison to the old Stability and Growth Pact procedure: after being proposed by the Commission they are 'deemed to have been adopted' by the Council unless they are *rejected* by a qualified majority.

Finally, there is the issue of ex ante surveillance: the presentation and evaluation of stability and convergence programmes occur before major decisions are taken concerning national budgets.[38] On this basis, the whole purpose of the European semester is henceforth to ensure beforehand the conformity of budgets, structural reforms and policies with European discipline and objectives.

2.3.2. Contents of the European semester 2011

These innovations considerably reinforce the Stability and Growth Pact. The focus of the European semester in 2011, very succinctly, was as follows.

Annual Growth Survey 2011

The Annual Growth Survey (AGS) in 2011 presented by the European Commission (2011a) early in the cycle – that is, January 2011 – presents ten priorities for member states' policies:

38. Point 7 of Regulation (EU) No 1175/2011 (European Parliament and Council 2011c).

— macroeconomic prerequisites for growth: (i) implement rigorous budgetary consolidation, (ii) correct macroeconomic imbalances and (iii) ensure the stability of the financial sector;

— mobilise labour markets and create jobs: (iv) make work more attractive, (v) reform pension systems, (vi) reintegrate the unemployed in the labour market and (vii) reconcile security and flexibility;

— give priority to ('frontloading') growth-enhancing measures: (viii) exploit the potential of the single market, (ix) attract private capital to finance growth and (x) enable access to energy at affordable prices.

To sum up, the vision of the European Commission for exiting the crisis centres on fiscal consolidation, structural reforms and targeted investments.

National Reform Programmes 2011

Naturally, it is impossible within the framework of the present study to examine the NRP of the 27 member states. Nevertheless, in order to get an overall view we can use a study (Degryse 2011) focusing on the reforms announced by 13 countries (Belgium, Cyprus, Czech Republic, Denmark, France, Germany, Greece, Ireland, Latvia, Poland, Romania, Spain and the United Kingdom) in their NRP 2011 focused on seven themes. In the absence of a detailed examination we will take an overall view of the spirit in which these NRP were drafted in the different countries.

With regard to the public sector and public spending all the countries under consideration – with the exception of Ireland and Belgium (caretaker government) – in 2011 provided for a set of measures aimed principally at controlling spending, improving the effectiveness and transparency of administration, enhancing the efficiency of public spending and in some instances restructuring or liberalising state-owned enterprises (Czech Republic, Greece, Latvia and Romania). Very few countries – such as Denmark and Spain – announced plans to invest in green infrastructure or in saving energy in public buildings.

With regard to public employment, in the countries under examination, nine countries engaged in public service reforms. These measures essentially are related to public sector pensions (Cyprus, France, Greece, Ireland, Romania, United Kingdom), wages (Cyprus, Czech Republic, Greece, Latvia, Romania, Spain) and hiring freezes (Cyprus, Greece).

Concerning public services in the broad sense the measures taken are aimed in particular at enhancing competition on the energy (gas and electricity) and passenger transport (rail and bus) markets. This enhancing of competition takes place chiefly through privatisation, in particular in Greece and Romania. Other measures concern the development and modernisation of infrastructure (telecommunications, technological research and development, transport and so on).

In health care, seven countries out of the 13 under examination provide for measures aimed primarily at reducing spending. Thus five countries (Cyprus, Czech Republic, Germany, Greece, Romania) are implementing health service reforms aimed, among other things, at establishing mechanisms to control spending, capping certain items of expenditure and better managing the supply of medicines (generic, public procurement and so on). Only two countries also provide for the implementation of measures aimed at improving access to health care among the disadvantaged (Denmark, Romania).

In general terms, the measures presented in the NRP with regard to education and training concern access to educational infrastructure and availability (Czech Republic, Denmark, France, Ireland, Spain, United Kingdom), enhancing vocational training and apprenticeships (France, Latvia, Poland, Romania, Spain, United Kingdom), lifelong learning (Belgium, France, Latvia, Poland, Romania), the issue of the certification and evaluation of curriculums (Czech Republic, Greece, Romania, Spain), general organisation restructuring and structural reforms (Denmark, Greece, Romania), the definition of target groups (Germany, Ireland) and, finally, improving the link between education and labour market needs (Cyprus, Germany).

Concerning social inclusion, the main measures concern specific actions (activation policies) in relation to the disabled, the elderly, immigrants and so on (Cyprus, Czech Republic, Denmark, France, Germany, Greece, Ireland, Latvia, Poland, Romania, Spain), the development of social services (Czech Republic, Denmark, Greece, Poland, Romania), reform of social protection systems (Cyprus, Czech Republic, Latvia, Romania, United Kingdom), income protection (fight against inequality and debt) (Belgium, Greece, Ireland, Latvia, Spain), housing (Czech Republic, France, Spain), the social economy (France, Greece, Poland) and paying particular attention to children and education (Greece, Poland, United Kingdom).

With regard to local and regional administration, the majority of measures concern budgetary discipline at the sub-national level.

Country-specific Recommendations 2012

Finally, with regard to recommendations specifically addressed to member states (CSR) in respect of the European semester, the large majority concern social policy reform.

Specifically, the CSR call for reform of wage indexation in countries that have adopted such a system, aligning wages with individual or regional productivity, in some cases revising the system of collective bargaining, cutting tax on low wages, prolonging working life, adapting pension systems to the development of life expectancy, activating vulnerable groups (older workers, women, young people, in particular the children of immigrants, the disabled and so on) and to activate people suffering from social exclusion and poverty in the labour market.

Table 1 **Country-Specific Recommendations (CSR) 2012 (social field only)**

	ES	MT	SI	BE	PL	AT	BG	IT	LT	LU	SK	CY	CZ	DE	EE	FI	FR	LV	NL	UK	DK	HU	SE	PT	Total
Youth employment: transition from school to work (apprenticeships)	1	1	1		1			1	1	1	1				1		1	1		1	1				13
Pensions: explicit link between pensionable age and life expectancy	1	1	1	1	1	1			1	1	1	1				1			1						12
Pensions: reducing early retirement		1	1	1	1	1	1			1			1			1			1		1				11
Tax: shift away from labour, with focus on low income earners	1			1		1					1		1	1			1	1				1			9
Work participation: women in the labour markets (full time care facilities)		1			1	1		1			1		1	1						1		1			9
EPL: adjusting employment protection legislation (EPL) to address youth unemployment			1		1			1	1								1						1		6
Wages: reviewing wage-setting systems (alignment with productivity)		1	1	1				1															1		5
Wages: reviewing wage indexation		1		1						1		1													4
Vulnerable: better targeting social assistance							1		1						1			1							4
Youth employment: transition from school to work (incentivising companies)	1															1								1	3
Pensions: promoting active ageing and life-long learning	1		1																						2
Vulnerable: ensuring the adequacy and coverage of social protection systems												1			1										2
Child poverty: facilitating access to childcare services							1													1					2
Work participation: reducing tax disincentives for second earners														1					1						2
Vulnerable: access to quality social services							1																		1
Child poverty: making child support more effective	1																								1
Total	6	6	6	5	5	4	4	4	4	4	4	3	3	3	3	3	3	3	3	3	2	2	2	1	86

Source: ©Christophe Degryse, 2012

Table 1 thematically summarises the recommendations addressed to the member states in 2012,[39] which closes the proceedings of the European semester 2012. Each state must then report in 2013 on the reforms undertaken in order to respond to these recommendations.

As for 'non-social' recommendations, they mainly concern the correction of excessive public debts and deficits, enhancing competition in certain areas (services, energy, distribution and so on), the consolidation of the financial sector, efficient tax policies, improving the environment for SMEs and the promotion of research and development.

The strong influence of the European Commission is discernible in the contents of the first European semester, aimed at concentrating the attention of the member states essentially on two elements: fiscal consolidation and structural reforms. A third element is also present, but it is much more limited: (very) targeted investments. As for structural reforms, it must be said that they almost exclusively concern social matters: wages, labour productivity, activation of employment policies, pensions, education, training, vulnerable groups and so on. Certain objectives of the Europe 2020 strategy appear to be absent from this new procedure, in particular the fight against global warming.

In terms of political and strategic priorities the European semester thus appears at the very outset to have taken precedence over Europe 2020. In other words, budgetary discipline and structural reforms have taken precedence over the medium-term socio-economic strategy.

Having examined in detail the new procedure of the European semester put in place to enhance surveillance and discipline in the EU and, in particular, in the Eurozone, we shall now resume the chronology of 2011, which should allow us to assess the effectiveness of the new measures.

Chronology 3	**Political differences (winter 2011)**
10 January	The European Commission denies that negotiations have taken place at the European level concerning possible international financial aid for Portugal. The German press documents pressure put on the Portuguese government by Germany and France to ask for international financial aid, which Lisbon rejects.
12 January	The Commission declares itself in favour of increasing the sums allotted to the European Financial Stabilisation Facility (EFSF).
25 January	The first round of funding is carried out successfully by the EFSF (5 billion euros in bonds coming to maturity in 2016).

39. Not including member states under financial assistance because they are subject to different procedures.

27 January	An agreement is concluded between the Spanish government and the trade unions on pension reform. The retirement age is raised to 67 for those who have paid in for less than 38.5 years.
11 February	In Germany, President of the Bundesbank Axel Weber resigns. The reasons for his resignation are not made public, but among other things are likely to have to do with differences of opinion with other members of the Governing Council of the ECB on the subject of managing the Greek crisis.
12 February	The Greek government judges 'unreasonable' the attitude of the representatives of the Commission, the ECB and the IMF who demand a privatisation plan that is much more severe than expected involving 50 billion euros up to 2015.
25 February	In the parliamentary elections in Ireland Fianna Fail (centre-right) pays for its austerity policy. The coalition agreement between Fine Gael (centre-progressive) and the Labour Party provides for renegotiating with the EU and the IMF the conditions attached to international aid, which Ireland considers humiliating.
7 March	Moody's downgrades Greek sovereign debt by three notches, from Ba1 to B1.

2.3.3. Adoption of the Euro Plus Pact (11 March 2011)

After the EU has reinforced the Stability and Growth Pact, launched the European semester and prepared the creation of the European Stability Mechanism (ESM), at the beginning of 2011 the German government got ready to present its own version of the 'European economic government' that French President Nicolas Sarkozy was calling for. In the eyes of German Chancellor Angela Merkel this 'government' must take the form of a 'competitiveness pact'. In a way, this was to be the second price to be paid for solidarity: after discipline, the strengthening of competitiveness by means of closer cooperation.

According to the press, for Berlin this consolidation will take the form of an examination of member states' wage policies (and the question of automatic wage indexation), labour market flexibility, the retirement age, taxation (creation of a common corporate tax base or common corporation tax rates), the accelerated harmonisation of rules on the mutual recognition of qualifications, the introduction of schemes for solving the banking crisis and, of course, limiting public debt, all to be set in stone.

Thus Angela Merkel agreed with Nicolas Sarkozy to present a 'competitiveness pact' at the European Council meeting of 4 February 2011. For the French President, this pact would make it possible to 'show observers throughout the world that the European economies are moving in the direction of convergence in the interest of competitiveness'.[40]

However, this initiative aroused controversy among the European partners with regard to the Franco-German partnership concerning both form and

40. Bulletin, Agence Europe, 5 February 2011.

substance. As regards the form the criticisms were twofold. On one hand, the pact had only been discussed in the Franco-German diplomatic arena, with no European debate. On the other hand, it was clearly presented as an intergovernmental initiative in which the role of the Commission was reduced to its simplest, namely the evaluation of national performance: 'it is a matter of simple coordination of member states, intergovernmental cooperation without transfer of competences', the German Chancellor emphasised at the European Council. It was thus perceived as a strange way of building 'economic governance'.

As regards substance, many member states focused on the content of the Pact as presented in the press: for example, Belgium disagreed with the proposition to end the wage indexation system; Luxembourg shared Belgium's viewpoint and also sought a debate on the minimum wage and working time; Ireland was opposed to fiscal convergence; Austria did not want a link between rising life expectancy and a rise in the retirement age. However, the German Chancellor declared that the ideas that had appeared in the press were only examples. She proposed that the 17 Eurozone states discuss the specific objectives to be embodied in the Pact and that it could then be opened up to the signature of non-members of the Eurozone. The proposal was accepted in principle by the European Council.

In the weeks that followed the 'details' of the Pact were discussed, but in a gloomy political atmosphere: small countries exasperated with the Franco-German duo, conservative governments against left-wing governments (Spain, Greece, Portugal) and Eurozone states against non-Eurozone states that increasingly felt marginalised (Poland), adherents of a Community approach against supporters of the intergovernmental method and so on.

For its part, the European Trade Union Confederation opposed a Pact which, according to it, paved the way for a race to the bottom. It presented its analysis in a press release: 'The 'Competitiveness Pact' is basically about exporting the model of little scope for wage increases which the Euro Area's core has been following over the last decade, this time to the entire Euro Area. The Pact, with its strict unit labour cost comparison, will force member states to enter into a competitive downward spiral of undercutting each others' wages and working conditions. This risks pushing the economy further towards deflation and depression. Meanwhile, profits, bonuses and dividends are soaring including among many of those whose actions were at the origin of the crisis.' (ETUC 2011)

On 25 February the Presidents of the European Council, Herman Van Rompuy, and of the European Commission, José Manuel Barroso, submitted the draft of the Competitiveness Pact with a view to adoption at an informal summit of the heads of state and government of the Eurozone called for 11 March. Convergence and competitiveness were the key terms of the document, which talks about aligning wages with productivity, making work more attractive and ensuring the sustainability of public finances with regard to both public debt and pension and social security systems. The choice of specific policies to implement would remain the choice of each state. But the objectives would be based on performance indicators covering competitiveness, employment, public finances and financial stability.

On 11 March 2011 the heads of state and government of the Eurozone approved what came to be called the Pact for the Euro, which established increased coordination of economic policies. After the Eurogroup summit of 11 March this Pact was submitted to the European Council of 24–25 March to allow the member states outside the Eurozone to participate. In the end, 23 member states signed up: the EU27 minus the United Kingdom, Sweden, Hungary and the Czech Republic. These 23 countries ('Euro+') thus committed themselves to taking enhanced measures with regard to competitiveness, employment, the viability of the public finances and financial stability.

The general aim of the Pact was to reinforce the economic pillar of the monetary union. The 23 signatory states committed themselves, on one hand, to taking specific convergence measures with regard to the development of wage costs, opening up to competition and structural reforms (labour markets, retirement and so on) and, on the other hand, to coordinate tax policies. Four rules dominate the pact: it is in agreement with the model of economic governance that already exists in the EU and reinforces it, while adding value; it covers essential areas of priority action to promote competitiveness and convergence; it implies specific national commitments made each year by every state (see below), with policy follow-up by the heads of state and government on the basis of a report by the Commission; and it respects the single market and complies with the treaties.

The Pact has four objectives. First, to promote competitiveness: on one hand, by controlling the development of labour costs by re-examining wage determination mechanisms and monitoring public sector wage agreements; on the other hand, by reinforcing productivity by opening up protected sectors to competition, encouraging research and development and education, and improving the environment for companies. Second, promoting employment: first of all, through labour market reforms favouring more flexicurity, reducing undeclared work and increasing labour market participation; then through lifelong education and training; finally, through tax reforms (reduction in the tax burden on labour) to make working more financially attractive and by measures aimed at facilitating the labour market participation of people providing a second household income. Third, ensuring the viability of the public finances: on one hand, through the viability of pensions, health care and social benefits by adapting the pension system to the national demographic situation (adjusting the real retirement age to life expectancy, increasing the activity rate and so on) and by limiting early retirement schemes and incentivising the employment of older workers (especially those over 55 years of age); on the other hand, through national budgetary regulations transposing into national legislation the budgetary provisions of the Stability and Growth Pact. Fourth, reinforcing financial stability: first of all, by establishing national legislation on solving bank failures that fully respect the acquis communautaire; then by conducting strict stress tests on the banks (coordinated at the European level); finally, by monitoring the levels of private debt of banks, households and non-financial enterprises.

Furthermore, the Pact aims at 'pragmatic' coordination of tax policies through structured discussions on tax policy issues for exchanging best practices, the prevention of harmful practices and the fight against fraud and tax evasion. The member states would also be able to establish a common tax base for corporation tax.

These commitments must be transposed into concrete action by the member states that will be reflected in their National Reform Programmes (NRP) and their stability programmes.

What the EU calls an 'exhaustive response' to the euro crisis is thus almost completed: rescue plans, reinforcement of fiscal discipline and macroeconomic surveillance (Six Pack and the European semester), Euro Plus Pact for economic policy convergence and finally preparation for the setting up of the European Stability Mechanism (see below). But that is not enough to halt the euro crisis. Its next target was Portugal.

Chronology 4 **New expansion of the crisis**

16 March	The German government plans to reduce the public deficit to 0.5 per cent of GDP by 2015.
16 March	Moody's downgrades Portugal's debt by two notches to A3.
17 March	The European Commission raises 4.6 billion euros to come to the assistance of Ireland via the European Financial Stability Mechanism (3.4 billion euros) and helps Romania via the Balance of Payments facility (1.2 billion euros).
21 March	According to President Jean-Claude Trichet the ECB does not favour euro bonds.
23 March	In Portugal, the centre-right parliamentary opposition rejects the austerity plan of José Socrates' socialist government. The Prime Minister is forced to resign.
23 March	In the United Kingdom finance minister (Chancellor of the Exchequer) George Osborne presents an austerity budget that envisages 21 billion pounds' worth of public spending cuts to reduce the public deficit from 9.9 per cent of GDP in 2011 to 7.9 per cent in 2012.
24–25 March	At the European Council Euro-group president Jean-Claude Trichet confirms that the EU is ready to intervene to help Portugal; outgoing Prime Minister Socrates declares that the country has no need of a rescue plan.
29 March	In the United Kingdom, according to the Office for National Statistics, for the first time in 30 years the population has seen its purchasing power fall (by 0.8 per cent in 2010).
31 March	Ireland's Central Bank announces that four Irish banks will need an additional 24 billion euros on top of the 46 billion euros already injected into the Irish banking system. In total the rescue of the Irish banking sector amounts to 70 billion euros or half Ireland's GDP.
5 April	After Standard and Poor's and Fitch, Moody's downgrades Portuguese debt once again.

2.3.4. Portuguese rescue plan

The EU's 'exhaustive response' to the crisis did not prevent it from expanding. In Portugal, it first of all took the form of a political crisis. The austerity measures presented by José Socrates's socialist government were systematically rejected by the centre-right opposition. On 23 March the government was forced to resign.

After declaring at the European Council of 24 and 25 March 2011 that his country did not need a rescue plan the outgoing Portuguese prime minister formally asked for European financial aid on 6 April. The problem was that the Portuguese banks did not have the resources to fund the state and that the rates that Portugal had to pay on the markets continued to increase.

In accordance with a scenario that was beginning to be familiar the Ecofin council acknowledged the Portuguese request on 8 April and asked the Commission, in cooperation with the ECB and the IMF, to negotiate an economic adjustment programme with Lisbon. The EU declared itself ready to mobilise up to 80 billion euros in exchange for austerity and privatisation plans.

Thus on 3 May the Troika reached an agreement with the outgoing government on a rescue plan worth 78 billion euros. In exchange, Lisbon committed itself to a deficit reduction programme mainly based on freezing public workers' wages, tax rises and a privatisation programme. This austerity plan was to be implemented by the new centre-right (PSD) government that was elected in June, the same centre-right that had brought about the fall of the Socrates government with its rejection of his austerity measures.

Chronology 5	**Demonstrations, days of action and the emergence of the 'indignants'**
15 April	After their evaluation mission the Troika (Commission, ECB and IMF) declares itself satisfied with the implementation of Ireland's economic adjustment programme, which opens the way to the payment of a tranche of aid worth 4.5 billion euros (out of a total of 67.5 billion euros).
15 April	Moody's downgrades Irish debt by two notches (from Baa1 to Baa3).
15 April	Greece presents a new austerity plan to save 26 billion euros by 2015. According to the president of the Euro-group, Jean-Claude Juncker, the rumours of a restructuring of Greek debt are totally unfounded.
16–17 April	The parliamentary elections in Finland give a major boost to the parties opposed to the rescue of Eurozone countries (the 'True Finns' party won 19 per cent of the votes).
9 May	Although a second rescue plan for Greece is increasingly on the cards Standard and Poor's again downgrades Greek sovereign debt, from BB– to B.
11 May	Political parties in Finland – without the 'True Finns' – approve the 'short-term' rescue plan for Portugal.
16 May	The Euro-group approves the Portuguese rescue plan and the austerity plan that Portugal is to implement.

18 May	A new tranche of aid worth 3 billion euros is disbursed to Ireland thanks to its good implementation of the economic adjustment programme.
22 May	In many cities and towns in Spain the 'Indignants' set up camps to denounce a failed system.
23 May	Under pressure from its creditors the Greek government announces further austerity measures in the amount of 6 billion euros with a view to obtaining a new tranche of aid.
23 May	Fitch downgrades Belgian debt from 'stable' to 'negative'.
24 May	The European Commission issues 4.75 billion euros of AAA-rated bonds to support Ireland and Portugal under the European Financial Stabilisation Mechanism.
5 June	At the Portuguese parliamentary elections José Socrates's socialist party suffers a heavy defeat. The Social Democratic Party (centre-left) is the winner and announces that it will implement the austerity plan.
6 June	Viktor Orbán's Hungarian government announces a series of measures to protect households against overindebtedness, often caused by Western banks (action on repossessions in the case of insolvency, exchange rates below the market level), the fixing of the minimum wage by the government and compelling those who had taken early retirement to go back to work.
9 June	A new tranche of aid worth 200 million euros for Latvia is unfrozen in exchange for the positive implementation of the economic adjustment programme.
10 June	In Germany the Bundestag declares itself ready to accept a second Greek rescue plan, but on condition – controversially – that private creditors pay part of the costs.
15 June	The Greek Prime Minister socialist Georgios Papandreou is unable to win the support of the opposition for the austerity plan. Athens is rocked by violent demonstrations.
16 June	In the Czech Republic there is significant popular mobilisation against the government's reform plans.
17 June	The Greek Prime Minister reshuffles his government to make it a smaller and closer knit team.
19 June	Against expectations the Eurozone finance ministers decide to postpone until July the fifth aid tranche of 12 billion euros for Greece. The IMF and the EU first want the Parliament to adopt further austerity measures.
19 June	More than 200,000 'indignants' demonstrate in Spain for real democracy.
21 June	The ETUC organises a European and national day of action and information to reinforce the European social model.
23–24 June	The European Council commits itself to rescuing Greece and the euro: it appoints Italian Mario Draghi as head of the ECB, replacing Frenchman Jean-Claude Trichet, whose term of office had expired.
24 June	The Greek government reaches agreement with the Troika on a new 'medium-term plan' that provides for a further 28 billion euros in cuts by 2015 and 50 billion from privatisation.
29 June	The Greek Parliament adopts the austerity strategy 2011–2015 presented by Georgios Papandreou's government.
30 June	A public sector strike is held in the United Kingdom against pension reform.
30 June	The Italian Minister of the Economy presents an austerity plan worth 43 billion euros to achieve a balanced budget by 2014.
2 July	The IMF and the Eurozone finance ministers unfreeze the fifth tranche of 12 billion euros provided for in the current Greek aid plan.
6 July	Moody's downgrades Portuguese sovereign debt. The European Commission strongly criticises this decision.

2.3.5. Treaty establishing the European Stability Mechanism (11 July 2011)

The establishment of the European Financial Stability Mechanism in May 2010 was initially envisaged for a limited period of six months (renewable). At the end of this period the Commission was supposed to re-examine whether the exceptional circumstances that had justified this implementation were still in place. But in fact Europe was only at the beginning of the unprecedented euro crisis that marked the years 2010 and 2011.

At its meeting on 28 and 29 October 2010 the European Council, more and more conscious of the risks of the Greek crisis spreading, considered it necessary to put in place a permanent crisis mechanism. This decision, at the behest of Germany and France,[41] revived a number of debates – 'unanimity was not achieved', Jean-Claude Juncker declared at the Council – especially on the subject of the form such a mechanism would take (intergovernmental or Community; involving private creditors or not, on a voluntary basis or not) and on the subject of the reform of the Lisbon Treaty that this decision would require, although the no bailout clause would not be modified. Officially, it is not a matter of authorising the rescue of a member state, but rather of the Eurozone.

The agreement on revising the Lisbon Treaty was reached at the European Council of 16 and 17 December 2010. According to this agreement Article 136 of the Treaty was to be amended in 2011 to authorise 'the member states of the Eurozone to create a stability mechanism if that proved indispensible to guarantee the stability of the euro as a whole'. In principle, this European Stability Mechanism (ESM) was to be established in July 2013 replacing the European Financial Stabilisation Facility (EFSF). Given the urgency it was finally decided to bring forward the deadline to July 2012 (but this new deadline was itself postponed).

At an enlarged meeting of the Euro-group on 14 February 2011 the EU ministers of finance reached agreement in principle to endow the ESM with 500 billion euros. On 21 March they reached agreement on the operations of the ESM. On 23 March the European Parliament approved modification of the Treaty. On 20 June the finance ministers reached a final agreement on the legal texts and on 11 July the treaty establishing the European Stability Mechanism was signed by the 17 heads of state and government of the Eurozone. The national ratification processes then commenced.

But once more this decision brought scarcely any respite to the Eurozone, which experienced its worst month in August.

41. Especially by Germany for reasons of legal certainty; the government feared that under the current treaty the creation of such a permanent mechanism would be rejected by the Constitutional Court.

Chronology 6 **Stock market meltdown and recapitalisation of European banks**

12 July	Italian prime minister Silvio Berlusconi calls for national unity; the Italian Senate debates an austerity plan in the amount of 48 billion euros.
14 July	The second Troika mission in Ireland, satisfied with implementation of the austerity programme, opens the way to the disbursement of a tranche of aid worth 4 billion euros.
21 July	While market tensions are at their height a Eurozone summit is convened. Agreement is reached on a second aid plan for Greece amounting to 110 billion euros and an expansion of the EFSF. 'Voluntary' private sector participation is enacted – in the estimated amount of 40 billion euros – which is considered by the rating agencies to be partial default.
25 July	Moody's downgrades Greek sovereign debt by two notches due to payment default (Ca).
27 July	Moody's downgrades Cypriot sovereign debt (from A2 to Baa1).
29 July	Spanish Prime Minister José Luis Zapatero announces early elections for 20 November.
4 August	Tensions concerning Italy and Spain reach their height; the ECB resumes buying these countries' bonds on the markets.
4 August	The President of the European Commission asks the Eurozone heads of state and government to review the capacities of the EFSF. The decisions taken on 21 July are already superseded.
4 August	World stock exchanges fall in Asia, Europe and the United States.
5 August	The presidents of the ECB and the Bank of Italy send a secret letter to the Italian government which calls on it to come up with a new austerity plan and privatisation on a grand scale.
5 August	The President of Cyprus forms a new government.
6 August	Standard and Poor's downgrades US debt.
12 August	After its 48 billion euro austerity plan adopted in July the Italian government reaches agreement on a second austerity plan in the amount of 45.5 billion euros, which in particular provides for a tax on high incomes.
16 August	At a Franco-German summit the German Chancellor and the French President announce that they would like to establish a European economic government in the form of 'euro summits', the first president of which would be the president of the European Council, Herman Van Rompuy. They call on the Eurozone member states to inscribe the principle of budgetary balance (the golden rule) in their constitutions. Finally, they insist on the implementation of a tax on financial transactions and a single corporation tax rate.
19 August	The Spanish government announces new measures to cut the public deficit in the amount of 5 billion euros.
22 August	The declaration that Finland has obtained a financial guarantee from Greece in exchange for its contribution embarrasses European governments. Other countries could demand such a guarantee.
24 August	The French government announces an austerity plan which, in particular, provides for 11 billion euros more in tax.
24 August	German head of state Christian Wulff criticises the policy of the ECB.
25 August	Cyprus's new finance minister, Kikis Kazamias, presents an austerity plan to Parliament.
29 August	The Italian Prime Minister decides to cancel the tax on high incomes provided for in the austerity plan of 12 August.
2 September	The Troika suspends its fifth mission to evaluate the economic and budgetary situation in Greece because it considers the country's budgetary efforts to be inadequate.
2 September	Spanish MPs vote in favour of inserting a 'golden rule' limiting public spending in the Spanish constitution.

8 September	The Dutch finance minister Jan Kees de Jager raises the possibility of Greece exiting the Eurozone.
9 September	Chief economist of the ECB Jürgen Stark resigns.
6–11 September	The Greek government announces new measures to speed up privatisation, restructure the public sector and introduce a real estate tax.
11 September	The German minister of the economy, the liberal Philipp Rösler, raises the scenario of an 'orderly default' on the part of Greece. This begins to gain ground and sends stock markets plummeting.
12 September	Black Monday for banking shares in France, Germany, Italy, Spain and, to a lesser extent, the United Kingdom.
15 September	The central banks of Switzerland, the United Kingdom, Japan, the United States and the ECB launch a concerted action to provide the European banks with unlimited liquidity.
15 September	The Spanish government announces the re-introduction of the wealth tax.
16 September	US Treasury Secretary Timothy Geithner participates in a meeting of the Eurogroup and calls on the Europeans to 'act in a decision fashion and to speak with one voice' in order to address the 'catastrophic risk' to the world economy of the euro crisis.
16 September	In the Danish parliamentary elections the left is victorious over the outgoing right.
19 September	Standard and Poor's downgrades Italian debt by one notch.
28 September	After Athens's announcement of new spending cuts the Troika resumes discussions with the government within the framework of a fifth examination of the implementation of its programme.
29 September	Germany's Bundestag approves an extra 440 billion euros for the European Financial Stabilisation Facility (EFSF).
29 September	In order to reduce its debt the Italian government kick-starts a major programme to dispose of public assets.
3 October	The Eurozone finance ministers report the disbursal of a new tranche of aid in the amount of 8 billion euros to Greece pending the launch of the privatisation programme.
3 October	Important figures on the European left – including Massimo D'Alema, former Prime Minister of Italy, Poul Nyrup Rasmussen, former Prime Minister of Denmark and President of theEuropean Socialist Party, Alfred Gusenbauer, former Austrian Chancellor and Paul Magnette, Belgian federal minister for climate and energy – call for a different economic policy in Europe; they initiate what could be a turning point in the management of the euro crisis.
6 October	The ECB decides – by consensus, not unanimously – to strengthen its non-convention based aid for refinancing the banking system.
6 October	In a letter to the presidents of the Commission and the European Council the prime ministers of the Netherlands, Sweden and Finland call for the EU to return to the road to growth while maintaining strict budgetary discipline by means of open markets, the single market, intelligent regulation, innovation, the structural funds and green and resource-efficient use of resources.
9 October	The downgrading of sovereign debt in banking portfolios undermines the European banking sector. The German Chancellor and the French President agree on a necessary recapitalisation of the banks (Dexia crisis); the second Greek rescue plan of 21 July is not enough and will have to be revised.
11 October	The Troika ends its fifth mission to evaluate the economic and budgetary situation in Greece, declaring that the recession is 'more acute than anticipated in June' and that the 2011 budgetary objectives will not be achieved, but it gives the green light to the disbursal of a new tranche of 8 billion euros.

11 October	The President of the European Systemic Risk Board, Jean-Claude Trichet, declares that the European banking sector needs recapitalisation (which the IMF had been asserting for months).
11 October	The Slovak Parliament rejects the reinforcement of the European Financial Stability Facility.
12 October	In the United Kingdom the Office for National Statistics announces that unemployment is at its highest level since 1994, with 2.57 million unemployed (8.1 per cent of the active population).
13 October	After the fall of the centre-right coalition government in Slovakia linked to the refusal to pass the reinforcement of the EFSF the social democrat opposition obtains assurance of new elections in March 2012 in exchange for its support for ratification of reinforcement of the EFSF. In a second vote the Slovak Parliament thus ratifies the extra 440 billion euros to boost the EFSF and flexibilisation of its competences (repurchasing of the sovereign debt of countries in difficulties, conditional loans to countries to recapitalise their banking sectors). This ratification renders the EFSF fully operational.
14 October	Standard and Poor's downgrades Spanish sovereign debt by a notch to AA–.
17 October	The Portuguese government presents a draft budget for 2012 centred on consolidating public finances by reducing expenditure (cuts of around 7.5 billion euros, including cuts of 2 billion euros in social benefits) and structural measures (prolonging working hours, abolition of the 13th and 14th month for public employees and pensioners whose monthly income exceeds 1,000 euros), as well as a rise in VAT to 23 per cent on some products. The Portuguese government would like to reduce the public deficit from 5.9 per cent in 2011 to 4.5 per cent in 2012.
20 October	After the Greek Parliament adopts austerity measures a demonstrator dies during the general strike and accompanying violent demonstrations.
23 October	There is a European Council and a meeting of the heads of state and government in Brussels to move things forward, in particular work on the recapitalisation of the banking sector and revision of the second Greek rescue plan, but without reaching agreement. In accordance with French and German demands, the European Council decides to appoint the Presidentof the European Council to preside over the meetings of the heads of state and government of the Eurozone.
26 October	The Italian prime minister presents a programme to reduce Italian debt and to restore growth. In particular, this provides for labour market reform (authorising layoffs for economic reasons), opening up the market much more to competition (shops, professions, public services), the modernisation of public administration, the insertion of a 'golden rule' in the Constitution, pension reform (progressive raising of the retirement age to 67 years by 2026), tax reform and privatisation of public assets.
26–27 October	At a new meeting of the European Council and a Eurozone summit the leaders of the Eurozone reach agreement on an 'exhaustive response' to the crisis: the EFSF will be increased from 440 billion euros to 1,000 billion, the main European banks will be recapitalised in the amount of 105 billion euros and private investors will 'voluntarily' accept a haircut of 50 per cent on the Greek debt that they hold.
31 October	Greek Prime Minister Georgios Papandreou announces a referendum on the European aid plan of 27 October. The EU and the IMF are appalled: the financial markets fall.
4 November	Georgios Papandreou obtains a vote of confidence in the Parliament.
6 November	Georgios Papandreou announces his resignation after reaching agreement with the leader of the right, Antonis Samaras, who voted against the austerity plans, to form a government of national unity before early parliamentary elections pencilled in for 19 February 2012.

8 November	Italian prime minister Silvio Berlusconi loses his absolute majority in the Chamber of Deputies.
9 November	Italian debt is targeted in the financial markets; interest rates on new Italian bonds exceed 7 per cent. The EU observation mission to Rome lets it be known that the measures promised in Berlusconi's programme are not enough and exhorts the government to immediately adopt supplementary measures.
10 November	Greek President Karolos Papoulias tasks Loukas Papadimos (former governor of the Bank of Greece and vice-president of the ECB) to form a national coalition government.
10 November	Due to a 'technical error' Standard and Poor's issues a warning that it will downgrade French debt.
11 November	The Portuguese Parliament approves draconian austerity measures to reduce the public deficit from 5.9 per cent of GDP in 2011 to 4.5 per cent in 2012.
12 November	Italian Prime Minister Silvio Berlusconi resigns.
12 November	Standard and Poor's downgrades Hungarian sovereign debt to BBB/A–3.
13 November	Mario Monti is tasked by the Italian President, Giorgio Napolitano, with forming a new government.
15 November	The Central Statistical Office announces that Dutch GDP has fallen by 0.3 per cent in the third trimester in comparison to the second. More austerity measures, adding to the 18 billion euros in cuts already decided, are considered.
18 November	Greece presents its draft budget 2012 developed under the tutelage of the Troika. It provides for a reduction in public spending of 5 per cent in comparison to 2011, an increase in tax revenues of 7 per cent and a return of the public deficit to 5.4 per cent of GDP (as against the 9 per cent anticipated in 2011).
20 November	In the Spanish parliamentary elections the right wing of Mariano Rajoy's Popular Party gains an important victory over José Luis Zapatero's socialists.
21 November	In Hungary, Viktor Orbán's government decides to call for formal financial assistance from the IMF and the European Commission.

2.3.6. November 2011: Adoption of the Six Pack and launch of the Two Pack

As we have seen, the Six Pack is aimed at strengthening the Stability and Growth Pact. After more than a year of discussions and negotiations it was formally adopted by the EU Council and the European Parliament in November 2011. It entered into force on 13 December 2011.

But given the development and expansion of the euro crisis it already seems incomplete. Starting with the twofold premise that 'manifest errors' in the drafting of national budgets must be detected as early as possible and that working out a common budgetary calendar for the Eurozone member states should allow better synchronisation in the preparation of these budgets the European Commission proposed on 23 November 2011 to add two new regulations – called the 'Two Pack' – to the Six Pack. At the time of writing (June 2012) these two regulations were still in the process of adoption and were aimed at further reinforcing control of national budgetary policies.

First of all, the idea is to complement the European semester with a 'common budgetary calendar' (European Commission 2011b); to complement the system of multilateral surveillance of budgetary policies in order to guarantee that the recommendations formulated by the EU in the fiscal domain are duly taken into account in the preparation of national budgets; and to complement the procedure for correcting excessive deficits with closer surveillance of the budgetary policies of member states subject to an excessive debt procedure in order to guarantee rapid and sustainable correction of excessive deficits. According to the main provisions of this Regulation the member states would be required once a year to make public – by 15 April at the latest – a medium term budgetary plan, at the same time as their stability programme. Drafts of budgetary plans for the following year would be submitted to the Commission and the Euro-group and made public every year (by 15 October at the latest). If the Commission declares that a draft budgetary plan contains a particularly serious breach with regard to the budgetary policy obligations laid down in the Stability and Growth Pact it would – publically – demand that the member state concerned revise the draft in the two weeks following its presentation.

The second Regulation (European Commission 2011c) is based on the premise that the intensity of economic and budgetary surveillance should be proportionate to the seriousness of the financial difficulties encountered by a member state – especially if it is a member of the Eurozone – and take account of the nature of the financial assistance provided: from simple support granted on a precautionary basis to a complete macroeconomic adjustment programme with strict economic policy conditions. Thus member states facing serious problems of financial stability or receiving budgetary assistance would be subject to intensified monitoring by the Commission and the ECB: increased surveillance, macroeconomic adjustment programme, evaluation missions in the country concerned, regular reports and so on.

Discussed and negotiated in the course of 2012 the Two Pack is becoming the place where the growing concern to promote European economic growth is beginning to express itself. Besides the discussions on the budgetary calendar – deadlines which a member state must meet in preparing its budget draft for the following year – the European Parliament is debating the question of budgetary solidarity via the creation of 'euro bonds' and a 'redemption fund' that would make it possible to temporarily mutualise the excessive debt of Eurozone countries (above 60 per cent of GDP). It is also discussing the introduction of a margin of interpretation in provisions concerning public deficit reduction in order to take into account their impact on growth and employment, as well as the implementation of an 'instrument for growth' that would make it possible to mobilise 1 per cent of GDP for a period of 10 years for investments in energy infrastructure and new technologies. To sum up, if budgetary discipline has not been called into question in these debates three new elements have been added: a relaxation of the rhythm of adjustment, instruments of budgetary solidarity and support for economic activities through investment. According to the advocates of these changes all this should help to develop a more balanced approach to the debt crisis.

Chronology 7 **'Maximum risk' of bank default (autumn 2011)**

23 November	In Greece, leader of the conservative party Antonis Samaras ends up supporting an agreement with the Troika on the second rescue plan.
24 November	Fitch downgrades Portuguese debt to the category of 'speculative'.
24 November	The Franco-German-Italian summit does not reach agreement on the creation of eurobonds.
25 November	Standard and Poor's downgrades Belgian debt. Ten days later the country establishes a federal government after 540 days of political crisis and promises a balanced budget by 2015.
30 November	Between one and two million British public sector workers demonstrate against the reforms and the austerity measures. Other demonstrations take place across Europe following the call issued by the European Federation of Public Sector Unions (EPSU).
4 December	The Italian government announces a new 20 billion euro austerity plan that provides for cuts in public spending, the re-introduction of a property tax, tax rises on luxury products, taxes on remittances from abroad by fraudsters and a progressive increase in higher VAT brackets. This plan, which also provides for 10 billion euros for economic recovery, is adopted by Parliament on 16 December.
5 December	The Irish government presents a new 3.8 billion euro austerity plan for 2012 which provides for an increase in VAT and a reduction in the health care and social benefit budgets.
7 December	Greece passes an extreme austerity budget for 2012: tax increases, wage cuts in the public sector and technical unemployment for tens of thousands of public sector workers.
8 December	The Cypriot government presents a budget that provides for a reduction of the public deficit by 2014: VAT is increased, public sector wages are frozen, job cuts in the public sector and tax rises.
9 December	At the European Council agreement is reached by 26 member states – without the United Kingdom – to toughen up common budgetary discipline.
16 December	The Commission and the IMF suspend their mission concerning financial aid to Hungary because of the Commission's worries about the intention of the Hungarian authorities to adopt laws that could undermine the independence of the central bank.
19 December	In Italy public sector workers go on strike against austerity and government plans to reform the Labour Code.
19 December	In a report on the financial stability of the Eurozone the ECB estimates that the risk of several banks defaulting has never been so great.
19 December	The new Spanish prime minister, Mariano Rajoy, announces a 16.5 billion euro austerity plan for 2012.
20 December	The Hungarian Parliament adopts an austerity budget for 2012.
22 December	Work stoppage by public sector workers in Belgium against the 11.3 billion euro austerity plan and the pension reform plan that provides for an increase in the early retirement age from 60 to 62.
30 December	In response to a public deficit that was higher than expected in 2011 the Spanish government announces new austerity measures in the amount of 8.9 billion euros in the public sector and new taxes amounting to 6.3 billion euros.
1 January 2012	The euro celebrates – albeit discretely – its tenth anniversary.

2.3.7. 30 January 2012: The Fiscal Compact

The treaty on stability, coordination and governance – or 'Fiscal Compact' – marks an additional stage in the strengthening of economic governance centred mainly on budgetary rigour, discipline and surveillance. Its origins are to be found in the meeting at the summit of 16 August 2011 between Angela Merkel and Nicolas Sarkozy.

At this summit the two leaders announced their intention to call on all the Eurozone states to insert the principle of a balanced budget – the 'golden rule' – in their national constitutions. They also wanted to instigate what they called a 'European economic government', essentially taking the form of 'euro summits' (the first president of which would be Herman Van Rompuy). With regard to policy coordination they insisted on the need to implement a single corporation tax, as well as a financial transaction tax.

Thus the main elements of the Fiscal Compact can be found in the conclusions of the Franco-German summit.

The resistance to this Franco-German axis was matched only by the intransigence of Germany in obtaining acceptance for the ensuing compromise. London and Warsaw increasingly feared a two-speed Europe: inside and outside the euro. David Cameron's government opposed any possible reform of the Lisbon Treaty to integrate elements of the Franco-German compromise.

The President of the European Council also tried to avoid opening up the Pandora's Box of a revision of the Treaty and proposed to do no more than amend the protocol on excessive deficits in order to insert the European golden rule. Another option would be to activate 'enhanced cooperation', already envisaged in the Lisbon Treaty, although that would mean – at least symbolically – a further division of the EU into those participating and those not participating.

Before the foreseeable difficulties of an agreement between the 27 member states to revise the Lisbon Treaty the Franco-German duo decided to force it through at the European Council of 9 December. In preparation for this Council they presented to Herman Van Rompuy a complete agreement to be adopted by the 17 Eurozone states before March 2012, without compromise.

Thus on 9 December the 17 heads of state and government of the Eurozone announced in a declaration their intention to adopt an intergovernmental agreement in the form of a Fiscal Compact. Nine other EU countries indicated that they might participate in this process. Only the United Kingdom refused. This new 'treaty on stability, coordination and governance' was approved on 30 January 2012 by 25 countries (the Czech Republic[42] ultimately refused to sign, too) and signed on 2 March 2012.

42. To justify its rejection of the Pact, Czech Prime Minister Petr Nečas raised three objections in the Czech press: the limited participation in the Eurozone summits, the fact that the project did not pay sufficient attention to the debt criterion and the fact that the ratification procedure is complex in the Czech Republic.

In the main, by signing this Pact a country commits itself to respecting 'through provisions of binding force and permanent character, preferably constitutional, or otherwise guaranteed to be fully respected and adhered to throughout the national budgetary processes' the 'golden rule' or the 'balanced budget rule', according to which the annual public budgets of these countries must be in balance or surplus, but they must henceforth not be in deficit except in exceptional circumstances.

The two other main novelties introduced by the Treaty on Stability, Coordination and Governance are a commitment to submit for discussion ex ante every important economic policy reform and the ratification of institutional innovations (establishment of euro summits and so on).

Stability can be expressed in terms of four points. First, a commitment to achieve a balanced or surplus budget. The limit of the structural deficit is fixed at 0.5 per cent of GDP, except in exceptional circumstances. If the public debt is below 60 per cent the deficit limit can be up to 1 per cent. If it deviates from it, an automatic correction mechanism is implemented. Second, public debt must be kept below 60 per cent of GDP. If this threshold is crossed the debt must be reduced at an average rate of one-twentieth per year. Third, in case of an excessive deficit, a budgetary and economic partnership programme (structural reforms) must be implemented, submitted to the Commission and the Council and supervised within the framework of the Stability and Growth Pact by the Commission and the Council. The Eurozone countries are committed to abiding by the recommendations of the Commission, unless reversed by a qualified majority. Fourth, if these rules are not transposed into national law – or are transposed badly – recourse to the EU Court of Justice is possible, which may result in financial sanctions.

Thus, coordination is ensured in two ways. On one hand, by a commitment to reinforce coordination of economic policies. Countries 'shall take the necessary actions and measures in all the domains which are essential to the good functioning of the euro area in pursuit of the objectives of fostering competitiveness, promoting employment, contributing further to the sustainability of public finances and reinforcing financial stability.' On the other hand, by a commitment by each country to submit for discussion ex ante every major economic policy reform it plans to implement.

Finally, governance consists of six points. First, the creation of 'euro summits' (informal meetings of Eurozone heads of state and government, the President of the European Commission and the President of the ECB) and the appointment of a president for the summits. Second, when necessary and at least twice a year a meeting will be held to discuss questions related to the responsibilities of Eurozone countries and the governance of the Eurozone. Third, participation by non-member states of the Eurozone that have signed the Fiscal Compact – in other words, with the exception of the United Kingdom and the Czech Republic. Fourth, the current Eurogroup will be tasked with the preparation and follow-up of summits. Fifth, the President of the European Parliament can speak at summits and will receive a report after each summit. Sixth, it is requested that a conference be held co-organised by the European Parliament and national parliamentary committees with a view to discussing budgetary policies and other questions covered by this Treaty.

The entry into force of this new treaty is envisaged for 1 January 2013 if 12 Eurozone countries have ratified it by this date. If not, it will be the first of the month following the twelfth ratification of the Eurozone. Five years after entry into force the Treaty will be re-evaluated to consider the question of its possible incorporation in the Lisbon Treaty.

This Fiscal Compact completes the establishment of the new European economic governance. To sum up, from 2010 to 2012 this included:

— aid plans concerning the balance of payments for Hungary, Latvia and Romania; rescue plans for Greece, Ireland and Portugal; and aid plans to recapitalise the banks in Spain and Cyprus;

— establishment of a European financial stabilisation mechanism and a European financial stability facility, then the creation of a European Stability Mechanism (ESM);

— reform of the Stability and Growth Pact via the Six Pack and the establishment of the European semester process for intensified budgetary and macroeconomic surveillance of the member states;

— adoption of a Euro Plus Pact to tighten fiscal discipline and reinforce the coordination of economic policy in the Eurozone;

— adoption of the Two Pack on the surveillance ex ante of budgetary and economic policies;

— adoption of the Treaty on Stability, Coordination and Governance and the insertion of the golden rule into national law.

Once again, the events of the first semester of 2012 show that these different initiatives are not enough to end the euro crisis. It is all as if, after two years and a half of preparation or improvisation the leaders of the European Union had put in place new pieces of a puzzle but without wanting to put them together in an overall plan. The multiplication of these initiatives led to a certain confusion and above all it seems that the heart of the problem has been carefully avoided: in the end, what level of political and economic integration are the Eurozone member states prepared to accept? In other words, what, ultimately, is the model of political union being constructed? And all this in a context of growing popular discontent in Greece, Spain, Portugal, Italy, Ireland and Romania, as well as elsewhere.

Chronology 8 **Second aid plan for Greece**

9 January 2012	The European Commission raises 3 billion euros in 30-year bonds rated AAA under the European Financial Stabilisation Mechanism for Ireland and Portugal.
13 January	Standard and Poor's downgrades the debt of nine Eurozone countries. Besides depriving France of its triple A status it downgrades Austria, Cyprus, Spain, Italy, Portugal, Malta, Slovakia and Slovenia.
20 January	The Italian government launches measures directed towards economic recovery in the form of liberalisation of several economic sectors.
24 January	The Ecofin Council issues a recommendation to Hungary that it take measures to deal with its public finances.
30 January	A general strike is held in Belgium against the government's austerity plan.
5 February	The Troika accepts that Ireland will henceforth devote part of the proceeds of privatisation to the creation of employment rather than to paying off the debt.
6 February	The Romanian Prime Minister announces the resignation of his government in the face of opposition by the 'indignants' who are protesting against the austerity plans.
6 February	German Chancellor Angela Merkel and French President Nicolas Sarkozy state that the sums collected in interest on the loans issued to Greece by the EU will be frozen in an account in order to guarantee the reimbursement of creditors.
9 February	The three principal members of the Greek government coalition under Loukas Papadimos agree on new austerity measures to be implemented in order to benefit from the second rescue plan in the amount of 130 billion euros. The next day, however, one of the parties, LAOS, goes back on its word.
10 February	The Spanish government presents a labour market reform plan aimed in particular at making redundancies easier and less costly.
10 February	In Greece, the four ministers of the extreme-right party in the government coalition tender their resignation in protest at the new austerity plan.
14 February	Moody's downgrades the debt of six Eurozone countries: Spain, Italy, Malta, Portugal, Slovakia and Slovenia.
15 February	The two remaining parties in the Greek government coalition – PASOK and New Democracy – agree in writing to implement the new austerity plan with a view to taking advantage of the second rescue plan, whatever the outcome of the upcoming parliamentary elections.
19 February	In Spain, more than 1 million people demonstrate against the new Labour Code.
21 February	The countries of the Eurozone finalise the second rescue plan to Greece, an unexpected agreement that provides for an envelope of 237 billion euros to avoid euro-exit.
23 February	The European Commission anticipates a 'mild recession' in the Eurozone in 2012 (–0.3 per cent) which relaunches the debate on austerity and growth.
24 February	ECB President Mario Draghi tells the Wall Street Journal that 'the European social model is dead'.
2 March	The Spanish government announces that its budgetary objective for 2012 will be a deficit of 5.8 per cent instead of the 4.4 per cent announced by the previous government.
5 March	The Commission demands that Spain pursue its initial objectives for 2012 and 2013; it threatens Madrid with sanctions in the event of non-compliance.
6 March	The Commission adopts a proposed recommendation demanding that Hungary take further budgetary measures.

9 March	The Greek government reaches a historic agreement with private creditors according to which banks, insurance providers and other funds agree to cancel half of the 206 billion euro debts of the countries concerned. A total of 83.7 per cent of the creditors agree to this, which enables Athens to avoid a disorderly default.
11 March	The Belgian government presents a new austerity plan to reduce government and social security spending, tax rises on tobacco, financial speculation and life insurance, strengthening of the fight against tax evasion and a reduction in the development cooperation budget.
14 March	Eurozone ministers formally approve the second rescue plan for Greece: 130 billion euros of public aid over three years, a reduction of 107 billion euros in Greek debt held by private creditors; the EFSF is authorised to disburse the first 39.4 billion euros, in several tranches.
21 March	The British government presents a budget for 2012–2013 intended to reduce the tax wedge for high earners and companies and to raise the tax threshold.
20–21 March	The Italian government agrees on a reform of the Labour Code with a view to relaxing the rules on redundancies; Italian MPs adopt an economic liberalisation plan.
22 March	General strike in Portugal against austerity, but called only by the CGTP.
29 March	General strike in Spain against labour market reforms.
30 March	The Spanish government presents its budget for 2012 which envisages cuts of 27 billion euros.
31 March	Half of Ireland's taxpayers boycott the new housing tax due on 31 March and imposed by the Troika within the framework of the aid plan.
3 April	According to the Troika Portugal is honouring its commitments and would like to return to the financial markets in September 2013 without a new aid plan.
4 April	A debt issue by Spain is partly unsuccessful; the interest rates demanded by the markets rise again.
9 April	In order to reassure the markets the Spanish government announces its intention to implement another 10 billion euros in cuts in the areas of health care and education and to reduce regional spending.
10 April	European stock markets fall; loan rates rise, especially in Spain and Italy. The spread between French and German loan rates widens to 1.35 points.
11 April	The Greek Prime Minister announces early parliamentary elections for 6 May.
13 April	A mission of experts from the European Commission goes to Madrid to examine Spain's accounts.
18 April	Because the recession is worse than expected the Italian government postpones the objective of returning to budgetary equilibrium from 2013 to 2015.
20 April	A four hour general strike is held in Italy to protest against the labour market reforms being discussed in Parliament, which envisage a relaxation of the rules on economic redundancies.
20 April	After relative calm at the beginning of the year, the situation in Spain and Italy makes the financial markets more and more feverish. More and more economists assert that excessive austerity in Europe is killing growth and will end up destroying the Eurozone (Paul Krugman, Joseph Stiglitz, Daniel Cohen, Patrick Artus, Heiner Flassbeck and so on). International organisations (OECD, IMF) begin to worry about excessively brutal consolidation.
21 April	The coalition government in the Netherlands loses its majority after the refusal of the Party for Freedom to support a budgetary consolidation plan in the amount of 14–18 billion euros.

25 April	The European Commission puts an end to its dispute with Hungary concerning the independence of the Hungarian central bank. It agrees to start talks on the financial assistance requested by the Hungarian government on 21 November 2011.
25 April	After a rebound in economic activity the UK Office for National Statistics announces a return of recession since the end of 2011.
26 April	The Troika opens the way to a new tranche of aid to Ireland worth 3.7 billion euros because of its exemplary implementation of its economic adjustment programme.
26 April	Standard and Poor's downgrades Spanish debt from A to BBB+.
26 April	An OECD report notes that in Greece wages have fallen by 22.5 per cent in comparison to 2011.
26 April	The minority government in the Netherlands (VVD and CDA, with the support of the opposition parties D66, the Greens and ChristenUnie, but without the extreme right PVV) manages to obtain approval of its 15 billion euro austerity plan. This plan provides for reform of the health care system, a reduction in subsidies for housing loans, a hike in VAT and an increase in the retirement age.
27 April	The Spanish Institute of Statistics announces an additional 366,000 unemployed in the first trimester of 2012. In total, 5.6 million people are unemployed in Spain, one-quarter of the active population. The question of an aid plan for Spain resurfaces.
27 April	The Romanian government (centre-right) falls because of the austerity policy imposed by the IMF and the EU.
30 April	The Portuguese government anticipates a recession amounting to 3 per cent of GDP.
30 April	In its report on global employment the ILO estimates that the downturn in the economic situation in the EU reflects the austerity trap.
30 April	The Italian government adopts a new plan to cut government spending by 4.2 billion euros.
2 May	According to Eurostat the unemployment rate in the Eurozone is 10.9 per cent, the highest level since the creation of the Monetary Union.
6 May	The French presidential elections are won by the Parti Socialiste candidate, François Hollande, who announces his intention to promote growth in Europe.
6 May	The results of the parliamentary election in Greece mean that it is impossible for the mainstream parties to form a majority. The conservatives of New Democracy receive only 18.85 per cent of the votes and PASOK (socialist) falls to 13.18 per cent. The big winners are the extreme left Syriza (16.78 per cent) and the extreme right Golden Dawn (6.97 per cent).

In the wake of the economists' debates, but also the initiation of major policy changes in certain member states – after, in particular, the presidential and parliamentary elections in France, the parliamentary elections in Greece and the regional elections in Italy, the United Kingdom and Germany – spring 2012 seemed opportune for a recalibration: after austerity the emphasis would be more on growth (investment) and solidarity (notably via euro-bonds). Will economic governance by austerity be complemented by an economic governance by recovery and solidarity? That was the whole debate that animated European capitals in spring 2012 and constituted the agenda of the European Council meeting of 28 and 29 June 2012 – a Council announced, once again, as a last resort.

As the crisis reached its climax this time it was the fate of the euro that was at stake. In spring 2012 the scenario of a Greek exit from the Eurozone (the so-called 'Grexit') seemed more tangible with every passing day. Rumours circulated of preparations for this 'Grexit' at the highest level (the Commission, the European Council and so on). The worsening of the crisis of the Spanish banking sector gave rise to concerns about a domino effect. Italy – which was reforming rapidly – continued to be punished by the financial markets. Cyprus's banking sector was undermined by the restructuring of Greek debt.

The Eurozone summit and the European Council of 28 and 29 June 2012 were held in a context of intensifying drama concerning the future of the Eurozone. The decisions taken there appear, for the first time since the beginning of the crisis, to explore other avenues than those inspired exclusively by austerity.

Chronology 9	**Help for Spain and Cyprus; Italy in the eye of the storm**
9 May 2012	Amidst a financial market storm the Spanish government nationalises Bankia, the country's fourth largest bank. The Spanish banking sector appears increasingly fragile.
14 May	The Spanish government adopts a reform of its banking sector: it demands from banking institutions supplementary provisions in the amount of 30 billion euros to cover potential future losses, the quarantining of toxic assets and the independent validation of accounts.
17 May	Faced with being unable to form a government, Greece avails itself of an interim government of experts. New parliamentary elections are called for 17 June. The political deadlock jeopardises the EU and IMF rescue plan. More and more people call for preparations for an exit from the euro.
17 May	Moody's downgrades sixteen Spanish banks, giving rise to a mood of panic among depositors.
18 May	The possibility of a return to the drachma creates a mood of panic among Greek depositors. Since the parliamentary elections billions of euros have been withdrawn from the banks.
18 May	The Spanish finance minister announces that the public deficit in 2011 was higher than had been declared to the Commission in March (from 8.51 per cent to 8.91 per cent). Spain's wish to honour its commitments with regard to the deficit (5.3 per cent of GDP in 2012) makes the situation more difficult than ever.
21 May	The Spanish government tasks two independent auditing firms with evaluating the banks' portfolios. 'Operation Truth' is aimed at assessing their capacity to withstand an 'adverse scenario'.
22 May	In a report the ILO estimates the number of young unemployed (15 to 24 years of age) in the world in 2012 at 75 million, an increase of almost 4 million since 2007. Significant increases have been observed in the European Union.
22 May	According to an OECD report, in 2012 the Eurozone will experience a mild recession (–0.1 per cent) and a very weak recovery in 2013 (+0.9 per cent). The unemployment rate will rise to 10.8 per cent in 2012 and 11.1 per cent in 2013.
23 May	At an informal European Council the new French president, François Hollande, seeks to relaunch the debate on growth, but also – with the strong support of Italy and Spain – on euro-bonds, which rekindles tensions with Germany and Chancellor Angela Merkel.

23 May	The EU heads of state and government reaffirm their wish that Greece remain in the Eurozone, on condition that it meets its commitments within the framework of its second rescue in March 2012.
25 May	The board of directors of Spain's fourth largest bank, Bankia, unveil a recapitalisation plan and ask the state for 19 billion euros in aid.
31 May	Fitch downgrades eight autonomous regions in Spain.
1 June	The Irish people in a referendum approve – 60 per cent for, 40 per cent against – the ratification of the Pact on stability, coordination and governance.
4 June	The governor of the Cypriot central bank lets it be known that the country could be forced to ask for European financial aid due to the costs arising for Cypriot banks from the restructuring of Greek debt.
6 June	The European Commission proposes a first step towards a European banking union, in other words, a set of European regulations for banking recovery and resolution.
9 June	The Eurozone finance ministers accept the principle of granting Spain financial aid in the amount of 100 billion euros to recapitalise its banks, without an austerity plan in exchange.
13 June	Moody's downgrades Spain's sovereign debt by 3 notches, from A3 to Baa3, in other words, to the 'speculative investment' or 'junk' category.
17 June	At the Greek parliamentary elections the conservative party New Democracy wins 29.7 per cent of the votes, ahead of the radical left Syriza (26.9 per cent).
20 June	A new Greek government is formed that backs austerity. Prime Minister Antonis Samaras (New Democracy) has the support of the socialists of PASOK and the moderate left (DIMAR). He seeks to obtain a relaxation of the conditions imposed on Greece within the framework of its financial rescue plan.
21 June	Based on a report by independent experts the Spanish authorities announce that the maximum financial needs of the Spanish banking sector will rise to 62 billion euros.
21 June	In order to meet the demands of the EU and the IMF the Hungarian government presents a new version of its law on the national central bank.
22 June	The heads of state or government of Germany, France, Italy and Spain meet at a summit in Rome to try to find a compromise on exiting the crisis in preparation for the European Council of 28 and 29 June. The results are minimal.
22 June	The procedure launched with regard to Hungary, aimed at freezing around 500 million euros from the Cohesion Fund, is suspended by the Ecofin Council because of measures taken by the Hungarian government to correct its excessive public deficit.
25 June	Cyprus becomes the fifth Eurozone member state to request financial assistance to meet its financing needs and to recapitalise its banks, weakened by the Greek crisis.
25 June	Spain officially requests European aid to recapitalise its banks.
25 June	Greek finance minister Vassilis Rapanos resigns for health reasons.
26 June	President of the European Council, the European Commission, the Euro-group and the ECB publish their joint report 'Towards a genuine economic and monetary union' as a basis for the discussion on reinforcing EMU on the agenda of the European Council of 28 and 29 June.
26 June	In Greece, the economist and former banker Yannis Stournaras is appointed finance minister.
28–29 June	The euro summit decides to establish a European 'banking union'.
28–29 June	The European Council adopts a 'Compact for growth and jobs'.

At the end of a night of particularly difficult negotiations the 17 Eurozone heads of state and government reached an unexpected agreement. They decided to establish a 'single supervisory mechanism … involving the ECB'.[43] The task at hand was to create a European banking supervision for all Eurozone banks, which could thus decide to recapitalise or restructure a national bank. The establishment of such a supervisory organ opens the way to giving the ESM the possibility to directly recapitalise banks itself, without going through governments. This possibility would 'rely on appropriate conditionality'.[44] The establishment of such a 'banking union' is aimed at breaking the vicious circle between bank debt and sovereign debt, a vicious circle which, one will recall, was owing in particular to the European demand in 2010 only to come to the aid of countries in difficulty via redeemable interest-bearing loans.

To this decision the European Council added the launch of a 'Compact for growth and jobs' before mobilising around 120 billion euros. Such a pact, desired by French President François Hollande and supported by a growing alliance – in particular Belgium, Spain and Italy – reflects the beginning of a change in attitude with regard to solutions to the crisis since 2010.

If these two big decisions are generally hailed by the press as a step in the right direction ('One small step for European mankind',[45] 'the path devised in Brussels is encouraging'[46]) many questions remained. What will be the precise extent of the new powers conferred on the ECB? Will the banking supervision concern only systemically important banks or also regional banks? Will the European supervisor be able to decide to recapitalise or restructure a bank against the wishes of a government? What will be the consequences of the fact that the banks of Europe's financial centre – the City (London) – will not be part of this European supervision? What will be the consequences of the fact that the rescue of a national banking sector will no longer be the responsibility of the national government but of the ESM? Will a mandate be necessary for the latter? And if yes, will it be conditional on a political agreement? What will be the conditionalities? Will it be necessary to modify the ESM treaty, which does not provide for direct injection of capital into the banks? Will the funds of the ESM – 500 billion euros – be enough?

Finally, this agreement neglects euro-bonds, which seem doomed to oblivion. On the eve of the European Council German Chancellor Angela Merkel had affirmed that there would be no euro-bonds in her lifetime, which, according to some observers, could restart the euro crisis.[47]

43. Declaration of the Euro Area Summit, Brussels, 29 June 2012.
44. Ibid.
45. *Financial Times*, 30 June–1 July 2012.
46. *Le Monde*, 1 July 2012.
47. Commentary by editorialist Wolfgang Münchau in the *Financial Times* of 1 July 2012 : 'If Ms Merkel is right and there are no eurozone bonds in her lifetime, the eurozone will not survive. Without eurozone bonds or a change in ECB policy, Italy's and Spain's debt – and eurozone membership – is not sustainable'.

2.3.8. After two years of chaos

What this second chapter shows is that to date, despite a multiplication of regulations, treaties and instruments of 'new governance', the European Union has not been able to curb the spiral of the euro crisis. It would certainly be easy, a posteriori, to question the short-term vision of the actors in this crisis. It needs to be recognised that the latter, over time, has taken on proportions that were inconceivable at its inception. Although EMU's gaps and faulty construction had been identified nothing could have been foreseen of where what at first was only a peripheral problem could lead the whole of the Eurozone.

In this storm the dynamic of the actors appears to be extremely complex and sometimes to evade rationality altogether. Whether it is the attitude of the financial markets, the rating agencies, the banking sector as such or of the European institutions, the Commission, the ECB, the IMF but also of governments acting alone or painstakingly working out unsatisfactory compromises in the European Council the multiplication of the parties to this crisis, their sometimes incoherent attitudes, not to mention the numerous dramatic turns of events that punctuated this period – resignations, falls of governments, unexpected announcements of referendums or early elections, revelations of secret letters, challenging of agreements reached, reports of urgent decisions, demonstrations, riots, strikes and so on – all this has contributed to make the crisis more and more incomprehensible.

This storm – or this impression of chaos – has also shown that numerous historic compromises or concessions worked out in the European Union were transformed in the course of the crisis into real structural weaknesses. As seen in the first part of this text, these compromises included, for example, the unfinished nature of EMU or the refusal to commit to closer political integration. To this one might add especially the fact that the member states are differently involved in EMU, with the Eurozone members, the countries that obtained an opt-out[48] (United Kingdom, Denmark) and non-member countries but invited to participate and wanting to or not (Sweden). This indicates that the different elements of the new governance largely overlap – Stability and Growth Pact, Euro Plus Pact, Fiscal Compact, banking union and so on – but without being articulated in an overall project because the levels of constraint and commitment – not to mention ambition – are not the same, according to the position of the states. Taking the most recent example, the announcement of the commencement of enhanced cooperation to establish a financial transaction tax because certain EU member states reject it for reasons of short-term national interest. There is no doubt that this other indecipherability – that of the European political project itself – is an aggravating factor in the crisis.

48. That is, authorisation not to participate in EMU.

In the absence of such a project or clear general plan to which the member states adhere in an a spirit of commitment and mutual confidence all the stages of the management of the crisis have been centred on the lowest common denominator: austerity, discipline, surveillance and sanctions.

However, more and more observers – Nobel Prize winners Joseph Stiglitz and Paul Krugman, economists such as Daniel Cohen and Paul de Grauwe, specialist editorialists such as Martin Wolf – have been ringing alarm bells since 2010: generalised austerity, by euthanising European economic growth, only serves to exacerbate the sovereign and private debt crisis (see below).

Furthermore, this governance by austerity has resulted in an unprecedented extension of the surveillance powers of the EU over the member states, in particular those sharing the same currency. This extension of powers has had a considerable impact on national social models: henceforth, the EU shall oversee national policies on, in particular, the retirement age, limiting unemployment entitlements, reducing health care costs, wage formation systems, collective bargaining and so on. Not to progressively equalise these social policies, as the European treaties invite us to do,[49] but to make of them the main adjustment variables in the crisis, finally vindicating the observers cited at the beginning of the first part of this report without having brought into being a political union to complement the monetary one.

It is thus essential to consider the relevance of the economic analysis, the social impact of the remedies applied and the democratic question of this development of the EU. These questions are the object of the following chapter.

49. One of the objectives laid down in the treaties concerns 'improved living and working conditions, so as to make possible their harmonisation while the improvement is being maintained' (Article 151 TFEU).

3. The new governance in question

As we have seen in the first two parts of this analysis the choice made in 1992 in the Maastricht Treaty which brought the euro into being but without European ‘government’ has not been fundamentally called into question during the crisis of 2008 and thereafter. At the time of writing (June 2012) the EU has not changed paradigm but has continued and even accelerated along an old path which has not always proved itself. Only the meeting of the heads of state and government of 28 and 29 June 2012 might suggest that a change of model is in the offing.

In what follows we shall look at four questions which, in our view, remained open in the summer of 2012. They concern the relevance of economic analysis and of statements made during the crisis; the relevance of the remedies applied given these analyses of the situation; the social question, which seems to have become the main variable of adjustment in the euro crisis; and finally the question of democracy, which could quickly become the most crucial issue for the future of the euro.

3.1. Relevance of the diagnosis

From 2010 the incipient European ‘climatic Keynesianism’ of 2009 was extinguished. A new discourse emerged as self-evident: after having squandered their budgets the member states now had to tighten their belts. The austerity plans would be the price to be paid for years of budgetary negligence. Thus German Chancellor Angela Merkel was worried about the ‘extreme debt of certain countries, accumulated over many years’.[50] Is this diagnosis correct?

If one looks at the development of the member states’ public finances before 2008 it is clear that they were being reduced throughout the 2000s (De Grauwe 2011). The member states basically kept to the convergence criteria of the Stability and Growth Pact. In 2007, the average budget deficit of the 27 member states was 0.9 per cent of GDP, substantially below the 3 per cent threshold. It was the financial crisis and its economic consequences that caused this level to rise above 6 per cent in 2009 and 2010.

50. Interview given jointly to six daily newspapers: *Le Monde*, *Süddeutsche Zeitung*, *The Guardian*, *La Stampa*, *El Pais* and *Gazeta Wyborcza*, 26 January 2012.

The same applies to public debts: from 1999 to 2007 the average public debt of the member states went from 65.7 per cent of GDP to 59 per cent, thus below the 60 per cent threshold in this case, too. From 2008 to 2010 the crisis pushed this up to 80.1 per cent.

From 2005 to 2007 Spain enjoyed a budgetary surplus. When it fell in 2008 it was because of the financial crisis and not a lack of virtue. Likewise, before the crisis Ireland had had a budget surplus since 1997. The only Irish deficit year during this period was 2002, with a very modest –0.4 per cent of GDP. But in 2010 it reached –32.4 per cent of GDP because of the bailout of the financial sector. Belgium reduced its public debt by 46 points in relation to GDP between 1995 (130 per cent of GDP) and 2007 (84 per cent), just before the crisis. Between 2000 and 2007 its budget deficits averaged –0.37 per cent of GDP.

With the exception of Greece – which is a special case – there has been no general drift that might have justified the constriction of budgetary rules and the imposition of forced austerity. The great upheaval has resulted from the bailout of the banking and financial industry and support for the real economy to avoid a great depression. As Martin Wolf emphasises, 'it is not budgetary indiscipline that was at the origin of this crisis. The indiscipline of the financial sector and, generally speaking, of the private sector, including lenders in the countries at the heart of the zone, played a much more important role' (Wolf 2011).

This being the case, it would have been reasonable to expect that these would be the aspects addressed in any attempt to diagnose the problem – framework and regulation of the financial industry and its role in the real economy – rather than focusing on the claim that the crisis was attributable to a catastrophic wayward drift of public finances. Now one can only be surprised, four years after the outbreak of the crisis, by the extreme slowness of the European measures on the regulation and governance of finance (rigorous control of the financial sector, financial transaction tax, resolute action against tax havens, fraud and tax evasion, separation of commercial and investment banking activities, partial debt pooling and so on) in comparison to the speed with which austerity plans have been imposed. The delaying tactics of the financial sector have been much more effective than social resistance to the austerity measures.

Furthermore, it should be emphasised here, even though it is not the object of the present study, that the financial crisis to a large extent stemmed from the increase in inequalities and downward pressure on wages and household incomes prior to 2008, deregulated finance replacing the loss of household purchasing power due to falling wages (non-adaptation of wages to the cost of living, precarisation of the labour market, wage austerity and so on).

3.2. Relevance of the remedies applied

According to Nobel Prize winning economist Paul Krugman (2010) the new European governance, being based on erroneous diagnoses, has resulted in bad remedies: 'punitive Europe' or 'austerity Europe'. As we have seen, the response of the European Union has mainly concerned the establishment of an arsenal of public finance supervision and sanction mechanisms in case thresholds are crossed. Recently, in the absence of budgetary solidarity between the member states and a federal budgetary actor the member states have been reduced to 'structural policies', regulations and budgetary discipline.

The justification offered for this choice is that it 'reassures the markets' so that they continue to finance states at low rates. Thus former ECB president Jean-Claude Trichet explains that these supervisory measures and austerity programmes are aimed at re-establishing market confidence in member states' budgetary policies. In this sense the establishment of a punitive Europe is mainly a response to the desire to offer guarantees to the financial markets and the rating agencies, which in turn can guarantee sustainable interest rates to the member states.

According to the Ecofin Council, the ECB and the European Commission the sequencing will be as follows: in order for Europe to get out of the financial crisis it has to re-establish the confidence of the financial markets by carrying out structural reforms with regard to wage formation and collective bargaining systems, pension and health care systems, as well as other social services. It is evident from the chronology that accompanies this study that this sequencing is far from valid. In this 'sequencing' the social is always presented as – and de facto becomes – the main adjustment variable in the management of the debt crisis (see below).

Nevertheless, the consensus is growing among economists and in the international organisations that the concerted application – and at an unprecedented pace – of austerity plans in Europe is having recessionary effects.[51] A fall in demand combined with wage moderation has an automatically negative effect on growth, at least in the short and medium terms.

The year 2012 was supposed to confirm the validity of the reasoning of the advocates of austerity in 2009–2010: the financial markets, reassured by the new instruments of European economic governance and the new culture of budgetary rigour, would regain trust in the Eurozone. In the first half of 2012 this virtuous circle did not manifest itself. The recessional effect of austerity plans, with unattainable deficit reduction objectives, in fact have exacerbated the debt crisis to a denominator effect – when GDP falls, debt automatically rises as a percentage of GDP – which has led certain member states to defer their objective of bringing the public accounts back into balance (Italy, Spain)

51. Six-month forecasts published by the OECD, 28 November 2011; IMF (2012).

and inspire a new distrust in the markets which, consequently, demand ever higher risk premiums which, in turn, increases states' financing costs.

It is increasingly becoming clear that the austerity path imposed from 2010 to 2012 by the Ecofin Council, the Commission and the ECB is a road to nowhere. At a seminar organised from 12 to 14 April 2012 in Berlin by the Institute for New Economic Thinking the discourse that has been dominant since 2010 was harshly called into question. According to press accounts OECD secretary general Angel Gurria declared that 'now most governments and international organisations are in agreement on one point: we will not restore confidence and growth solely by imposing austerity'. Nobel Prize winner Joseph Stiglitz emphasised that 'global instability is as much, if not more, the result of the behaviour of countries with a trade surplus than of countries with a trade deficit ... Whatever their reasons, the surplus countries impose costs on others and the persistence of these surpluses has unsustainable consequences'. Finally, for German Heiner Flassbeck, chief economist of UNCTAD, 'if you do not give the [euro countries] the means to run a surplus they cannot repay their debts. In the Monetary Union their only option is not to repay their debts or to leave the Monetary Union'. As for economist Paul Krugman, he declared in the *New York Times* on 15 April that 'European leaders are on course to cause the economic suicide of the entire continent'.[52]

According to a personal estimate based on accounts in the European press,[53] between 2010 and 2012 substantially more than 700 billion euros in public spending cuts were decided on in fifteen EU countries.[54] This enormous 'European austerity plan' largely affects various areas of social protection, public employment and public investment. The budget cuts are usually accompanied by tax rises, in particular VAT, and wage freezes.

3.3. The social question

The choice of austerity is in reality a choice by default. As we have seen, in the absence of political union, a federal budget and an instrument of economic convergence the ultimate adjustment variable available to the member states in the crisis – deprived, as they are, of the instruments of devaluation and public investment – is 'internal devaluation' (or expatriation of nationals – employment emigration). In other words, in the absence of competitive monetary devaluation one applies 'competitive wage devaluation', 'competitive deregulation of labour rights' and 'competitive pension and health care reforms'. The social domain has become the adjustment variable for managing the crisis, which allows the European central banker Mario Draghi to take the view that the European social model is dead.

52. Extracts published in *Le Monde*, 21 April 2012.
53. Mainly *Financial Times*, *Le Monde* and *Agence Europe*.
54. Austria, Belgium, Cyprus, Czech Republic, France, Germany, Greece, Hungary, Ireland, Italy, the Netherlands, Portugal, Romania, Spain, United Kingdom.

The future of this social model within the framework of austerity is thus bleak. In the process of multilateral surveillance a set of 'structural reforms' is being put in place aimed, on one hand, at accelerating the consolidation of public finances and, on the other, at reinforcing economic competitiveness. In principle, the EU does not have legal competences – or those it does have are very weak – to address questions concerning such issues as national wage indexation systems, collective negotiations and pensions.

Nevertheless, specifically, it requires of countries that have adopted a wage indexation system that they 'reform' it (it should be noted that the four countries with such a system have unemployment rates largely below the European average). The EU requires that wages be aligned with individual or regional productivity and, in some cases, that collective bargaining systems be revised. With regard to pensions it requires that working lives be prolonged and that pension systems be adapted to longer life expectancy. With regard to employment, it is a matter of 'activating' all groups that have a tendency to leave the labour market: older workers, women, young people – in particular those with immigrant parents –, the disabled and so on. With regard to poverty the bulk of the measures advocated concern employment activation and vocational training.

None of these demands or recommendations are to be ruled out a priori; in some cases, structural reforms might be necessary. But at least three imbalances are evident. First of all, there is not one word in the European documents concerning redistribution, taxation, reinforcement of solidarity mechanisms and social integration. Next, measures for boosting the economy almost all concern supply side policies, aimed at furnishing enterprises with the most favourable environment possible. Demand-side policies are not in evidence. Finally, 'turnkey' measures addressed to member states generally appear to be inspired more by ideological models than real shortcomings or failures. In this way the EU seems to be acting as if the crisis represents a window of opportunity for imposing its reforms.

Such is the case with regard to the demand that Belgium raise the legal retirement age – within the framework of the sustainability of public finances – when the country's main problem is the excessively high rate of early retirements. Furthermore, Belgium's social model has been widely criticised – Belgium has received in 2011 no fewer than nine recommendations in the social domain, making it one of the countries must under pressure from the EU, together with the Czech Republic, Malta and Spain – while traditional indicators show that it has withstood the crisis better than the majority of member states.[55] Some will be tempted to see this exercise not as an analysis

55. The socialist General Federation of Belgian Labour (FGTB) notes in its socio-economic barometer based on OECD and Eurostat data that in 1996–2007, before the financial crisis, the growth of real added value in the Belgian economy and employment growth were better than in Germany; also that with regard to social inequality in 2009 Belgium did better than Germany in terms of the Gini coefficient; that the risk of poverty among workers is lower in Belgium than in Germany, France and the Netherlands; and that the number of lowest paid workers is smaller than in Germany.

grounded on the facts, but as the reflection of a war between ideological models that does not take account of specific situations or problems.

'Social' policy thus sees itself transformed into a productive factor whose main mission is to reinforce the competitiveness of enterprises and the economy as a whole. Economic recovery itself, which seems to have returned to the agenda in 2012, is supposed to be rooted in structural reforms. As Richard Hyman (2011) (London School of Economics) writes, such a policy rather than protecting the vulnerable from the market is aimed increasingly at forcing them to adapt to the market. 'Hence it is entirely logical that, as noted above, DG ECFIN [Directorate General of the European Commission responsible for economic and financial affairs] should increasingly take charge of the formulation of social policy'. As Martin Höpner and Armin Schäfer (2010) have also underlined, the EU is increasingly playing a role in the commoditisation of social relations and not in protection against 'leaving everything to the market' or in the development of a common social dimension. This is ultimately what Bruno Palier (2011) highlights with regard to member states in the Bismarckian tradition: the social is to be adapted to make it compatible with the dominant economic and monetary paradigm.

On the other hand, where the treaties do confer real power on the EU – in this case, the promotion of social dialogue (Article 154 TFEU) – it acts in the opposite direction. National institutions of social dialogue are now being called into question in a number of member states, also under European pressure (Clauwaert and Schömann 2012), while European cross-sectoral and sectoral social dialogue is suffering difficulties (OSE 2011). Others have highlighted the fact that effective institutions of social dialogue help to reduce the impact of the crisis (Laulom *et al.* 2012).

Finally, it is worth mentioning that a number of fundamental social challenges have been left by the wayside by the new governance. For example, decent work and workers in poverty. The much vaunted German model is exemplary in this regard: according to the study by the University of Duisburg-Essen, 22 per cent of German wage earners earned less than 8.5 euros an hour in 2009 and 4 per cent (or 1.2 million people) less than 5 euros. According to the authors of the study the low wage sector developed in particular at the end of the 1990s and at the beginning of the 2000s with the so-called 'Hartz reforms' (Kalina and Weinkopf 2009). This largely explains the current competitiveness of the German model, but is it really one to be followed? Since competitiveness is relative, if all the countries in the Eurozone based their competitiveness on low wages this would cancel out Germany's advantage, thus setting in motion a race to the bottom that is not in line with '[improving] living and working conditions, so as to make possible their harmonisation while the improvement is being maintained' laid down in the treaties (Article 151 TFEU).

In this same context, what about the increasingly unequal distribution of the fruits of growth? What about taxation as an instrument of greater social justice in the current circumstances? A recent OECD report (2011) highlights the fact that even in traditionally 'egalitarian' countries such as Germany, Sweden or Finland, inequalities grew between 1985 and 2008. There can be no sustainable exit from the crisis without a reduction in inequalities (Wilkinson and Pickett 2010; Reich 2011).

3.4. The question of democracy

The last critical point with regard to the new governance concerns the questions it raises about democracy. Various authors have expressed many worries about this issue (de Witte 2011; Barbier 2011; Degryse and Pochet 2011).

According to Bruno de Witte, after the market failure of the banking and financial industry one might wonder about a potential 'democratic failure' within the framework of implementation of the new governance. And one might mention all the decisions taken to save the euro but without going through public deliberation and parliamentary discussion: the establishment of the European Stability Mechanism, the Euro Plus Pact, the self-proclamation of 'Eurozone summits', the insertion of the 'golden rule' in national constitutions, the Europeanisation of the procedure for adopting national budgets (ex ante), limiting the prerogatives of national parliaments and Franco-German steering at the level of heads of state and government with regard to the strengthening of economic governance (the famous 'Merkozy', which considerably reduced the ability of other government and social actors to exert influence). Also to be added to this list is the frenetic pace at which the Commission, the ECB and the IMF imposed reform programmes on member states on financial life-support or threatening to become so; and the secret injunctions sent by the ECB to Italy dictating economic and social measures to be taken urgently; and Germany's suggestion – admittedly denied – to organise a referendum on exit from the euro in Greece.

According to Philippe Pochet (ETUI),[56] another risk is to construct a two (or more)-speed Europe in which some member states will be able to utilise their national monitoring procedures – for example in Germany: the Bundestag, the Constitutional Court in Karlsruhe and so on – whereas other governments will be told by the European institutions – the Commission, the ECB – which measures to adopt in accordance with the principle that sovereignty ceases where insolvency begins.

Furthermore, according to the two regulatory principles adopted by the Commission to complement the Six Pack the Eurozone countries must henceforth present their budget drafts during the same period each year and authorise the Commission to analyse them and, if need be, to issue advice on them. Thus the Commission will be able to seek their revision if it takes the view that they fall seriously short of the policy obligations laid down in the Stability and Growth Pact. The second regulation will reinforce

56. P. Pochet, forthcoming.

the surveillance exercised on the member states benefiting from a financial assistance programme or which are under grave threat of financial instability. Accordingly, the Commission will be able to decide whether a member state in difficulties must be subject to enhanced supervision and the Council will be able to recommend that this member state request financial assistance. These measures, in particular the first proposal for a regulation, have been the object of heated debate in the member states. For some, such as Paul de Grauwe (2012), the fact that the Commission may be granted the right to interfere in national budgets poses a real problem with regard to democratic legitimacy: 'The problem here is that the European Commission does not bear the political costs of its decisions.' If such a power were to be conferred on the Commission it would have to take on political responsibility before an elected assembly, in this instance the European Parliament.

Finally, as Wolfgang Streeck (2011) underlines, there is a risk that in some countries, in any event, 'Citizens increasingly perceive their national governments, not as their agents, but as those of other states or of international organizations, such as the IMF or the European Union, that are immeasurably more insulated from electoral pressure than was the traditional nation-state. In countries like Greece and Ireland in particular, anything resembling democracy will be effectively suspended for many years as national governments of whatever political color, forced to behave responsibly as defined by international markets and organizations, will have to impose strict austerity on their societies, at the price of becoming increasingly unresponsive to their citizens.'

Such 'democracy under surveillance' is, some claim, a 'necessary evil' to get through the storm of the crisis. The problem is that the measures adopted or in the course of being adopted by the EU, far from being temporary emergency measures, are meant to be permanent and, as they say, set in stone. Thus it will be difficult to modify them in response to an important development in the economic or social context, political change in the member states or a change in the dominant paradigm. Thus the negotiation of a new treaty involving major constitutional changes – the insertion of the 'golden rule' in national constitutions or by means of binding and permanent provisions without democratic deliberation is certainly the most striking example. The ETUC (2012) is right to call – for the first time in its history – for opposition to a European treaty in the process of negotiations.

3.5. Some elements of an alternative approach

After two years' implementing the approach advocated by the EU to combat the crisis 2012 has not delivered the expected results but, on the contrary, has seen the recession heightened, the debt crisis exacerbated by the denominator effect, unemployment soaring (in particular among young people), political crises provoked in a number of countries, with the risk of rising extremism, and Greece pushed to the brink of Eurozone exit.

If one looks positively at the challenges facing the EU and its member states three things emerge: the strengthening of the Economic and Monetary Union launched at Maastricht in 1992; the reversal of current trends, increasingly strong, towards growth in inequalities, the hyperconcentration of wealth and economic and social disintegration (as much within member states as between them); and the transition towards a low carbon economy.[57] These three challenges are not isolated from one another, but intrinsically linked.

Thus the strengthening of the Economic and Monetary Union should involve the pooling – to some extent – of sovereign debt via the creation of European bonds, as well as by the taxation of financial transactions, which would make it possible to support coordinated investment in green infrastructure, renewable energy, research and development and upgrading industrial structures. Fiscal discipline would be maintained, but austerity plans that set unrealistic goals within untenable time periods would be replaced by reasonable multiannual programmes on the economic, social and democratic plane. The role of the ECB would be reinforced to make it the 'lender of last resort'. The capital of the European Investment Bank (EIB) would be increased to enable the progressive implementation of a common industrial policy.

The reversal of current tendencies to exacerbate inequalities must involve the diminution of tax competitiveness between member states through the harmonisation of corporate tax bases and then of tax rates. That must also involve each member state fixing minima below which wages may not be permitted to fall. Reducing social and developmental inequalities would make it possible to strengthen cohesion in the EU and the Eurozone, a cohesion which is currently being undermined by significant macroeconomic imbalances. Europe really needs to adopt a serious regulatory framework for the financial industry and voluntarily put an end to the fraud and tax evasion made possible by the scandal of tax havens.

According to Robert Kuttner (2012), there is a significant consensus on this alternative approach in both the academic community and among progressive political parties, trade union organisations and social movements. Certainly, some aspects of this consensus remain to be constructed or consolidated. Furthermore, the actors who are attempting to bring it about currently lack visionary and ambitious political supporters and a favourable balance of power.

As Joseph Stiglitz emphasises, European leaders have by default chosen economic and social competition rather than investment and solidarity, which they reject. But this choice risks the following: whereas when Economic and Monetary Union was launched at Maastricht in 1992 it was supposed to strengthen the European Union, twenty years later it could be one of the causes of its weakening.

57. A growth in inequalities which is not unrelated to the outbreak of the financial crisis and thus the euro crisis (cf. *supra*).

Conclusion

The observations that emerge from analysis of the euro crisis can be summed up as follows.

Since the origin of the Economic and Monetary Union – that is, since the Maastricht Treaty was signed in 1992 – the institutional and political architecture of the single currency has experienced structural problems. The lack of an enhanced political union among the member states participating in the euro has been only partially – and inadequately – compensated by the adoption of common rules of conduct and procedure intended to 'govern' the Eurozone (the Stability and Growth Pact among others). It was possible to camouflage these shortcomings in the coordination of budgetary policies, investment policies, fiscal policies and social policies, as well as with regard to economic convergence because of 'calm weather', characterised in particular by low interest rates and easy access to credit.

The financial crisis unleashed in 2008 brought to light these structural deficiencies (besides revealing the problems – also structural – with deregulation of the financial industry). The crisis spread to virtually the whole of Europe and, due to the effects of rescue plans and bank recapitalisations, it turned into a public debt crisis. Between October 2008 and October 2011 European governments gave around 4.5 trillion euros in state aid to their financial institutions, according to the Commission. This is the equivalent of 37 per cent of EU GDP.

While, for a brief period – end of 2008, beginning of 2009 – the EU and its member states declared that this crisis will be the occasion for both 're-regulating capitalism' and to prepare the economy for the green transition using public investments, under the impact of growing public debts and deficits, as well as the outbreak of the Greek crisis at the end of 2009, the discourse of European leaders faltered rapidly and refocused on the absolute necessity for 'budgetary consolidation' within time frames and at a pace that would prove to be totally unsustainable. Most member states adopted austerity plans which, in addition, amounted to hundreds of billions of euros.

By a strange reversal of perspective the various solidarity mechanisms and social policy instruments have been pilloried: pension, health care and unemployment systems have been accused of being responsible for the crisis, alongside wage formation and collective bargaining systems. As Wolfgang Streeck (2012) has observed, one is witnessing 'standard neoliberal supply-side policy, designed to reassure prospective investors'.

After three years of such remedies the euro crisis has only grown: economic recession has been prolonged, public debt continues to grow in the relevant countries, the vulnerability of European banks goes on – although concealed by the stress tests that convinced no one – enterprises are closing and unemployment is exploding. Furthermore, far from converging, the economies of Eurozone members are caught in a process of divergence. The growing heterogeneity of the Eurozone is in turn exacerbating the doubts of the financial markets concerning the sustainability of all this.

Certainly, the EU has tried, step by step, to apply structural remedies to the crisis, but unsuccessfully to date: reinforcement of the Stability and Growth Pact, creation of a European Stability Mechanism, better coordination of economic policies through the Euro Plus Pact and a constitutional commitment to respect budgetary balance, not to mention the rescue plans amounting to more than 600 billion euros in the form of loans to Greece, Ireland, Portugal, Spain and Cyprus, support for the balance of payments in Hungary, Romania and Latvia to the tune of more than 50 billion euros, the ECB's injection of more than 1,000 billion euros in the European banking system and the provision of liquidity at fixed rates and in an unlimited amount up to January 2013. This latter action by the ECB has bought some time. But time in which to do what?

The only way out of the crisis, in mid-2012, seemed to be to reinforce political union between the Eurozone member states: what some call a 'federal leap', which would consist of establishing instruments of responsibility (advocated by the German government) and of solidarity (advocated by the French government) between all the countries of the Eurozone. But this requires a significant amount of courage and political vision. Does the decision taken at the Eurozone summit of 28 and 29 June 2012 to establish a 'European banking union' constitute a first step towards the political union indispensible to the single currency? Is there an alternative?

Long and patient reconstruction work is required to restore confidence to nations and citizens in the European project that should belong to them, a confidence that has been eroded – and that is putting it mildly – over the past three years and without which this project is doomed to failure.

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