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# EDITORIAL

by Stefano Bertozzi

Views from the North and the South on the challenge posed to the EU by the untested resilience of the euro in weathering the world financial crisis and on the need for Europe to have a crisis prevention "toolbox" for the future; the potential consequences of the social dimension of the EU internal market; and, lastly, how globalisation has brought to the surface the need for new political impetus to make Europe's Single Market more efficient and socially responsible – these are the four main issues covered in April's BEPA Monthly.

The first lead article by Fernando Navarrete Rojas, of FAES, is highly topical and looks at how the current economic crisis has revealed the weak spots of monetary union and undermined its very foundations. Lessons can therefore be drawn from this article, including the need for strong political support from Europe's leaders and institutions, a consistent and fiscally sound macroeconomic strategy and a more robust and rules-based framework across Europe.

The second lead article by Daniela Schwarzer, of SWP, while praising the virtues of the euro in coping with the current economic crisis, stresses that Europe needs to have a sound crisis management toolbox and to improve surveillance of macroeconomic imbalances. Ms Schwarzer also favours moving towards closer market integration and, in the long run, creating automatic stabilisers to minimise the adverse and uneven effects brought about by asymmetric shocks. Looking at the prospects of reform, she argues that the current political conditions are not conducive to far-reaching reforms. The EMU governance discussion needs to be reframed and to introduce more European thinking into domestic policy debate.

The third lead article is by Jacques Pelkmans and provides useful insights into how to assess the meaning of the social dimension of the Single Market today. While acknowledging that the EU has limited powers on social matters, he argues that there is scope for political manoeuvre to give social dimension a more prominent place in a new internal market initiative. This objective could be attained, for example, by improving coordination of national employment strategies, especially within the context of EU2020.

The fourth lead article by Paola Rossi gives a detailed account of the workshop organised by BEPA and Bruegel before the Easter break on the new strategy for the Single Market. Although this event confirmed that there are no ready-made recipes for revamping the Single Market, participants made it clear that the Single Market needs to generate new political momentum and to foster closer market integration while at the same time encompassing new areas.

## 1 The restoration of fiscal discipline. A view from Southern Europe or a vision for Europe?

By Fernando Navarrete Rojas*

After the abundance of cheap money and credit during boom times, the hard crash with reality has finally arrived and the myths of the past are tumbling down. The myth that stated that the public sector could replace the private sector without major consequences has come to an end with the eruption of severe fiscal and sovereign debt crisis that pose a risk to the whole economy. Pain for the past excesses will not and cannot be avoided. We can only partially select the timing and who will bear the costs. And in any of these transfers of costs and responsibility we can only add to the total amount of cost to be assumed specially due to the long-term consequences of a loss of incentives and discipline.

The euro has brought about a much deeper level of interdependence among the different European economies than was thought possible back in the 1990s when its design was discussed. Therefore, problems in the public accounts of specific European countries are not only, or even mainly, a problem involving their respective citizens and political leaders anymore, but a problem for banks, taxpayers and their corresponding political leaders elsewhere. Also interdependence works in the other direction and problems in the financial systems in some core countries do pose a problem for others. This is the current setting and it is good to have it like this. Political decision making has to adapt to all this through an explicit rules based system. That is a major task ahead that in the latest EU leaders' summit was only briefly pointed out.

The European project is indeed in a quandary that will shape its future for the next decades to come. The main issue that will ultimately shape the economy, policies, and power balances in the future Europe is the response to the fiscal crisis that is taking place in several of the euro area countries.

It is important to understand that what should really concern European leaders regarding the fiscal crisis is not what finally happens with Greece, – as important as it is especially for the Greek people – but what could happen to other countries that do pose a real systemic risk for the euro area. In this regard, the mechanism devised to alleviate the Greek debt crisis is of outmost importance, as it will enable us to see which incentives and political and economic restrictions other struggling countries will have to face in order to cope with a fiscal crisis that cannot be denied anymore. Short-term pain savings may not be worth the long-term consequences of putting again in place bad incentives against fiscal discipline for the second time in the short history of the euro.

The original (design) structure of the euro, as set out in the Treaty of Maastricht, has proved unable to respond to these challenges. The entire institutional architecture was based upon fiscal rules (the Stability and Growth Pact) precisely designed to avoid situations we are in today. This was a Pact that was originally intended to preserve a euro that exported the monetary and fiscal stability of the leading countries to all members of the club. This was indeed the strength and the raison d'être of the euro: a single and stable currency, not just a common currency. That was the deal and the aim many countries fought hard to achieve and that final objective should not be opportunistically changed.

The real history of the euro proves how wrong it is the idea that postulates that there is a group of countries best suited 'genetically' for responsibility and stability, and another group – basically Mediterranean countries – with worse behavioural attitudes to stability. Following this myth some argue this second group should not be invited to join in and if so, tight discipline should be imposed on them at whatever cost. Working solutions should be based on realities and not on baseless myths. We must bear in mind that, after the bursting of the dot.com bubble, economic problems spread all across Europe. The crisis and unemployment spread across those countries more reluctant to reform their economies. Certainly, different governments were in office in those days. It was not precisely Mediterranean countries who first breached and

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then fought fierce to change the rules mid-game, thus demonstrating their power within the EU, because the rules were not convenient in the short term. The political message that was sent out to all countries of the euro was crystal clear. The seed of fiscal irresponsibility had been sown, and once grown it had backfired against everyone.

The result is that we have reached the point we were seeking to avoid, and now the response to a situation that has been deliberately ignored is somewhat improvised. Fortunately early draft plans that ruled out IMF intervention were dismissed. Now the challenge is to realise that the damage to the Greek economy was made earlier and there is little that can be done apart from the tough fiscal decisions that should be taken by Greek national authorities and from following standard procedure for public debt laden countries, i.e. providing liquidity support based on strict conditionality monitored by a third party.

To many observers it might surprise how much has been written recently on the amount of funds available if requested by the Greek authorities, how much tax payers across Europe will contribute, what would trigger the mechanism, the interest rates to be applied to the different tranches of loans etc. and how little attention has been paid to the conditionality that should be attached to the assistance programme. This shows that there is a risk of missing the whole point: the challenge for the European leaders is how to make credible again the Eurozone as a zone of stability. This is incompatible with benevolent myopic decisions. To bring the euro back on track is a major political challenge that needs much more than therapeutic policy- making. The political (and not merely technical) message that the euro project we all agreed on is by definition incompatible with irresponsible and unsustainable national fiscal policies should be heard loudly. For this to be achieved, European leaders and EU institutions should promote the adoption of national stability agreements among all the political parties that in each country will be governing the national budgets in the decades to come.

## 2 The need to reframe the governance debate in the Eurozone

By Daniela Schwarzer*

The economic and financial crisis is the first serious stress test to the Eurozone and at first sight the young currency is navigating through the storm surprisingly well. Its unique governance set-up has proven sufficiently flexible to handle situations unexpected at the time the EMU's architecture was devised. But there is no reason to relax: The conditions for finding long-term solutions for the EMU's apparent governance problems have deteriorated.

### Adjusting crisis management and prevention tools and tackling long-term challenges

The Eurozone has to tackle serious shortcomings of economic and fiscal governance to ensure its survival. Currently, the management and prevention of those crises induced by unsustainable economic and fiscal policies are the most pressing aspects.

The Eurozone will have to deal with further budgetary crises and possibly with sovereign defaults. To date, it does not dispose of proper crisis management instruments. The Greek case is being handled on an ad hoc basis. This ad-hocery should not be repeated – and not only because the overt political disputes over the issue have had negative repercussions for the Euro's image in the world and on public opinion within the Union. Upcoming cases may also be too large to be handled in a comparable way and market reactions may be more violent. A general crisis resolution mechanism should include a European Monetary Fund along with clear rules for conditionality and transparent procedures to handle a sovereign default to increase predictability.

With regard to crisis prevention, it is increasingly acknowledged that budgetary discipline is insufficient to prevent instability. The next fiscally problematic country cases following on Greece are likely to be those which result from competitiveness problems (such as Spain). The EMU thus not only needs a framework which can prevent fiscal misbehavior and misreporting. It also has to reduce the economic imbalances that may cause more serious economic and political tensions. This implies stronger surveillance of real exchange rates and their underlying variables such as wage and price developments, taxation policies etc.

Correcting imbalances may also be a necessary part of the solution to the problems of some highly indebted countries. Fiscal consolidation and real exchange rate adjustment pursued for instance by the Greek government may not be sufficient if the country runs into a vicious circle of recession and pro-cyclical consolidation policies. In that case, the country may need to be helped through an adjustment on the part of the "current account surplus" countries or via higher fiscal transfers over a longer period.

In order to tackle persistent divergence within its borders in the long run, the Eurozone should pursue a three-fold strategy: Firstly, market integration should be pushed in order to better accommodate asymmetric shocks. Secondly, with regard to the future EU budget, EU money is not spent in a way that unleashes pro-cyclical effects, but rather the contrary: ways should be found to extend EU spending over the cycle or to vary co-financing. Thirdly, the question whether the Eurozone would fare better in good and bad times with automatic stabilisers on the EMU level should be thoroughly debated.

### Another crisis driving further integration?

Since the crisis broke out, economic governance mechanisms in the EMU have undergone important dynamics. Some policy watchers have identified big leaps in European integration thanks to the crisis. Among the examples commonly cited is the first Eurozone summit of October 2008 or the legislative package on Financial Market Supervision (which admittedly does not meet the

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expectations of those who argue for even stronger European supervision). Another example is the new willingness to apply existing policy coordination mechanisms more rigorously. Both are examples that indeed the European level is strengthened in surveillance and in policy coordination.

But there is little reason to assume that the current crisis – like other crises in the past decades – catalyses a big leap forward. One could even argue that the conditions for cooperative political behaviour on the side of the member states have deteriorated. This explains the difficulties countering the challenges outlined above.

### Sensitive public opinion

Historical data on public opinion shows that support for European integration is low when the economic situation is bad (low growth, high unemployment, individuals feel of economic and social insecurity correlate with little support for integration). And since the real economic effects have hit the EU member states in 2009, there is indeed some evidence of declining support for integration.

But on the other hand, there are rising public expectations as regards the EU's problem-solving and protective capacity in the economic and social dimensions. This tendency is likely to rise with new generations becoming voters who have grown up in a Euro-reality, without personal memories of the age of national currencies.

Nevertheless, high expectations not only mean potential backing for joint European initiatives, but also greater potential for public disappointment. Failed expectations could result in an even stronger decline in support for the EU. The importance of active communication and opinion leadership on the benefits of the EU and the Euro is hence rising.

### Little opinion leadership on EU issues to be expected

For some time now, observers deplore growing EU indifference or skepticism and the lack of political leadership. The domestic political context at least in some member states may rather deteriorate than improve in the near future. The effects of the crisis, the adaptation to rising competitive pressure and need for real devaluation may cause political backlash. Political fragmentation and rising populism may weaken some governments' appetite for integration.

Since the 1990s, member states look at the net costs and benefits of EU membership more closely. In the long run, there is the risk that net payers revise previous assumptions on necessary solidarity and cohesion in the E(M)U to the bottom. Policy choices are assessed with predominantly short-term considerations with less of a historical perspective on the challenges. Among the reasons for this is the change of generations among political leaders and the fact that external challenges (which of course do exist but which tend to be largely underestimated) exert little integrative pressure, compared to the Cold War. Questions about changes in European engagement are raised in particular with regard to Germany, not least with regard to the recent ruling of the German Constitutional Court and more recently Germany's debate and position on Greece.

### Germany and the economic governance debate

In particular, the German EMU governance debate seems somewhat out of phase with discussions on the Eurozone that develop in Brussels, in European and international academic/think tank circles or in European and international media. The interpretation of the Eurogroup statement of March 15, 2010 illustrates one of the aspects. It prominently mentions external imbalances (and not only current account deficits) as a problem acknowledging that imbalances should be tackled both by deficit and surplus countries. Meanwhile, the interpretation in Berlin is still widely that adaptation is the deficit countries' duty.

The debate on Greece (and the idea that "Germany could pay most of the share") has touched the nerves of the population, media and the government. The criticism of Germany's export strength (which has replaced the D-Mark as the strongest symbol of national identity) and the reproach that Germany is "free-riding" on others has provoked profound feelings of unfairness. Mistrust towards fellow Eurozone members has risen, there are profound concerns that the stability orientation of the EMU is at danger, which revives deeply rooted German fears about the devastating consequences of monetary and economic instability the country experiences in the first half of the 20th century.

With regard to the question of sharing the costs of adaptation in the current crisis, at least part of the German press has a tendency to ridicule discussions on the question whether Germany needs to adapt its growth model. The majority of statements and press articles transport the idea that the German way is the only feasible one, that there is in any case no way to influence domestic demand and there is little mentioning of the question whether the German strategy would at all be sustainable if the other Eurozone member states indeed followed.

The way the debate on Greece has evolved in Germany has probably lead to ideological hardening of positions and perceptions. This is part of the reasons why Germany will most likely continue to be very reluctant on further governance debates. The question of “fair share” will probably arise when the question of fiscal exit is discussed as some observers start making the case that Germany should withdraw fiscal stimulus later than national conditions would suggest in order to support Eurozone-wide recovery.

## A need to reframe the issue

The EU currently faces a window of opportunity to bring forward the governance debate, as the crisis management period and the “case of Greece” correlate with the EU2020 and EU budget debate. But so far, the political focus is on risk management and prevention, but not on the strategic question how to develop the Eurozone further and to improve its performance. In order to open up the discussions, the current debate should be reframed by consciously giving European impulses in national debates. Some elements could be:

Eurozone problems need Eurozone answers: There is a need to explain more clearly that in many ways domestic economic (and in the end social conditions) cannot be seriously tackled without stronger coordination in the Eurozone. This is more than crisis prevention and management, there is a need for a coherent and growth enhancing policy mix.

Eurozone problems need strong Eurozone actors: The crisis has made clear that the Eurozone has particular coordination requirements. It needs efforts of confidence building among its leaders and a strategic debate on its own development. While the increased interest of the European Council in EU economic matters is positive, closer political exchange among the EMU-16 should be pursued in parallel. EU members which are not (yet) part of the Eurozone should be informed, but should not be the reason not to deal with EMU issues among EMU members.

The dynamics outside the Eurozone should not be neglected: Closer and continuous political exchange in the Eurozone is all the more important as it will have to react to global dynamics (such as e.g. the rebalancing of the US-China relationship). The rapidly changing international environment (in political, economic, security and demographic terms) and its consequences for Europe should be highlighted to enable more realistic assessments of what single member states would be able to achieve on their own.

Eurozone citizens have to be taken along: A permanent issue in the governance debate is the discrepancy between national sovereignty and the economic interdependencies within the Eurozone. Governments stick to national approaches at the cost of potentially suboptimal political and economic outcomes – even if joint approaches would be a win-win-situation for all. In a short view, this is neither irrational nor illegitimate given their national constituencies. In the long run, this problem can only truly be overcome by a quantum lead in integration: a democratisation of Euro-level economic governance.

## 3 How social the Single Market?

By Jacques Pelkmans*

In two weeks time, Professor Mario Monti is expected to present his suggestions for a revival of the Single Market to Commission President Barroso. In his entrusting letter to Monti, Barroso rightly points to "…the dramatic consequences that would derive from undermining the Single Market. That would erode the basis for economic integration and growth and employment throughout the EU…" [See PRES(2009) D/2250 ]. After rehearsing the oft-heard refrain that the Single Market is far from being completely in place and the Commission's intention to "… take a more systematic and integrated approach…", he notes that the financial crisis induced "… some critical reconsideration of the functioning of markets" as well as "… enhanced concerns about the social dimension." Given that the Lisbon Treaty says that "… the Union […] shall work […] for a highly competitive social market economy…", the Commission President calls for a fresh look "at how the market and the social dimensions of an integrated European economy can be mutually strengthened". Indeed, in the preparatory discussions to support Monti's reflections, many observers referred to the negative or sceptical perceptions currently held in Europe about "more market", including "more internal market". Some analysts think that the 'neo-liberal paradigm' has been discredited; others note that numerous citizens and workers have lost confidence in the authorities' ability to properly regulate and supervise financial markets and the leading actors in the markets – with profoundly negative repercussions for all – and yet others find that public money is being spent on banks and far less on mitigating the social consequences that have befallen those who had nothing to do with the cause. One inference of these deliberations is to place the 'social dimension upfront' when reviving the Single Market.

The social dimension of the internal market has been a theme for debate ever since 1987, when Jacques Delors introduced it as a counterbalance to the emerging "Europhoria" of European business about the EC-1992 Single Market programme. Although the complaints about the lack of a "Social Europe" make it into the local and European press much more easily than a sober analysis of the actual meaning of the label and the factual progress made, this CEPS Commentary encourages the reader to step back for a moment and reflect on what "the" social dimension of the Single Market does and does not mean and to assess where we stand today. Only then, it seems to me, is it possible to draw some inferences about the potential and scope of "putting the social dimension upfront" in a new internal market initiative.

### Social dimension at the EU level?

The biggest initial fear was that the internal market's deepening and widening would engender a Thatcherite wave of deregulation across the EU12. In the Hannover European Council of 1988, this fear was dispelled by announcing high standards of social protection for the EU, a phrase later incorporated in the Maastricht Treaty. Of course, those standards were not set at the EU level since Member States were very reluctant to transfer significant social powers to the EU. So, it was up to the Member States. However, whenever the EU did have the competences, such a high level of protection had to be pursued at EU level. Similarly, the internal market should not undermine such standards and where a problem might arise, minimum harmonisation would guarantee a "floor" of social protection. The Social Protocol was attached to the Maastricht Treaty in a legally complex fashion owing to the fact that the UK government was unwilling to ratify. This suggested that the Protocol was socially ambitious (which it definitely was not) and that Member States other than the UK were significantly less sensitive to a further delegation of social powers to the EU level (which was not the case either). In 1997 the Labour government wasted no time in formally accepting the Protocol. During the 1990s and to some extent in more recent years, a series of

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minimum social requirements have been incorporated into EU directives.[1] The Social Dialogue, also introduced in Maastricht, has been used by the social partners to jointly formulate the texts of some of these directives[2] as well as a large number of specialised sectoral agreements. Thus, even though Member States are loathe to transfer social competences to the EU level, increasing market integration has been accompanied by a considerable EU effort ensuring that the Single Market was not derailed into becoming an anti-social project. Merely asserting that "the" social dimension of the Single Market has been neglected at the EU level seems to be more an expression of a political preference than a factual observation. Lest it be forgotten, the same Member States do not allow for an expansion of the EU budget, say, to engineer an EU-tier of complementary social spending e.g. on unemployment benefits.[3] Understandably, perhaps, because such or much other social spending would probably not pass a subsidiarity test and the amounts would have to be quite large before becoming meaningful. But the sole reliance on regulatory approaches severely constrains the EU level in what it can and cannot do. Within the regulatory perspective, in turn, Member States are not keen on a serious expansion of EU powers.

## The social dimension after the Eastern enlargement

When the two Eastern enlargements arrived, social anxieties increased in the high-income part of the EU. It is useful to remember that host country control (HCC) had been "acquis" since the early 1970s (and still is). Labour unions typically regarded this as a form of (national) social protection, allowing them to accept the free movement of workers (formally, though not practically, in place since 1968). HCC ensures that workers migrating to another EU country cannot compete on the essentials of labour market regulation in the destination country, whether minimum wages, holidays, working time or (most) other aspects. It is a convenient rule among countries with more or less similar income levels: given the complexity of labour law and its manifold links with the local welfare state, clarity about which country's law applies is helpful. With Eastern enlargements, however, income levels suddenly were drastically different. The upshot is an awful dilemma between HCC in high-income EU countries and ensuring in reality the rights of workers from the new Member States. Workers in high-income EU countries tend to stick to HCC, as before, but nonetheless find that somehow Eastern workers flock to 'their' labour markets, in particular in segments like construction, horticulture, cleaning, simple restaurants and meat processing. What is the EU element of this predicament (and what is not)? What is not so 'social' about this manifestation of the internal market, giving the latter a bad reputation?

Economically, a strict adherence to HCC has the effect of reducing or eliminating the demand for Eastern workers in the high-income EU countries.[4] This is so irrespective of whether they come as migrants taking up a regular job or as posted workers for temporary services. The only scope for those workers to be hired is 1) the differential between the minimum wage and the wages actually paid and 2) a willingness to work longer hours and on Saturdays since they are away from home in any event. Apart from this limited scope, HCC is therefore protectionist: it keeps Eastern workers out; worse, they cannot exploit their social rights (of free movement) under the treaty, namely, the income-raising opportunity of working in the Single Market where the well-paid jobs are. Thus, what is "social" for high-income workers, is "asocial" for Eastern workers and they are the poor lot. It is simply incorrect to argue that high-income countries – in imposing HCC on Eastern workers interested to come to their labour market – are exercising a benign form of "social protection" on their behalf.[5] The contrary is correct: HCC ensures that the effective demand for those workers dries up so that there will be nobody from poor EU countries to protect in the first place. HCC robs free movement of workers (or free movement to provide temporary services) from relatively poor EU countries of its socio-economic meaning. The European Court of Justice (and the Celle court in Germany, having requested a preliminary ruling) spotted this correctly in the 2008 Ruefert case.[6]

### The Polish plumber who never was

A closely related social anxiety was the French myth about the Polish plumber. Proof that the Polish plumber in France never really existed – indeed, could not exist – is disarmingly simple. There was no basis for accusations of "the" EU, neither in the EU 'constitution' nor in the acquis at the time (nor today). One wonders who has talked the French press and citizens into this and why the elementary unravelling of the story never had a chance. There are four options for the notion of the Polish plumber and four is exhaustive:

i) The plumber may get into France (or many other EU countries) as a normal migrant, taking up a regular job; this labour contract is under HCC (and already was, decades ago); this applies equally when the plumber would work for an employment agency.

ii) The plumber may come as a posted worker for a temporary (plumbing) job; as noted above, posted workers fall under HCC (Dir. 96/71), irrespective of whether the firm posting him is established in Poland or e.g. in France.[7]

iii) The plumber may come to France (or elsewhere in the EU) as an independent-without-personnel (IWP); here, matters are different because our plumber can now enter into a service contract for a total work project (say, doing the plumbing of a school building) for a fixed amount; the implicit hourly wage of that contract can be below the HCC wage since he is an independent (with all the risks that this entails). This option is not new at all, however, and has nothing to do with a new twist in the Single Market or with enlargement as such. Note that most such independents only operate domestically. At issue here are those who make most of their living from contracts in other Member States. What explains the recent increase of the use[8] of this option is that Eastern workers are more risk-prone than their counterparts in the EU15, given the enormous opportunities for skilled construction workers in the west of the Union (today, after the crisis, they might reconsider, but that is another matter). Cross-border IWP services were not frequently supplied before, simply because the sacrifices of this option, with the service providers away for many weeks from home time and again, are such that few people would wish to do this for a long time.

iv) Our plumber might get into France illegally, that is, work illegally under contracts or arrangements that infringe French law (and EU law as well). The EU cannot be accused because people misbehave (given wage discrepancies) and it is up to local enforcement to stop it.

It follows that the Polish plumber cannot symbolise a lack of the social dimension of the internal market: options i and ii are 'social' in the sense of protecting French social entitlements; option iii allows selective competition outside HCC but it has been around for decades (with no ripple effects whatsoever, and balanced by much higher risks for those independents) and option iv is simply a violation of EU and national rules (and France itself ought to stop that).

### Balking at Bolkestein's draft?

Could the turbulent debate around the horizontal services directive have left a lingering idea of a too weak social dimension? The obsessive debate (often actually a non-debate) in the EP on the draft directive made it impossible to pay proper attention to very sensible solutions to the problem, which were surely social, too. One great contribution by the Dutch Socio-Economic Council[9] was not taken up, much to the peril of the EP and the EU. In a most careful and extremely detailed report, the Council not only explains in a painstaking fashion all the misunderstandings and false soundings around the draft directive but also adopts a limited list of amendments that enabled the text to remain based on the country-of-origin principle, with more derogations (but not as many as the EP allowed due to lobbying) and circumscribing some boundary issues (like private law questions under the Rome Conventions). The report, in fact almost a ready text for adoption, was approved unanimously by the social partners and the independent experts. One cannot seriously argue that the Dutch Socio-Economic Council, with the active participation of labour union leaders and a 60-year social record envied by many elsewhere, does not pay due attention to the social dimension.

## Is the Single Market an agent of globalisation?

Could the impact of globalisation on a very open EU market for manufactured goods be the ultimate culprit? Because it is so open, so the story goes, the single goods market boils down to direct competition with China; hence, the incessant pressure to cut non-wage labour costs (mainly, social charges) and to invest in China itself. It is argued that both trends would, in the long run, threaten the viability of Europe's social models, possibly even the EU's prosperity levels.[10] Of course, this is a very one-sided picture (and only for goods, not to forget), ignoring the fact that international economic intercourse is a win-win game. So far, the EU problem is one of restructuring, adjustment and shifts to new economic activities and this has worked reasonably well, in part also because Central and Eastern Europe has served as an alternative to remain competitive in certain industries. Indeed, to the rest of the world, it is often the EU that is regarded as a, if not the, leader in globalisation (certainly in services and direct investment, besides capital, intermediate and high quality goods). For the EU to continue this relatively successful shift so far, it needs to be far more aggressive in innovation and change, beginning inside its internal market. Nobody in Europe seriously pleads for the Single Market to be closed. Other options are all related to innovation and adjustment, the more so as ageing can be a menace to our future productivity growth for another two decades. Since services represent 70% of value added, competition and dynamism in this sector – non-tradable "domestic" services just as much as potentially tradable services in the internal market – must be central to any long-run growth strategy.

## Putting the social dimension of the Single Market upfront?

In the light of this quick overview, one should reflect on what putting the social dimension of the internal market upfront would actually mean. As shown, the Single Market already has built in a social "floor", as it were. Eastern enlargement has increased sensitivities, no doubt, but it has also demonstrated the ugly side of HCC: it all depends on whether one focuses on "rich" or "poor" EU workers. Still, with catch-up growth returning soon in Central Europe, this problem will gradually go away in another decade.

Perhaps putting the social dimension upfront means that in 2012 (when the services Directive 2006/123 has to be reviewed), the Socio-Economic Council proposal should be taken up again as an improvement over today's badly drafted and unclear directive, with too many derogations.

Or perhaps it means that the EU should go for growth and jobs even more than before so as to pull workers back into jobs. There has been firm talk by ministers of a European Employment summit and an employment strategy in the framework of EU2020. With so many unemployed in the EU, this is indeed an initiative one can start with. No doubt, the social and economic gain of lowering unemployment in Europe renders it an overriding priority. Who would possibly oppose it? But is this tantamount to the social dimension of the Single Market, or is it once again a coordination of basically national strategies and few if any concrete Single Market tools?

Or perhaps it means that the internal market cannot be deepened where social sensitivities are expected to pop up. Knowing that such sensitivities persist mainly in labour migration and in services, such prudence would pre-empt any move to bring genuine productivity improvements (except the long-awaited EU patent). It would force Professor Monti into side shows such as education (crucial, true, but the EU has few powers here) or into rehearsing the crucial role of domestic reforms (sadly, also these are in services and labour markets) where the EU can mainly act by persuasion and this has not been successful so far in some crucial eurozone countries. But Barroso has already noted that there is still a range of stubborn barriers to migration inside the Single Market in matters such as health insurance, mutual recognition of diplomas, pensions, housing (for workers with lower wages) and occasional tax conflicts between Member States.

Or perhaps advocates of putting the social dimension upfront refer to accompanying measures which, in and by themselves, are not part and parcel of the Single Market, such as typical Lisbon/EU2020-type goals of fostering social inclusion (they are typically local, too), pursuing "flexicurity" in national labour markets, improving active labour policies and emphasising "upskilling" the European workforce much more than before. All of these are in principle worth pursuing (and presumably overlap with employment strategies), but not all of them fall into the Single Market domain (large as it is) and the EU level has no direct powers and just tiny funds at best to deliver.

Finally, perhaps one has to go against the perception that "the" Single Market is there for (big?) European business. Of course, that is not and should not be the philosophy: it is overall economic welfare that increases over time, and in specific terms, it is the citizens, workers and consumers, who benefit. However, it has been next to impossible to convey this message convincingly to EU consumers and citizens for many technically complicated measures over many years, still apart from the robustness of the empirical economic analysis. If and when one does try to convey these complicated measures, it quickly becomes an abstract and conceptual exercise, with the fall-back option consisting of anecdotes. The fact remains that it is predominantly the relatively big and successful firms that actively exploit the Single Market;[11] whether we like it or not, they are the effective agents making the Single Market work. The recent progress on facilitating SMEs operating in the internal market (with the measures in the Small Business Act, by lowering thresholds and cutting red tape) is welcome and can only help. We need them. A renewed emphasis on consumers and citizens in the internal agenda deserves strong support (Malcolm Harbour, Chair of the EP Internal Market and Consumers Committee, has stressed this recently, too), but this can hardly be denoted as "putting the social dimension upfront". Consumers and citizens simply are agents benefiting from greater choice and wider options from cross-border competition, hopefully also (more) on-line, and from price discipline exercised by intra-EU competition.

## Conclusion

Unlike more than two decades ago, today's social dimension of the internal market has created a robust social minimum "floor" of requirements. Surely, one might wish to add some such minimum harmonisation in a few areas or make them a little more ambitious when revising directives. Broadly speaking, however, the Member States want the EU level to be responsible for the current social dimension of the Single Market… and no more. The social powers of the EU are limited,[12] which is exactly what the Member States want. It is therefore misleading as well as pointless to accuse the EU as such of not doing enough in areas in which it has no competence to deliver. In the context of EU2020 or otherwise, it is useful to stimulate Member States to reform more at home and to coordinate their national employment strategies, but this is largely independent of further internal market initiatives. Of course, one can bring them together in a wider "strategy". After all, both are eminently sensible. If this is what is meant by "putting the social dimension upfront" in a new internal market initiative, I would be all in favour.

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## Endnotes

1 Without being exhaustive, they concern health and safety at the work place, information and consultation of workers (e.g. on major investments and mergers), collective redundancies, avoiding nightshifts, etc. for pregnant women, maternity leave, working time (with a host of exceptions for special reasons), posted workers, the European Work Councils for large European companies and directives on part-time and fixed-time contracts. Later examples include, among others, a directive on temporary agency work and on protection of workers in the event of insolvency of employers. Also, several of these directives have meanwhile been strengthened.

2 Based on Art. 139, EC, now Art. 155, TFEU.

3 The relatively small EU Social Fund and the tiny European Globalisation Adjustment Fund have found their place within today's political EU budget cap of 1% of EU GNP. Ideas about a complementary EU employment fund go back to the 1975 Marjolin report.

4 For a formal economic analysis, see Pelkmans (2006, pp. 197-198).

5 Note that the fine sounding slogan "same workers, same site, same labour conditions" may have similarly perverse effects of locking out Eastern workers.

6 Case C-346 / 06, ruling 3 April 2008. The ECJ sided with the Celle court which said that complying with local collective agreements would make them "… lose the competitive advantage which they enjoy…" Similarly, the same obligation does not lead to 'equal treatment' with German workers either "… but rather prevents [posted] workers … from being employed in Germany".

7 Incidentally, since France has general minimum wage legislation, unlike e.g. Germany, one would expect the inflow of posted workers to be far stronger in Germany than in France. This is borne out by the data. In the 2008 "Employment in Europe" report of DG Employment, Chart 5, p. 121, it is shown that more than 80% of posted workers in 2006 in Germany were from the new EU Member States, as against only one-fifth in France.

8 In fact, going beyond anecdotes, we know precious little about cross-border services provided by IWPs. According to the European Foundation for the Improvement of Living and Working Conditions (2009), one recently observes both trends of declining IWPs in some Member States and of an increase in other ones e.g. Belgium, France, the Netherlands, Germany, Romania, and the UK. However, in France in 2007, this increase had merely led to a share of 5.8% of total employment for IWPs, when including agriculture, and around 4 % without. Apart from Luxembourg and Denmark, France still has the lowest share of all EU countries. The Polish share is fairly high (15%), but shares in Italy, Portugal, Greece and Romania are higher still. What these data do not show is where exactly the services of the IWPs are delivered, home or abroad and to what extent.

9 SER, 2005.

10 Arguably the sharpest reminder of this fear is the title of a famous article in 1995 by Professor Richard Freeman, "Are your wages set in Beijing?". See also Brenton & Pelkmans (1999) for extensive analysis of the issues in Europe.

11 For revealing results, based on research with data at the individual firm level, see Mayer & Ottaviano (2007).

12 For an accessible and brief survey of those powers and their limits, see Pelkmans (2006, chapter 15) or Pelkmans (2008). Note that the Convention in February 2003 in working group 11 decided that the social powers of the EU were just about right.

## 4 Towards economic union: a new strategy for the Single Market

By Paola Rossi

On March 30 2010 BEPA organised, in close cooperation with Bruegel, a Workshop on the theme "Towards economic union: a new strategy for the Single Market".

The rationale behind this Workshop lies in President Barroso's conviction that the Single Market calls for renewed political commitment to withstand the insidious threat of economic nationalism and tap into its full potential, as set out in the political guidelines the President proposed for the new Commission.

We are now approaching the 20th anniversary of the symbolic date of 1992, which marked the birth of the Single Market. At the time, the renowned Cecchini report entitled the "Costs of non-Europe (1988)" specified the conditions for establishing the fourth freedoms (goods, capitals, services and works) by carefully examining the costs and benefits of a Single Market in Europe, in accordance with the – at the time – Treaty of Rome. That strategic decision, along with the integration efforts made by the Delors Commission, has now a second blush of youth.

President Barroso clearly stated that one of the objectives of the Commission action in the coming years will be to "regain the momentum in the internal market, making it the powerhouse of the European economy". The Single Market is "the jewel in the EU's crown", the backbone of the European economy and must be the cornerstone of Europe's recovery.

To this end, last October President Barroso invited Mario Monti, President of the Bocconi University and former Commissioner for Internal Market, Financial Services and Tax Policy (1995-1999) and for Competition (1999-2004) to draw up a report on the re-launch of the Single Market. To perform this delicate duty, Mr Monti liaises directly with the President and avails himself of the expertise and logistical support of Commission staff. Mr Monti has already consulted Member States, Commissioners, Members of the European Parliament and other stakeholders.

Before completing his report, which is due by the end of April, Mr Monti asked BEPA and Bruegel to organise the above-mentioned Workshop, which provided a unique forum to exchange ideas with the academic community and with the most relevant think tanks engaged in European matters. The main objectives of this gathering were to obtain additional information and broaden the audience of his consultation exercise and to test his ideas and get high-quality inputs.

The Workshop has been divided into two sessions, as the revamping of a well-performing and efficient Single Market needs both regulatory and non-regulatory measures. This combination of measures will help markets move towards closer integration and, at the same time, it will make this further integration politically rewarding and socially acceptable.

After having briefly outlined the progress in the Single Market report, Mr Monti brought to the table some key questions in order to encourage the discussion (e.g. which are the new engines of the political and economic integration? Will the new Member States take up the flag and become the driver of the market reform? What will be the role of the old Member States in this respect?

The first session – "The political economy of the Single Market today" – looked at the obstacles that continue to remain and at the best way to overcome them. Under the helpful guidance of Marco Buti, Director-General of DG ECFIN, Paul Seabright (Professor and Researcher at the "Institut d'Economie Industrielle" of the Toulouse University), Helen Wallace (Professor on European Integration at the LSE) and Roger Liddle (Chair of Policy Network think tank) put forward a strategy to be followed and areas in which the Commission should act in the years to come. What it clearly emerged was the need to generate a new political momentum to make the Single Market engine work again at full speed.

Some keynote speakers contented that existing differences in "appetite" between old and new Member States could create a favourable level playing field for establishing an economic governance in Europe.

The discussion also focussed on other areas, including education, health, environment and digital economy, where certain speakers felt that the Commission should become more active. More specifically, Professor Wallace emphasised the need for the Commission to improve regulation and to pay careful attention to health services, e-industry, green technologies and energy. Roger Liddle mentioned tax coordination and the need for a re-regulation of financial services at EU level, especially in the current crisis framework.

The second session was chaired by Robert Verrue, Director-General of DG EMPL. Nicolas Jabko, Senior Research Fellow at the Faculty of Political Sciences, Paris, Daniel Daianu, Professor of Economics at the National School of Political and Administrative Studies in Bucharest, former Minister of Finance and MEP, and André Sapir, Senior Fellow at Bruegel and Professor of Economics at the ULB, Brussels took part in this session. It was argued by some that the completion of the Single Market could only be achieved at the expense of the welfare and social dimension, and this perception had become even more deep-rooted as a result the world economic crisis. Nicolas Jabko presented his view of the "Janus faced Europe", between liberalism on one side and solidarity on the other. He underlined the importance of the so-called political space for the Single Market, which had recently shrunk. In order to "re-launch" the Single Market, Mr Jabko suggested to put the social dimension upfront, re-engineer the Single Market and involve more politicians and citizens in this important project. Little was said, however, on how these objectives could be attained.

Mr Daianu insisted that moral/ethical values should be more present in the business dimension and that taming financial markets (via better regulation and supervision) would unleash more entrepreneurship and dynamism.

Mr Sapir framed the Single Market within the context of the global Europe, underlying the tension between equity and efficiency in the Market and suggesting that Europe should invest more on education.

The Workshop made it clear that there are no magic and ready-made recipes for a renewed and strong Single Market. Nevertheless, one of the main outcomes of this Workshop was the need to create a new political appetite for the Single Market –as it was the case in the 1990s – and to move ahead towards an Economic Union (Europe has successfully completed its Monetary Union but failed to add the economic component to the EMU). In a nutshell, the seminar's overall outcome seemed to imply that Europe has still a long way to go to accomplish the objective of a "highly competitive social market economy" as set out in the Treaty on the functioning of the European Union.