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The building of economic governance in the European Union

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Summary

This article seeks to shed light on the development over the past decades of the concept of economic governance. It asks what is understood by economic governance and what role the social dimension has played. The article offers an analysis of the problems and possible issues confronting the EU as it seeks ways to address the sovereign debt crisis by embarking on deeper economic integration. The article concludes that from the early days there have been questions about the exact interaction between economic and monetary integration and thus between 'economic' and 'monetary' union. Despite Delors' original inclination, few were willing to establish any linkage between EMU and social matters. The crises have again brought out the need to consider the two in tandem. Moreover, with the increased role in economic governance accorded to EU-level institutions, there is a need to rethink the EU democratic model.

Résumé

Cet article vise à faire la lumière sur le développement, au cours des dernières décennies, du concept de gouvernance économique. Il soulève la question de savoir ce que l'on entend par gouvernance économique et quel est le rôle que la dimension sociale a joué. Le présent article propose une analyse des problèmes et des enjeux possibles auxquels est confrontée l'UE, dans la mesure où elle cherche des solutions à la crise de la dette souveraine en se lançant dans une intégration économique accrue. L'article conclut que dès le début, il y a eu des questions sur l'interaction exacte entre intégration économique et intégration monétaire et donc entre union «économique» et union «monétaire». Malgré le penchant initial de Jacques Delors pour une telle association, il ne s'est pas trouvé grande monde pour établir un lien quelconque entre l'UEM et les questions sociales. Les crises ont à nouveau mis en évidence la nécessité d'aborder ces deux aspects ensemble. En outre, avec le rôle accru de gouvernance économique accordée aux institutions européennes, il est nécessaire de repenser le modèle démocratique de l'UE.

Zusammenfassung

Dieser Beitrag beleuchtet die Entwicklung des Konzepts der wirtschaftspolitischen Steuerung oder „Economic Governance" in den letzten Jahrzehnten. Er untersucht, was unter diesem Begriff verstanden wird und welche Rolle die soziale Dimension dabei gespielt hat. Der Beitrag

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liefert eine Analyse der Probleme und möglichen Fragen, die sich für die EU bei ihrer Suche nach Wegen aus der Staatsschuldenkrise durch eine vertiefte wirtschaftliche Integration stellen. Der Beitrag gelangt zu dem Schluss, dass es von Beginn an Fragen über die genaue Interaktion zwischen wirtschaftspolitischer und währungspolitischer Integration und somit zwischen „Wirtschafts-“ und „Währungs“-Union gegeben hat. Trotz des ursprünglich von Jacques Delors vertretenen Ziels waren nur wenige bereit, die WWU in irgendeiner Form mit sozialen Themen zu verknüpfen. Durch die Krisen ist allerdings wieder deutlich geworden, dass diese beiden Aspekte zusammen betrachtet werden müssen. Und angesichts der verstärkten Rolle, die den EU-Institutionen bei der Economic Governance zukommt, ist es auch notwendig, das Demokratiemodell der EU neu zu überdenken.

Keywords
Economic and Monetary Union (EMU), economic governance, European Union, political integration, public finance, social dimension, supranational governance

Introduction

Over the past 50 years the issue of economic governance has been on the agenda many times, often in connection with renewed interest in deeper European integration. It featured prominently in the debates over Economic and Monetary Union (EMU) in 1969–1971 and in 1989–1991, finding its way into the 1970 Werner Report and the 1989 Delors Report. Until a few years ago, academics paid only sporadic attention to economic governance. This changed however with the onset of the financial crisis, the subsequent economic crisis and most recently the sovereign debt crisis, and the topic now has the full attention of academics and policy-makers throughout the world.

As the crisis continues, many are asking whether EMU is possible without deeper economic governance. But what exactly does economic governance mean? What role is played by social and political integration as economic integration deepens? The recently approved Euro Plus Pact by 21 European Union (EU) Member States, together with the introduction of tighter rules via the so-called 'six-pack', has led many to question what effects these could have on wage setting and collective bargaining. Those upholding the existence of the celebrated 'Social Europe' (Trubek and Trubek, 2005; Scharpf, 2002) and 'Europe's Social Model of Society' (Martin and Ross, 2004) are wondering how the process will affect public spending and what these new rules might mean for the future of welfare states across Europe.

This article seeks to shed some light on the development of the concept of economic governance over the past decades, asking what is understood by economic governance and what role the social dimension has played. The article offers an analysis of the problems on the table and possible issues confronting the EU as it seeks ways to address the sovereign debt crisis by embarking on deeper economic integration. Again, the question will be on what role is accorded to the social dimension.

The article is structured as follows. The next section looks at the historical background, economic governance and the EMU's social dimension. Section three discusses why economic governance is needed. The fourth section looks at the impact of the crisis in its various guises on EU governance and the social dimension, going into how the EU has responded to the crisis and what the new rules entail. The fifth examines what these new rules might imply for good governance, the role of the social partners, public spending and welfare states. The article then concludes.

Historical background

Economic governance has been on the agenda ever since European Community (EC) Member States started contemplating deeper integration. It is worthwhile remembering that in the 1960s EC Member States sought to balance plans for deeper monetary integration with what they then called deeper 'economic integration'. The distinction between 'monetary' and 'economic' integration might confuse contemporary readers, as one could argue that the latter encompasses the former. In fact the terminology was the result of a dispute between the so-called 'economists' and the 'monetarists' (Kruse, 1980; Tsoukalis, 1977; Verdun, 2000). Whereas the former advocated deeper economic integration across the board before integrating monetary policy (including fixing exchange rates, transferring monetary policy to a supranational institution and ultimately introducing a single currency), the latter argued that monetary policy should be transferred to the supranational level first and that deeper economic integration would follow. The understanding of economic governance at that time included the creation of a supranational Centre of Decision for Economic Policy, the coordination of budgetary and fiscal policies, a larger role for supranational governance in regional and structural policies and a consultative role for the social partners (Werner Report, 1970: 11).

The 1977 MacDougall Report examined the possible need for Community public finance to accompany deeper economic and monetary integration. The report offered some insights into mature federal states, concluding that public finance could serve many goals such as cushioning the effects of a recession or reducing differences in per capita income among the different regions of a fiscal federation (European Commission, 1977: 12): 'As well as redistributing income regionally on a continuing basis, public finance in existing economic unions plays a major role in cushioning short-term and cyclical fluctuations.' By having a larger budget and by levying taxes, Community public finance could serve as an automatic stabilizer. In fact, the Report deemed it conceivable that the Community could somehow become involved in matters ultimately affecting income differentials, calling for:

'... Community action in the areas of structural and cyclical policies (regional, manpower, unemployment) to ensure so far as possible that the benefits of closer integration are seen to accrue to all, that there is growing convergence – or at least not widening divergence – in the economic performance and fortunes of Member States. Those measures should make a start in reducing the inequalities in per capita incomes between the various parts of the area; the situation in the eight countries studied tends to confirm that this is a necessary part of economic union.' (European Commission, 1977: 14) Furthermore, it called for a Community budget of 2–2.5 per cent of gross domestic product (GDP) for the so-called 'pre-federal stage' and higher percentages for subsequent economic integration scenarios giving a larger role to Community public finance (European Commission, 1977: 17).

Due to a cocktail of unfavourable circumstances existing at that time, the MacDougall Report went unheeded, making EMU unlikely to be achieved in the near future. Instead, the 1980s focused on the European Monetary System (EMS), the Single European Act and the re-launching of the Internal Market project. And once EMU came back onto the agenda, there was no backing for any increase in the Community budget.

Though the 1989 Delors Report re-examined the earlier reports, no further provision was made for a new supranational body to be created in parallel to the European System of Central Banks (ESCB). Coordination was now supposed to take place through agreeing to a macroeconomic framework and via binding rules and procedures (Delors Report, 1989: 14). Monetary union was defined in the same terms as in the Werner Report:

'– the assurance of total and irreversible convertibility of currencies;
– the complete liberalization of capital transactions and full integration of banking and other financial markets; and
– the elimination of margins of fluctuation and the irrevocable locking of exchange rate parities'. (Delors Report, 1989: 14–15)

The definition of economic union was however somewhat changed, now being defined as:
'– the single market within which persons, goods, services and capital can move freely;
– competition policy and other measures aimed at strengthening market mechanisms;
– common policies aimed at structural change and regional development; and macroeconomic policy coordination, including binding rules for budgetary policies.' (Delors Report, 1989: 16)

In terms of institutional provisions, the Delors Report pointed to the existence of Community institutions (Commission, Council, Court of Justice, European Parliament, Monetary Committee), stating that '[The new Treaty] would have to specifically define these changes and determine the areas in which decision-making authority would have to be transferred from the national to the Community level.' (Delors Report, 1989: 23)

Compared to the Werner Report, the Delors Report accorded the social partners a somewhat different role. Apart from binding rules on budgetary deficits and public debt, all other forms of macroeconomic governance (wage bargaining and other economic and social matters) were to be decided at national or sub-national level:

> 'Many developments in macroeconomic conditions would continue to be determined by factors and decisions operating at the national or local level. This would include not only wage negotiations and other economic decisions in the fields of production savings and investment, but also the action of public authorities in the economic and social sphere.' (Delors Report, 1989: 19)

The role accorded to the social partners was limited to the national or sub-national level, and was to support the overall macroeconomic framework:

> 'As regards wage formation and industrial relations, the autonomous negotiating process would need to be preserved, but efforts would have to be made to convince European management and labour of the advantages of gearing wage policies largely to improvements in productivity. Governments, for their part, would refrain from direct intervention in the wage and price formation process.' (Delors Report, 1989: 20)

In other words, the transition from Werner to Delors saw a shift from a (somewhat) supranational to a national level for social matters.

The Treaty on European Union signed in Maastricht in February 1992 did not fundamentally deviate from the Delors Report in this respect, with the Delors blueprint being incorporated into the Maastricht Treaty. Economic governance was not however fully addressed in the Treaty. The Germans were keen on greater political union and more economic governance but the French were less enthusiastic about having the German vision thereof incorporated into the Treaty (Dyson and Featherstone, 1999; Verdun, 2000, 2003). The Germans in the early 1990s had been concerned that an EMU without clear rules on budgetary deficits and public debts would create problems later on. They were also of the opinion that deeper integration would be needed to accompany monetary integration. The French were less interested in the type of economic governance the Germans had in mind, advocating at times that the European Central Bank be less independent. With a lack of consensus as to what kind of economic governance would be needed, the decision was taken to install a rules-based system. In addition, although the French and Germans were reasonably open to social matters, the United Kingdom was opposed to introducing social elements into the Maastricht Treaty. Against the background of a felt need to create a Treaty containing EMU and a Social Chapter, these issues were negotiated as separate parts of the Treaty, with the United Kingdom being granted an opt-out from both EMU and the Social Chapter.[1] Before EMU was finalized the Commission contributed to the debate on the topic by commissioning four major studies in support of the decision to move towards EMU.

The first study was the One Market, One Money Report (European Commission, 1990), followed shortly afterwards by the 'The Economics of EMU' report containing background studies supporting the first report (European Commission, 1991). These two reports offered the economic rationale for EMU and its particular design. Contributors included Commission staff as well as independent economists, but very few of them focused on the social dimension or the question of whether EMU would affect the welfare state (e.g. European Commission, 1991, Chapter 6). Though the third and fourth major studies had already been compiled in 1991–1992, Commission President Jacques Delors stopped their publication (Verdun, 2000) as he was concerned the topic was too politically sensitive for the state of the debate on Maastricht and its EMU. It will come as no surprise that the third and fourth reports were about public finance: 'Stable-sound finances: Community public finance in the perspective of EMU' (European Commission, 1993a) and 'The Economics of Community Public Finance' (European Commission, 1993b). Since the MacDougall Report the wind had changed, with the report concluding that major public finance would not be required to support EMU.

In an earlier study of this period I sought to examine the impact of the upcoming EMU on social partners and the welfare state, interviewing monetary experts in trade unions, employers' associations, ministries of finance and central banks in Britain, France and Germany with a view to ascertaining what type of EMU was being created. I examined the period before and after 1989 to understand the particular EMU design being chosen. In particular I was curious to find out why the emphasis was on a very well-developed 'monetary union', with the institutional design of EMU featuring a much less well-developed 'economic union'. My research suggested that trade unions were in decline and experts felt that welfare states needed to be restructured. Indeed I concluded that:

> '*the monetary implications of EMU* have been a primary influence in the process of creating EMU in Europe; policy makers did not scrutinize the potential effects of EMU on other policy areas such as national fiscal and social policies or the distribution of wealth across regions. In evaluating the validity of the hypothesis, the article has shown that the first part of the hypothesis, indeed, holds, although the second part needs to be revised. The results of this research demonstrate that the "Economic Union" is deliberately underdeveloped. Experts argued that they favoured EMU *exactly because* it would lead to a process of harmonization through market forces. EMU would offer legitimacy for restructuring the expensive welfare state. The "asymmetrical EMU", therefore, was a result of consensus among policy makers that further integration at this stage was only feasible in the realm of *monetary* policy making.' (Verdun, 1996: 80)

One might wonder why trade unions were complacent about the creation of EMU in light of these findings. Finding themselves marginalized, they were hoping that EMU, created under the leadership of Jacques Delors, would eventually feature a role for the social partners and that

1 On becoming UK Prime Minister in 1997, Labour leader Tony Blair adopted the Social Chapter, while upholding the EMU opt-out.

accompanying policy-making would develop to secure the social dimension of the EU or EMU. Indeed the British Trades Union Congress (TUC) linked its support of EMU to the acceptance of the Social Protocol (Verdun, 2000: 202). The French trade union CFDT was concerned that monetary objectives would trump all other objectives including fighting unemployment and a more equal distribution of wealth (Verdun, 2000: 202). The German trade union federation DGB stressed the importance of being at the table so as to develop further the 'economic' component of EMU (Verdun, 2000: 202). What was observed here was that trade unions had not only lost their privileged position that they had enjoyed in certain western European countries but that they were also increasingly losing prominence in the policy-making process. They hoped that the entire edifice of Europe would be seen as 'work in progress' and that the economic and social dimension would stay on or return to the agenda. Based on the study the following policy recommendation was articulated (Verdun, 1995, 2000):

> 'If this study had to advise the Member States, its recommendations to them would be that they should start reserving financial resources for the "costs" of EMU. *They should be aware that EMU could cost them more than they have been willing to accept*. If aggregate benefits of EMU are really significant, then these costs should on the whole not be too high for the Member States. It is naive to assume that one can only integrate monetary policy and leave harmonization of related policy areas to market forces, and be convinced that the domestic and European actors as well as national governments will be happy with the outcome. The belief is held here that EMU will eventually necessitate more integration of economic, fiscal, social and labour policies.' (Verdun, 1995: 343, 2000: 212)

Thus, a thorough analysis of the creation of EMU and the perceptions of the monetary experts around the table during the creation of EMU identified the need for deeper integration, flanking policies and funding at some point. The other concern, however, was how to ensure compliance with fiscal rules in the absence of an authority able to enforce rules once EMU had entered the third stage. Under German leadership, once the Treaty entered into force, the Stability and Growth Pact (SGP) was established to ensure compliance with the rules after the introduction of the euro (Heipertz and Verdun, 2010). It is remarkable that during the debates on the proposed Treaty establishing a Constitution for Europe, the issue of economic governance was never really on the agenda. The only institutional change of note was the formalization of the role of the Eurogroup (Puetter, 2006). With the SGP crisis of 2003 and its reform in 2005, again the economic governance discussion was not centre stage in EU circles, even though it was clear that EMU would not function properly without some form of budget and fiscal policy coordination (see Heipertz and Verdun, 2010).

Thus, at the start of EMU stage three on 1 January 1999, the concept of economic governance was not fully fleshed out (Verdun, 2003). Though various scholars had pointed to the need to have 'economic' and 'monetary' union go hand in hand, they differed in their understanding of what such 'economic governance' might imply. It could range from soft coordination of budgetary and fiscal policies, via budgetary deficit and public debt targets, to a much more ambitious understanding of cooperation, or even integration, in this field. In fact, the arrangement chosen was minimalistic: coordination through the so-called Stability and Growth Pact (limits on budgetary deficits with fairly weak instruments to enforce compliance). Those who thought that more economic governance might need to be developed one day alongside monetary union foresaw the need to transfer more tax revenue and spending power to an EU-level authority, and more firm coordination mechanisms at EU level, including possibly an increase in power to enforce compliance with these targets. What this would mean for the social dimension was also not clear. Again there was a range of opinions, and again, the arrangement ultimately agreed upon was very decentralized, leaving very little role for the EU level. While some thought that – even with deeper economic integration – social policy should remain completely at national level, others felt that deeper economic governance might need to be accompanied by greater control of wages and social spending. Some even wondered whether more social spending would need to be coordinated at EU level. But in all cases, these matters were far from settled. Any ideas on taking action on these issues were postponed, with the view being held that if and when a crisis necessitating action emerged, such time would be soon enough to deal with these matters.

Why economic governance?

Why is there a need for an economic government or some sort of economic governance? In mature federal states economic policies, such as monetary and fiscal policies, are conducted in tandem, with the former influencing money supply and the latter determining how much a government can tax and spend. In combination, the two provide favourable economic conditions in a country. EU history shows that Member States have been able to agree on the need for fixed exchange rates and have benefited from fixed exchange regimes for some time. Also during this time, Member States followed the lead of the German Bundesbank and in this way coordinated central bank policies. Yet, the accompanying need for economic governance of budgetary and fiscal policies has remained a national prerogative. In part the problem is political. Though it is relatively easy to transfer sovereignty to an independent monetary authority – a central bank – and provide it with the fairly simple mandate of ensuring price stability and providing support for the Union's economic objectives, it is much more difficult to transfer responsibility for budgetary deficits and public debt to the European Commission, allowing it to take non-political, technocratic decisions over these macroeconomic indicators. To date, all that has happened is that leaders – at the level of the Heads of States and Governments and at the Council of Ministers / Council of the EU – have reached agreement on what the numerical criteria should be for budgetary deficits and public debts. But again, that is only part of the coordination needed to coordinate economic policy-making.

The literature suggests that when a country is in a monetary union the chances are that it will find itself needing a government body similar to what in the United States (US) is called a 'treasury' (a 'European Ministry of Finance'). At a minimum the European Commission needs to be invested with more powers to tax and spend (Eichengreen, 2012; see also Verdun, 1996, 2003). Furthermore, in recent years it has become clear that part of the problem is that it is not very credible to have the simple numerical targets for budgetary deficits (close-to-balance-or-in-surplus) for the immediate budgetary cycle. As economic conditions worsen, it makes more sense to run a deficit possibly exceeding the 3 per cent rule. In addition, when the original SGP was created, the decision was taken to focus on the budgetary deficit (rather than the public debt) criterion because it was the one that elected politicians could be held accountable for. The larger problem was posed by countries with large public debts (especially those countries that had a debt to GDP ratio of over 100 per cent). Recently, with the ongoing sovereign debt crisis, it has become clear that not only budgetary deficits and public debt are of relevance, but also the state of the banking sector. In a union in which capital is free and the banking sector is highly integrated, problems in the banking sector in one country can easily generate a crisis in another country because money is so very mobile, with the cost of transferring funds to another bank denominated in the same currency in another country relatively low.

EMU and the crises

The crises of 2007 to the present have severely shaken the EU, highlighting the failure of the EU's economic and monetary architecture. It is once again important to stress that EMU design was purposely left incomplete, with the strategy being to wait until it became clear that some form of EU action would be needed. Even so, the onset of the crises left many shocked. Few had expected that the crises would set off such a major soul-searching exercise in the EU. Let us start by briefly describing the various crises and then turn to the EU responses to them.

The financial crisis started in summer 2007, when the credit market dried up (Verdun, 2012). It was further aggravated by various events, the most noteworthy being the bankruptcy of Lehman Brothers on 15 September 2008. In its wake, stock exchanges fell and company access to credit became increasingly difficult. With the worst of the financial crisis over, advanced economies faced a major recession taking hold during 2009. Governments had been responding to the crisis by spending money – which they did not have. The result was a sovereign debt crisis that started in 2010 and is still ongoing at the time of writing. The latter has triggered an existential crisis within the EU, bringing to the surface the EMU design flaws and more particularly the lack of a common vision on the solutions needed to combat the crisis. The EU is currently facing what Shambaugh (2012) has called three crises: a banking crisis (banks are undercapitalized), a sovereign debt crisis (public debt and budgetary deficits in many Member States are too high), and a growth crisis. I would add to this that the growth crisis is in fact a lack of economic activity crisis – manifested by high unemployment rates in many EU Member States and extremely high youth unemployment – in particular in southern Europe.

The EU response (Commission and Council) to the financial and economic crises was rather slow. By contrast, the European Central Bank (ECB) moved quickly (see Drudi et al., 2012), making available credit in unprecedented amounts and without onerous restrictions right at the start of the financial crisis in August 2007. Similarly, it participated in various coordinated interest rate decisions with other major central banks. The lack of Commission/Council decisions, however, prompted Member States to take unilateral action. On entering the sovereign debt stage, the situation deteriorated still further. The EU had difficulties deciding what to do. There were a number of reasons for this lack of speedy response, among them the so-called 'no-bailout clause' which meant that Member States were unable to assist another Member State faced with public debt problems. Also, it was concerned about moral hazard: how to assist a country in difficulties, while at the same time ensuring that the problems would not recur in the future. A final concern was that these problems had emerged on account of EMU's imperfect institutional design. The implication was that the response had somehow to include a revamping of the institutional governance structure (Eichengreen, 2012). The problem was that deeper integration typically requires permissive consensus for European integration. At this time, however, it was felt that such a permissive consensus would not be attainable among all 27 Member States. Hence the impasse that followed.

How did the EU respond? At the end of the day, a number of major decisions were taken by the EU Member States acting in concert. First, a general stance was developed in the context of the Europe 2020 strategy. This strategy was to follow the so-called Lisbon strategy (which had been formulated in 2000) that stipulated as its goal to have the EU become the most competitive economy by 2010 offering a fairly informal framework for socio-economic policy coordination. As the Lisbon strategy before it, the Europe 2020 strategy had elements that sought to target employment, social inclusion, growth and sustainability. Although nice goals, some scholars find this strategy for the most part nothing more than a window-dressing exercise (see Degryse and Natali, 2011).

The EU also sought to deal with the particular sovereign debt crisis. In May 2010 the EU assisted in bailing out Greece. Together with the International Monetary Fund (IMF), the Member States provided Greece with €110bn in loans, with the Greek government agreeing to austerity measures in return. On 9 May 2010 the Council of ministers of economic and financial affairs (Ecofin Council) announced the creation of a European Financial Stability Facility (EFSF). Member States acting in their intergovernmental capacity agreed to provide it with €440bn for loans to ailing Member States and the IMF also agreed to earmark another €250bn. Soon other Member States, including Ireland and Portugal, needed assistance, being at risk of defaulting on their debt obligations. In October 2011, EFSF funds were expanded to €1000bn (€1trn). At the European Council of 21 March 2011, the decision was taken to create a permanent fund, the European Stability Mechanism, to replace the EFSF by 1 July 2013. To do so, they agreed to a minor Treaty amendment.[2] In December 2011 the European Council decided to bring the date forward to 1 July 2012. In September 2012 the German Constitutional Court in Karlsruhe ruled that the ESM is in accordance with the German constitution and it was inaugurated in Luxembourg on 8 October 2012. In March 2012 Greece needed support again. This time it managed to secure a major restructuring of its debt (the biggest in history). By the end of June Spain also needed support, with its ailing banks being provided directly with credit.

Various other changes were made that have an impact on EMU governance. Earlier, in March 2011, the Council agreed to revise and tighten SGP rules, via its 'six-pack' (five regulations and one directive). These rules include such features as the Reverse Qualified Majority Vote (RQMV) which means that it now requires a Qualified Majority Vote (QMV) *to undo* proposals put forward by the Commission, thereby making it more difficult to undo corrective measures. The bottom line is a stricter application of SGP rules.

In December 2011 an intergovernmental treaty was agreed to by 25 of the 27 Member States. This agreement is formally called the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG). It is commonly referred to as the Fiscal Compact. This treaty enters into force when at least 12 Member States of the euro area ratify it and is only binding on those Member States that have adopted the euro. The TSCG imposes stricter compliance with the rules in a number of ways: for instance, the European Court of Justice (ECJ) may impose sanctions of up to 0.1 per cent of the GDP of the Member State in question for not complying with the new budget rules.

Finally, a new instrument, the European Semester, has been introduced to coordinate and monitor developments in Member States during a six-month cycle. It assists in coordinating economic policies in Member States and has been streamlined to support the further strengthening of the SGP. The European Semester was a response in part to the Europe 2020 initiative (to become more competitive). It also focused on the goal of creating growth, jobs and social inclusion. Recommendations from the Commission to Member States' national plans focus among other things on the social dimension (ensuring for instance that Member State national governments adopt policies addressing unemployment, low labour participation, pensions, etc.). This development constitutes a major change, and scholars are divided on the question of whether this

2 In order to create the ESM, the Treaty on the Functioning of the European Union had to be amended. The European Council adopted an amended Article 136 by adding a paragraph 'The Member States whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality.' This clause would only formally enter into force when ratified by 21 Member States. For a discussion of the legal provisions of the measures around the EFSF and the ESM see De Witte (2011).

development is positive (the Commission putting pressure on national governments to ensure social goals) or more negative (does the Commission have the legitimacy to tell a Member State government what to do in this policy area – to which I will return in the next section).

What this section has shown is that the crises of 2007 up to the present have signalled the need for the EU to move towards deeper integration, counteracting the risk of the European Union falling apart or of certain policy areas disintegrating in which to date major developments have taken place. The EMU architects failed to appreciate that it could be politically very difficult to deepen integration in a crisis when there is a lack of permissive consensus on the part of the people. Thus, although many can point to some possible developments that need to be made to offset the problems of the crisis, the lack of political will of the people and the challenge to EU leadership imply that this task is much more difficult than was originally anticipated when EMU was being designed. Not only is economic governance a concept that requires a transfer of sovereignty, but also the lack of any clear vision of the social dimension needed to accompany deeper economic integration remains a major challenge to the EU.

Implications of the new governance architecture

The EU's revised economic governance architecture may very well lead to closer coordination of economic policies. However, concerns have been raised by academics and policy analysts alike that these new rules may not have incorporated enough room for various actors who typically play a role in the policy-making process. Have provisions for good governance been made? What are the implications for social partners, wage bargaining and the welfare state?

In terms of good governance, the new architecture may very well need to be adjusted to some extent. Hallerberg et al. (2011) argue that the European Semester has far-reaching implications, but that the democratic accountability process may be lacking. They argue that in this context the Commission and the Council should be kept in check by the European Parliament – the reason being that the roles of the former two are quite substantial in the policy-making process. However, no such provision has been made.

As for the implications for social partners, the new architecture has not focused too much attention on giving the social partners any formal role. Typically, over the past two decades, as highlighted above, no major formal role had been accorded to the social partners at EU level (even if in the 1960s that role was still deemed substantial). Instead, the social partners were invited, and indeed participated in the policy process at national level. While the social partners were naturally involved in EU policy-making at large, they were not necessarily formally incorporated at EU level with respect to economic and monetary policy-making. With a move from a national to a more substantial EU role in economic coordination, one wonders how these actors may be able to play a role (see also Hancké, in this issue). The new rules on economic governance may require Member States to make major changes to their macroeconomic governance but under directions issued by EU institutions. What might be the implications? Will we see the Commission and Council telling Member States to cut wages, reduce public sector employment, or issuing other labour policy-related recommendations? An early analysis of the renewed SGP and the European Semester gives the impression that, should Member States fail to meet the SGP threshold criteria, the Commission may indeed issue such recommendations. In that context, it would make sense for the economic governance structure to include a larger role for social partner consultation. It seems that the new architecture may well put considerable strain on wage bargaining at the national level, in particular if aggregate macroeconomic statistics turn out to differ significantly from what had been anticipated.

With regard to the welfare state, what might be the result? Strictly speaking, nothing in the new economic governance architecture necessarily restricts the welfare state spending of any given state. In fact, there are considerable differences between Member States. The concern uttered by those who have been advocating the protection of the 'European Model of Society' and the European welfare state is that with large budget cuts and the need to ensure that public debt stay within the agreed limits, any room for manoeuvre becomes more limited, meaning that governments will have to make careful trade-offs between taxing and spending. This will put pressure on all forms of state spending. Thus, even if the welfare state is not a target, those who are concerned that the welfare state might come under pressure do have a point.

Conclusion

Ever since the first blueprints of economic and monetary union were published, there have been questions about the exact interaction between economic and monetary integration. There has been many a vision as to what economic governance or economic integration means. In the 1960s, in a different era, a larger role for supranational governance including a role for social partners had been envisaged. By the late 1980s economic governance was to be attained without major centralization and transfer of powers to a supranational body, and social matters became divorced from economic and monetary unification plans. Coordination of 'economic governance' (budgetary and fiscal policy) was to be achieved via rules and social matters were considered the responsibility of Member States. Despite Delors' original inclination, few were willing to establish any formal linkage between EMU and a need to consider social matters (other than that of course the Social Chapter and EMU emerged in the Maastricht Treaty at the same time; but the two were not connected to each other as such). Shortly after the EMU blueprint was incorporated into the Treaty, it became clear that further rules were necessary – hence the creation of the SGP. The 2000s demonstrated the political fragility of the rules-based system, with Member States easily able to undermine it. Those discussing EMU in depth kept implications for social matters off the agenda. Such matters were considered separate agendas and there were few advocates seeking to link EMU with the need to consider the social dimension.

With the financial, economic and sovereign debt crises, the need for economic governance has become extremely clear. The challenge is how to construct it. The EU's new institutional architecture envisages stricter rules, a larger role for EU institutions in enforcing these rules, and penalties for those not meeting the criteria. Even so, the EU baulked at setting up fully-fledged governance structures at EU level, with the expectation still being that Member States will simply meet the criteria. If not, there will be guidance, instructions, and possibly sanctions imposed by EU institutions.

The social dimension has been all but forgotten as an element of EMU and economic governance. With the results of the crises now pointing to mass unemployment and unacceptably high levels of youth unemployment, it is becoming obvious that EMU and the social dimension must be looked at in tandem. A stronger role in the policy-making process needs to be played by various actors not as yet actively involved in EU-level EMU governance. For instance, social partners and other advocates of the 'European Model of Society' and welfare states have seen their work mainly confined to the national level. With the establishment of the European Semester, the EU economic governance model is now also beginning to focus on social matters, presenting the opportunity to expand the role of the social partners at EU level.

With the increased role in economic governance accorded to EU-level institutions, there is a need to rethink the EU democratic model. The currently envisaged model without the checks and balances of democratic institutions (European Parliament) and other institutional stakeholders (the social partners) may not benefit the EU in the long run. It is to be hoped that the EU will remain open to considering how best to ensure good governance in the EU context as it evaluates the pros and cons of the new economic governance architecture in the EU.

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