

Research Fellowship Programme - Future of the EMU

Essay on The political economy of EMU: political union, transfer of sovereignty and social compact

Background

The euro-area sovereign debt crisis has increasingly brought to the fore the challenge of national interdependence in the wake of the economic and financial crisis. While trade and financial linkages have always implied a certain degree of interdependence across the euro area, even in pre-crisis periods, the different stages of the crises since 2007 have widened and intensified national spillovers, coordination problems and cross-border liability. The financial and sovereign crises have already brought comprehensive changes in the euro-area / EU policy framework, including a considerable reinforcement of macroeconomic and budgetary surveillance with a set of more automatic sanctions and the obligation for euro-area Member States to transpose some of the constraints of EU fiscal discipline into national legislation. A decisive step is arguably the creation of macro-financial assistance programmes, beginning with Greece in May 2010 and later also spanning Ireland and Portugal. These programmes represent an explicit departure from the pre-crisis premise of fiscal self-reliance, as evidenced by the joint EU/IMF assistance programmes and the EFSF and ESM 'firewalls', for which joint guarantees and/or capital shares directly measure the extent of burden sharing between Member States. From a theoretical perspective, these developments have added overt supranational facets to domestic economic policy throughout the euro area.

Aims of the essay and key questions to be tackled

The overarching aim of the essay is to take stock of the changes in economic and financial policy issues in the euro area in terms of their implications for national policy autonomy, and to examine the extent to which a smooth functioning of EMU requires further transfers of national sovereignty in these areas, and potentially even beyond them. In particular, the essay should analyse in depth the following issues and questions:

- Is there a need for further fiscal integration, and what form(s) should it take? In particular, under which conditions and to what extent is some burden-sharing for sovereign debt warranted that goes beyond the assistance measures currently in place or under discussion (i.e. EFSF, ESM and stability bonds)? How far towards a centralised system of taxation and fiscal transfers should one go, what are the potential benefits and risks (including in terms of moral hazard and the potential loss of market signals), and what forms could this take? How would potential proposals fit in with the current architecture of fiscal surveillance?

- On what basis could the case be made that greater fiscal integration should be accompanied by more political and social integration, for instance through a 'social compact' covering e.g. welfare or labour market issues? What would be the costs and benefits? Would some integration in these areas be a necessary condition for a deeper fiscal union, and if so, what criteria should integration in these areas fulfil?

- In what sense has the euro-area's comprehensive crisis response affected power relations in EU and euro-area economic policy making? In how far would deeper political and social integration affect the role of national parliaments? What would be the implications for

democratic accountability and legitimacy of further integration, and what are the ramifications of such quasi-federalist changes at the citizen's level? What would be the implications for the relationship between euro and non-euro countries in the EU.