European University Institute

ROBERT SCHUMAN CENTRE FOR ADVANCED STUDIES

Responses of European Economic Cultures to Europe's Crisis Politics: The Example of German-Italian Discrepancies

Edited by:
Josef Hien and Christian Joerges

This work has been published by the European University Institute,
Robert Schuman Centre for Advanced Studies.

doi:10.2870/83554
ISBN:978-92-9084-711-3
QM-05-18-106-EN-N

Publications Office

With the support of the
Erasmus+ Programme
of the European Union

RESPONSES OF EUROPEAN ECONOMIC CULTURES TO EUROPE'S CRISIS POLITICS: THE EXAMPLE OF GERMAN-ITALIAN DISCREPANCIES

Edited by:
Josef Hien and
Christian Joerges

TABLE OF CONTENTS

D) The Legacy of the Welfare State in Europe

E) The Demise of Law

F) Justice Deficits and Solidarity

Summarising Comments

Two Annexes

ACKNOWLEDGEMENTS

We had excellent support for this project from both sides of the Alps. In particular, we want to thank the DAAD for trusting us to do something meaningful with the money that we won in the framework of the "Hochschuldialog mit Südeuropa, 2018". Second, a big thanks goes to all members of the ERC-funded REScEU project at the University of Milan, especially, the Principal Investigator Maurizio Ferrera, who REScEUed us from a small financial disaster, and without whom all this would have never happened.[1] Third, we wish to thank the Villa Vigoni for providing the most fantastic setting, food and administrative support imaginable for the conference. Fourth, we want to thank Brigid Laffan at the Robert Schumann Centre of the European University Institute for giving us a platform for publication. Fifth, we are deeply grateful to Ines Andre-Schulze for her administrative support and the third-party funding bureau at the Hertie School of Governance in Berlin. A cheer for our tireless language editor Chris Engert and to our beloved ones.

Josef Hien and Christian Joerges, Stockholm/ Milan and Bremen/Berlin, October 2018

1 The work of Josef Hien for this collection has been carried out within the framework of the REScEU project (REScEU: Reconciling Economic and Social Europe: the role of ideas, values and politics) hosted at the University of Milan and financed by the European Research Council (grant no. 340534). Josef Hien also wants to thank the Institute for Future Studies in Stockholm, Stefan Svallfors and Gustaf Arrhenius who have hosted him as a guest during the late stage of this project.

INTRODUCTORY EXPLANATIONS

I. Political Turmoil

When we started our preparation for this project only a year ago, our prime concerns were the deepening of the social and economic asymmetries between the North and the South under the impact of the financial crisis, with Germany and Italy providing an example of existential importance for the EU as a whole. Both of us had resided in the two countries for prolonged periods in the past, and we had never witnessed such a surge in antagonistic feelings on both sides of the Alps as occurred during the Euro crisis. This can even be measured: while it had been common in Germany, at the beginning of the crisis, to talk about the PIIGS states (Portugal, Ireland, Italy, Greece and Spain), with Italy figuring among them as an important member,[2] the percentage of Italians having a positive image of Germany crashed only from 75 to 65 per cent during the immediate crisis period, and now the majority of the Italians thinks that Germany has too much influence in Europe and that it uses this influence at the expense of Southern Member States.[3] While our application for funding was still pending, we witnessed two crucial events that increased the pertinence of our project way beyond our expectations. First, on the 24 September 2017, for the first time in post-war German history, a far right party entered the German *Bundestag* with a landslide victory, receiving 14 per cent of the popular vote and 100 parliamentary seats. Second, only five months later in Italy, the far-right *Lega* party and the *Movimento Cinque Stelle* emerged as the big winners from the Italian federal elections of the 4th of

2 This notion has disappeared from the public discourse; it re-surfaced somewhat modified in Commissioner Oettingers comments on the plans of the present Italian government; see, for references, the contribution of K. Mangold, F 1.

3 Olmastroni, F. / Pellegata, A. (2017): Once we were friends. EU support and reciprocal views between Germany and Italy. http://www.euvisions.eu/friends-support-reciprocal.

March 2018. Forming a previously unthinkable coalition between right-wing and left-wing populism, they entered into government. We are not so naïve as to believe that the variety of Europe's crises could be understood and adequately analysed as though these were isolated events. The course of Italy's economic and social policy has so obviously been affected by the migration burdens that Italy has had to shoulder and the lack of European solidarity; the bitter disappointment could be turned into populist critique of the constraints that European rule imposes upon national policies and the public announcement of disobedience by members of the Italian government. In a similar vein, the *Alternative für Deutschland* (*AfD*) in Germany had been founded as an anti-Euro rescue party, which catalysed quickly through the immigration crisis of 2015 into a xenophobic far-right populist party, sharing many positions with the Italian *Lega*. While the parties and alliances in both countries had capitalised very much upon the antagonisms between Italy and Germany and their positions during the Euro crisis by building on nationalist sentiments, today we have reached a true anti-climax when one observes that the intensification of tensions are accompanied by the founding of new alliances and a contagion towards formerly non-populist and non-far right parties in both countries: "Europe does not want migrants, it wants our money" (Luigi Di Maio); "Migration is the Mother of all problems" (Horst Seehofer). Both the *AfD* in Germany and the *Lega* in Italy share two major targets against which they direct their rage: European integration, especially in the economic realm, and immigration. We refrain, however, from attempting to disentangle all these interdependencies, but hope that our study of the two exemplary cases of Italy and Germany will provide us with some answers to the question of what led us down this road. We believe that the approach which we have pursued in our design of this project provides illuminating insights of lasting importance.

II. The Challenge of European Varieties

It is difficult to identify uncontroversial statements in the crisis literature. Among them, however, is the - at first sight - counter-intuitive *factum brutum* that, notwithstanding the enormous efforts of Europe's crisis politics, the economies and welfare systems of the EU did not converge, these differences became instead more pronounced. We owe the most influential explanations of this phenomenon to the Varieties of Capitalism (VoC) studies initiated by the seminal volume of Peter A. Hall and David Soskice.[4] Their message was that different countries in Europe have developed different institutional complementarities that give them specific economic advantages.[5] The crisis drastically showcased a strong variety of this within the co-ordinated market economies of Europe. VoC scholars amended their theories, underlining the differences in wage-bargaining regimes or union-membership density between Northern and Southern countries. What the original VoC literature had neglected was that all European co-ordinated market economies had been subject to far-reaching trends of liberalisation since the 1980s that had been enacted to overcome the low growth of the stagflation crisis of the late 1970s. All countries liberalised, albeit in very different ways which set them on very different growth paths in the 1990s and 2000s. From these findings the new growth model literature emerged, pointing especially to the divergences between the Southern, internal demand-driven growth led, and the Northern, external demand-driven growth led Member States of the EU/Eurozone. The EMU, with its hard currency approach, benefits some of these models but puts stress on

4 Hall, P.A., and Soskice, D. (2001): *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*, Oxford: Oxford University Press.

5 Hall, Peter A. (2014): "Varieties of Capitalism and the Euro Crisis", *West European Politics* 37 (6) (August 14): 1223-1243: id., (2012): "The Economics and Politics of the Euro Crisis", *German Politics*, 21:4, 355-371.

others.[6] Even the Commission, traditionally a fierce defendant of the convergence approach, has recently underlined European diversities. In its White Paper for a multi-speed Europe, it pleads for differentiated integration.[7] The merits of the Varieties of Capitalism approach, upon which the scholarly debate builds, are, in many respects, undeniable. However, we distance ourselves from the one-dimensional reliance on efficiency considerations in the evaluation of institutional complementarities.[8] In a similar vein, we also think that the material interest kernel of the growth model perspective is still incomplete. We believe that more attention should be devoted to the ideational and cultural side of the diversities of Europe's organised types of capitalism. These diversities span across the fields of economic, social and legal theory, and have evolved in iterative relation with norms, institutions, politics, and cultural historical trajectories for centuries. The economy unfolds not only within a set of institutions that are rationally trimmed to maximise profits, but these institutions themselves evolve within a cultural environment composed of ideas, ideologies, traditions and the collective sentiments of their people.

Could such a broadening of analytical perspectives help us to understand better why the asymmetry between the North and the South of Europe has re-erupted and become a core problem for the European integration project?[9] This is the query which we sought to pursue with the help of the contributors to the Vigoni conference. It is a long-term agenda. We could not, and did not, expect a comprehensive coverage of the many aspects and dimensions of the diverging socio-economic approaches and needs in both Southern and Northern Europe, or an ideational convergence of the analyses which our contributors were invited to submit. We would, however, like to substantiate our own move from the varieties and growth model studies in order to a focus on economic cultures. This move is anything but idiosyncratic. The concept of "economic cultures" has been defined and defended by both economic historians[10] and path-breaking comparative law scholarship.[11] One important aspect which is underlined in both disciplines is the resistance of economic cultures against the imposition of changes, which can render interventions meaningless or even destructive. Werner Abelshauser submits that the imposition of structural reforms through which Europe's crisis politics seeks to accomplish socio-economic convergence risks, instead, de-stabilising the targeted economies further.[12] Gunther Teubner has submitted corresponding objec-

6 Armingeon, K., Guthmann, K., and Weisstanner, D. (2015): "How the Euro Divides the Union: The Effect of Economic Adjustment on Support for Democracy in Europe", *Socio-Economic Review* 14(1): 1 26. First published online: 12 November 2015. DOI: 10.1093/ser/mwv028; see, also, Armingeon, K., and Baccaro, L. (2014): "Germania: l'indomabile trading state", *Quaderni di rassegna sindacale - Lavori*[check]", 15: 2, 19-45; English version: Armingeon, K., and Baccaro, L. (2014): "The Crisis and Germany: The Trading State Unleashed", in: Eberlein, B., and Schneider, V. (eds): *Complex Democracy. Varieties, Crisis, and Transformations*, Wiesbaden: Springer VS, 165-184.

7 "White paper on the future of Europe. Reflections and scenarios for the EU27 by 2025", COM(2017) 2025 of 1 March 2017. See, for a scholarly discussion, Schmidt, V. (2017): "Inventing a New Future for Europe: Differentiated Integration with more EU and more Member-States?", Ms. Boston (on file with authors).

8 Streeck, W. (2005): "Requirements for a useful Concept of Complementarity", in: Crouch, C., Streeck, W., Boyer, R., Amable, B., Hall, P.A., and Jackson, G., "Dialogue on 'Institutional Complementarities and Political Economy'", *Socio Economic Review* 3, 359-382.

9 See, recently, Scharpf, F.W. (2016): "Forced Structural Convergence in the Eurozone - Or a Differentiated European Monetary Community", MPIfG Discussion Paper 16/15, available at: http://www.mpi-fg-koeln.mpg.de/pu/mpifg_dp/dp16-15.pdf (last accessed 21 June 2017).

10 Abelshauser, W. (2003): *Kulturkampf: Der deutsche Weg in die Neue Wirtschaft und die amerikanische Herausforderung*, Berlin: Kadmos. Abelshauser, W., Gilgen, D. and Leutzsch, A. (eds) (2013), *Kulturen der Weltwirtschaft*, Göttingen: Vandenhoek und Ruprecht.

11 Teubner, G. (2001): "How Unifying Law Ends Up in New Differences", in: Hall. P.A., and Soskice, D. (eds), *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*, Oxford: Oxford University Press, 417-441.

12 Abelshauser, W. (2018): "Europa in Vielfalt einigen. Eine Denkschrift", in: Atkinson, A.B., Huber, P.M., James, H., Scharpf, F.W. (eds), *Nationalstaat und Europäische Union. Eine Bestandsaufnahme*, Baden-Baden: Nomos, 2016, 275-294, available at: http://wwwhomes.uni-bielefeld.de/wabelsha/Denkschrift.pdf (last accessed 21 June 2017); id., "Viele Wege führen nach Rom", FAZ, Nr. 61, 30.3.2017, 6.

tions against legal unification politics.[13] Both of them refrain - in this respect fully in line with the messages of VoC studies - from a ranking of the models that they have discerned; they highlight their specific advantages, instead. The difference is that the economic cultures approach does not solely focus on institutional configurations (VoC) and sectoral interests (growth models) but also includes a distinctively historical perspective that sheds light on the political evolution of these economies and how it is embedded in national cultures, traditions, and economic ideas.[14] Moreover, while VoC research is firmly in the hands of political economists and sociologists, the notion of economic cultures is more integrative, synthesising history, law, politics, sociology, anthropology, and cognitive science. It seems to us to be especially odd that law is left by the wayside in most political and social analyses of European forms of capitalism. We ask ourselves, how should the abundance of proposals to better the socio-economic aspects of the state of integration be put into practice without thinking through their legal practicality and implementation. Accordingly, one of the objectives of our conference was to build a bridge between the VoC, the growth model, and the economic cultures perspectives.

What we suggest is that Europe should stop lamenting about its diversity. It should, instead, learn to take the fortunate motto of the ill-fated constitutional Treaty of 2004 seriously and learn to establish its *unitas in diversitate*.[15] We even expect that this learning process has the potential to generate political, social and economic benefits.

13 N. 10 above.

14 Another leading authority in this regard is Alexander Nützenadel, whose research includes intensive studies of the Italian economy; suffice it here to name two projects: "Programmare il miracolo economico?" Industriepolitik in Italienzwischen Boom und Krise, 1958-1973", (DFG, 2011-2013); "Experience and Expectation: Historical Foundations of Economic Behavior", (DFG, 2015-2022); see https://www.geschichte.hu-berlin.de/de/bereiche-und-lehrstuehle/sozial-wirtschaftsgeschichte/forschung (last accessed 21 June 2017).

15 CT 2ßß4 by Motto of the Draft Constitutional Treaty 2004

III. The Individual Contributions

Our overriding concern is a renewal of the debate on Europe's diversity. The challenges are manifold. We distinguish between thematic, conceptual, and normative dimensions. What is certainly not unique, but still quite innovative about our agenda is the multi-dimensional approach to the integration process. We deal with "Europeanisation" in the conventional sense of the establishment of European rules, policies, and governance practices. The EU, we have internalised this message since way back, is a multi-level system. We are, of course, also aware of implementation studies which have highlighted the failings or unevenness of the European *praxis*. Our focus on the German-Italian discrepancies highlights a phenomenon which the "ever more Europe" mantra of European studies tends to neglect. "More Europe" has an discomforting destructive potential. What is perceived as a new accomplishment of the process may generate disintegrative effects.[16] Indeed, what we document is that our two cases, Italy and Germany, have, in the structure of their economies, not converged, but rather grown apart since Maastricht. What we highlight is that disintegration is not only bad within a Member State, but may also – and here the tensions between Italy and Germany are of exemplary importance – affect the Union as a whole: the "ever closer Union" is characterised by ever more hostility. Last, but not least, we have to take into account what is left of the political "ownership" of the Member States. We disagree with qualifications of this residual power as an obstacle to smooth implementation. We believe that it would, instead, be important to

16 See, for a general debate, Annegret Eppler and Henrik Scheller (eds), *Europäische Desintegration in Zeiten der Krise. Zur Konzeptionalisierung europäischer Desintegration*, Baden-Baden: Nomos 2013; on the case of EMU, see Fritz W. Scharpf, "The Costs of Non-disintegration: The Case of the European Monetary Union", in: Chalmers, D., Jachtenfuchs, M., and Joerges, C. (eds), *The End of the Eurocrats' Dream: Adjusting to European Diversity*, Cambridge: Cambridge University Press, 2016, 29-49.

take cultural diversities into account.[17]

This latter observation concerns our core theoretical message to which we will return in the following comments on the individual contributions.

A) The political economy of Germany and Italy

Today, we have a plethora of rivalling explanations of why the Eurozone crisis happened.[18] All of them agree on one point: the currency union was too heterogeneous for a single currency. But what is it really that makes these economies and their demands to a common regulatory framework, market and currency so different and have they converged over time? In Part One of our collection, we unleash five political economists to come to terms with this question, by comparing the Italian and German political economies.

Philip Manow[19] gives us a meticulous account of the transformation of the German political economy during the past twenty years. He argues that the tradition of supply-side corporatism in Germany enabled socio-economic actors to co-ordinate wage restraint and to embark on painstaking structural reforms that, together, successfully transitioned the German economy from its position as sick man to that of the strong man of Europe during the 2000s and 2010s. Here, Manow defends the German reforms against many internal and external critics by arguing that it has led to "dualisation" but not to a decrease in the social protection of the core of the workforce. Moreover, in contrast to what the critics anticipated, the structural reforms did not lead to a deterioration of the well-protected core of the workforce, but, instead, made it larger. Today, Germany has, together with Sweden, the second most active workforce, and differs, in this respect, remarkably from Italy. Manow acknowledges that the transformation of the German model has put severe stress on the Southern European political economies. Germany had a tradition of coping with hard currency while the demand-led regimes of the South are penalised by the Euro. They cannot devaluate any longer. The introduction of the Euro and the Eurozone crisis have cemented these two different political economic models in Europe: an export-oriented Northern model and an internal-demand-driven Southern model. Manow sees two ways forward for the Eurozone: 1. Painstaking structural reforms in the South backed through heavy transfers form the North or, 2. The split of the Eurozone into two different currency zones.

Donato Di Carlo challenges this view and the underlying assumptions of the growth model perspective in Manow's account. Comparing wage development and wage-setting institutions for the public sector in Italy and Germany, he points out that it is not wage restraint and co-ordination between the social partners which led to the freezing of public sector wages in Germany but the idiosyncratic wage-setting dynamics in German federalism. In Italy, in contrast, he argues it is not due to un-coordinated bids by multiple trade unions that first strongly increased and later cut public-sector wages, but, instead, the political geography of Italy, where parties in the South must rely heavily on the votes form public-sector employees, which is decisive. The implications elaborated in Di Carlo's study for the current trend in political economy, towards the growth model perspective, are huge: wage restraint is not part of an intelligent design. A growth model

17 As we will underline, the trenches between the disciplines are as deep as ever; there are very few lawyers who have followed the Variety of Capitalism studies. Among the few, the most famous is Gunther Teubner. His discovery of the resistance of legal cultures against imposed unification ("Legal Irritants: Good Faith in British Law", (1998) 61 *Modern Law Review*, 11-32) was re-published at the best conceivable location: see n.10 above.

18 The latest account we became aware of is Ashoka Mody's EuroTragedy. A Drama in Nine Acts, Oxford, OUP, 2018. Ashoka's reconstructions reach far beyond economic occurences. His chapter 8 on Italy (pp. 318-360) documents his precise awareness of the specifics of Italy's institutional and political constellations - and their apparently irresolvable problems.

19 Philip, Manow, "The German Political Economy under the Euro – and a Comparison to the 'Southern Model'", (2018), A 1.

or regime does not exist; instead, unintended outcomes created through institutional configurations of the German polity (federalism) conditioned parts of the new export-orientation of the German economy. Hence, also the accusations from Southern European countries waged against the German export surplus fall short. The co-ordination power that the growth model perspective ascribes to all actors does not exist. Di Carlo returns to this with a second contribution in the Annex.[20]

Margarita Estevez-Abe, who is among the originators of the Varieties of Capitalism school, provides us with a glance form the outside helping us to come to terms with the controversial discussion about the German export-led growth regime.[21] Using Japan as a counterfactual allows her to control for the impact of a unified currency zone. Estevez-Abe shows that Germany does not only hide behind the EU when it gets accused of trade deficits by the US and other international actors but that Germany, benefited enormously form the Euro. The Euro made German exports cheaper. Hence, the German role within the single currency has not only led to tensions between North and South in Europe but has triggered heavy geo-political stress. Merkel's reply to Donald Trump cited as the opener in Estevez-Abe's fascinating study nails it: "You can't do a trade deal with Germany, only the EU."

While the first three contributions to this volume deal with economic institutions (Manow), political institutions (Di Carlo) and economic interests (Estevez-Abe), Federico Bruno analyses in the fourth contribution the prevalent economic ideas that led Italy and Germany into the formation of the Eurozone and guided them through the economic crisis.[22] Assessing the explanatory value of idiosyncratic socio-economic ideas such as ordoliberalism and Italian style Keynesianism, Bruno concludes that the influence of ideas can only be understood if they are put into the context of the political landscape and electoral coalitions in both countries. Like Di Carlo, Bruno points at the importance of political and electoral coalitions for Italian Eurozone positions. The focus is hereby on the political split of the country between North and South. National traditions of economic thought matter, not as direct causal factors, but because they are used as cues to the electorate.

What we have assembled so far are contributions from different analytical and methodological angles in which institutions, interests and ideas all feature separately as explanatory variables. This calls for synthetisation. In the last contribution to Part One, Josef Hien introduces the concept of cultural political economy to integrate the above laid out approaches to the crisis.[23] For the rest of social science, culture as an explanatory variable is (often not unfoundedly), accused of being a residual category that is evoked when all other explanations fail. However, the strength of a cultural political economy is that it can integrate the trichotomy between institutions, interests, and ideas. As in Weber's famous switchmen metaphor, it is not interest, ideas or institutions that determine action, but all of them together. When interest, institutions and ideas all point in the same direction, they form a self-reinforcing compound, an amalgam that is very hard to overcome or to break up, even for a superpower like the EU. Hien uses neo-Weberian theory to build an integrative analytical framework to explain from a long-term historical-sociological perspective why Italy and Germany seem to be set on different tracks. With a special focus on the diverging cultural background of both countries, Hien re-constructs the pathways of both political economies since the 1950s, explaining how they could end up in such different positions today.

All five contributions in Part One of our collection show that Italy and Germany have grown apart,

20 Donato Di Carlo, "Germany is Quietly Rebalancing its Economy – But this will not Fix the Eurozone's Flaws" (2018). Annex 3.

21 "Geo-Politics of Exporting Too Much: Contrasting Trajectories of Germany and Japan".

22 "Ideational differences between Italian and German governments during the crisis".

23 "Cultural Foundations of the Italian and German Political Economy."

rather than converged, during the past 30 years. Now, we will look at divergences across specific sectors of the economy in Part Two.

B) Sectors of the Political Economy of Italy and Germany

Part One of the present collection showed us how the divergences of the German and Italian political economies play out on the aggregated level, but we know little about how the divergences manifest across different sectors of the economy. We have selected the housing-construction sectors and the banking sectors as prime infrastructural backbones of both systems. These are supplemented with a comparative study on family cultures and family policy in both cases. Albeit not an economic sector in the strict traditional sense (though child and elderly care employ ever more people) and a policy-field that is usually side-lined in the mainstream political economy literature, we want to highlight its cross-sectoral implications since it is central to the functioning of the economy as a whole, structuring the supply of young and skilled workforce.

Sebastian Kohl and Alexander Spielau target the "forgotten sector" of housing and construction, as they call it in their contribution.[24] Pointing to its impact on employment and GDP growth, they observe that it is strange that classical political economy sidesteps it. Kohl and Spielau point out that housing and construction differs dramatically between both countries and that it plays a central role in both economies. While the existence of a large rental stock reinforces the export led-growth model of Germany, the large homeownership rates in Italy fuel into an internal demand-driven economy in Italy. This led to different demands and requirements that both countries have towards the single currency. In a meticulously well-informed and detailed study, the authors follow the trajectories of the housing sectors of both countries from WW II till today, putting the thesis of distinct clusters of Southern-European housing-construction economies and Northern-rental-export economies on the agenda.

With the banking sector, we look at another crucial infrastructural backbone of the Italian and German economy. Frederik Traut scrutinises the interventions in both countries during the banking crisis.[25] Somewhat unexpectedly, he finds that Germany, in staunch neglect of its supposed ordoliberal orientation, intervened heavily once its banking sector got into trouble during the great financial crisis. In the case of *IKB*, a bank specialised in lending to small and medium-size enterprises, the government injected 7 bn Euros out of fear that the failing of the bank would bring down the rest of the economy. After this and other large-scale bail-outs in Germany, the government was eager to promote a harsh bail-in regulation at European level. In Italy, due to better banking supervision, the government did not have to intervene in the banking sector. However, once the financial crisis gave way to a global recession, this changed due to many non-performing loans that Italian banks had given to companies now hit by the recession. Italy therefore faced a hidden, longer and time-lagged banking crisis, in contrast to Germany. With the new European regulation in place that the Germans had pushed for, the Italian government saw its hands tied once the slow-boiling crisis became ever more evident in Italy. Traut argues, convincingly in our view, that the Italian government had no other option than to circumvent the new regulation giving its banks the same medicine that the German banks had obtained from their government before, facing, however, strong criticism from Germany. Lucia Quaglia's contribution corroborates Traut's findings.[26] She scrutinises the policy-process around the establishment of the banking union, pointing out that Germany's and Italy's preferences and positions were at odds, representing the North-South cleavage within the European Union, in which the

24 Sebastian Kohl and Alexander Spielau, "Worlds Apart: the Divergences of Southern European Housing-construction Economies and Northern European Export Economies" (2018).

25 "Banking Crisis Interventions in Germany and Italy: The Unpleasant Case of the New European Bank Resolution Framework."

26 "Comparing the German and Italian Approaches to Banking Union."

decisive difference was in the fact that Germany had already overcome its banking crisis. Traut's and Quaglia's findings resonate well with Kohl and Spielau's: the different impact and unfolding of the banking crisis stems from the structural difference between the banking and lending sectors in Italy and Germany, that evolve from the differences in the housing and construction sectors.

The Varieties of Capitalism and growth model perspectives neglect family policy and family cultures, which are crucial to understand the widening gap between Italy's and Germany's socio-economic profiles. Agnes Blome sheds light on the staunchly diverse paths that the two countries have followed since the 1990s. In the early 1990s, Italy and Germany shared similar conservative cultures and institutions concerning early childcare and the employment of women with children.[27] In both countries, female employment rates hovered just above 50 per cent. In the 2000s, Germany embarked on a reform trajectory abolishing the male-breadwinner-centred family policy model that had been in place for over half a century by introducing parental leave schemes and early child-care coverage for under three-year-olds. Blome shows how a change in cultural values after the 1990s accelerated the German reform trajectory, while Italy did not experience such a change in values. As a result, the mothers employment rates in Italy have only moved from 54 to 56 percentage points during the past 30 years while the German mothers employment rate is with over 70 per cent, the second highest in the EU.

We see now that both economies reacted differently not only when one looks at them from an aggregated perspective as we did in Part One, but also across different sectors of the economy, as we showed in Part Two. This, as we will now show in Part Three, has impacted strongly on the attitudes that German and Italian citizens have towards each other, and how they perceive their country's relation to the European Union.

27 "Maternal employment, attitudes toward gender equality and work-family policies. German-Italian Discrepancies"?

C) German and Italian Perceptions, Differences and Misgivings

So far our collection shows that both countries have grown apart since the 1990s. The differences in institutions, interests and culture that set both economies apart have a dire impact on the feeling of citizens towards one another. The adverse feelings to one another and towards the EU have also re-structured the party systems in both countries. The backdrop to these attitudinal changes is the different experience of the crisis and of the structural reform process connected to it.

Alessandro Pelegatta shows how the widening gap between Italy and Germany in institutions, social structure and political attitudes is mirrored in the attitudes of the citizens of both countries towards one another.[28] This view is strongly associated with the feelings that the citizens of both countries have towards the EU. Italian citizens tend to blame Germany for the Euro crisis and for the bad Italian economic situation. They think that Germany is abusing its power in Europe and that its behaviour has made the crisis worse. The EU, in this sense, has become a project dominated by Germany. Moreover, the countries have reversed their positions regarding their position towards European integration. While, traditionally, Italians have been in favour of integration while Germans were sceptical, the past decade saw the inversion of these positions.

Hanspeter Kriesi illuminates how this fed into the new party system configurations in Italy and Germany.[29] He embeds the two most recent elections in Germany and Italy into the wider European picture and the trends of party-system change, pointing to profound tensions between the élites and the people in both countries, which have given rise to populist challenger parties. The flaring up of the party systems has made government formation difficult and while Germany opted for the old grand-coalition model, Italy has now

28 "Italy and Germany during the Crisis. Support of the EU and Reciprocal Views."

29 "The Political Space in Italy and Germany during the Crisis: Italian and German Populism Compared."

an all populist government. Both, Kriesi argues, are unstable. The grand coalition model because it "ain't so grand no more", combining only 53 per cent of votes. The Italian government coalition is unstable due to the tensions between the two populist parties on ideological issues.

Providing the background for the populist surge, Filippo Taddei takes issue both with the term and demand for structural reforms.[30] Having been involved as practitioner in the *Jobs Act* reform in Italy, he launches a powerful argument that structural reforms, as demanded by Northern European states from Southern European countries in crisis, can only be structural if they can marshal political and popular consensus at home. Comparing the *Fornero Pension Reform* of 2011 with the *Jobs Act* of 2015, two structural reforms enacted in Italy during the crisis, Taddei concludes that "only reforms investing political capital and gathering consensus in their scope can persist in time and affect ordinary economic and social behaviour". He thereby provides a clue as to why the structural reforms in Italy, seen by the population as imposed from the North, have led to anti German and anti-EU feelings, as described by both Pelegatta and Kriesi. It also explains why these reforms are about to be partly rolled back by the new populist government, and makes a strong case for the counter-productivity of octruating structural reforms from the outside.

Manos Matsaganis looks at the impact of the European crisis and its aftermath in the European South with a special focus on the Italian (non-) recovery.[31] Analysing and comparing economic indicators both pre- and post-crisis, Manos findings are shocking. Portugal, but none of the other Southern European countries are back to pre-crisis levels of economic performance. Besides the worst-case scenario of Greece, Italy is the second worst off. Matsaganis hints at the co-evolution of political extremism in the European South (except in Portugal) with the way in which the crisis was handled in terms of structural reforms by the EU and Northern European governments. This links well into the first-hand practitioner insights that Filippo Taddei provides for the Italian case, in which he theorises form his experiences about the necessity of domestic political ownership as a pre-condition for a successful structural reforms in the European South.

Ilaria Madama and Matteo Jessoula's contribution shows how the Europe 2020 framework is implemented in very different ways in national contexts.[32] The authors give us a wonderful study of the contrasting implementation of poverty and social exclusion policies in Italy and Germany during the first five cycles of the European semester. This also shows that the differences between welfare-state institutions in Italy and Germany have become broader, instead of narrower, over the past two decades. Both countries fight poverty very differently under the same European provisions. Germany distorted the policy framework to fit with its century old traditions and institutions of poverty relief and social exclusion policies. In Italy, in contrast, the targets and the institutions that Brussels proposed were fully embraced since the country had only a weak social exclusion and poverty relief policy before. The contribution not only provides a rigid analysis of the policy process, but also theorises when and how EU programmes are implemented or re-formulated to fit national traditions and culture.

What we have seen in Part Three of our collection is that the structural and widening differences between both countries have an impact on public opinion, party systems, and government formation. With the assessment of structural reforms in Italy and the diverging ways in which the EU provisions are implemented in both countries, we have also come to a first idea of about why, after 30 years of accelerated and forceful socio-economic integration in Europe, the two countries are still "worlds apart from one another".

30 "European Integration and Political Ownership: Fiction and Reality behind Structural Reforms and Risk Sharing."

31 "The Political Economy of Recovery in Southern Europe."

32 "Accommodating EU's Influence vs Protecting National Sovereignty. The Fight Against Poverty in Italy and Germany at the Time of 'Europe 2020'."

D) The Legacy of the Welfare State in Europe

Ever since Alan Milward's seminal study on *The European Rescue of the Welfare State*[33] "Social Europe" and the search for a "European Social Model" keeps irritating the students of European integration – conceptually, empirically, and politically. Milward's rescue thesis was published in the year which witnessed the signing of the Maastricht Treaty and the move towards a common currency. It is difficult to read these events as a "rescue operation" and Bo Stråth, Milward's successor at the EUI History Department, had good reasons to underline that this Union was no longer the Europe of Milward.[34] And yet, in a paradoxical sense, Milward's thesis has regained topicality. In his October 2014 speech to the European Parliament, European Commission President elect, Jean-Claude Juncker, spoke of his wish for Europe to be "triple-A on social issues", putting social issues further up on the agenda.[35] Pamela Pansardi[36] shows that it was not only this speech but that all his speeches are decisively more pro welfare in their vocabulary than those of the previous Barroso Commission. What this was supposed to mean was codified in the European Pillar of Social Rights,[37] and subsequently solemnly supported by the Commission, the Council and the European Parliament.[38] This is definitely a spectacular return of "the social" on the European agenda. Both Florian Rödl[39] and Vladimir Bogoeski[40] are not impressed, however. Rödl lists the many obstacles against the realisation of a common social legislative agenda and opts for a re-orientation of the conceptualisation of the function of the economic freedoms which would inhibit their instrumentalisation for a de-regulation of national social accomplishments. Bogoeski reads the proclamation of the Social Pillar as an exercise in whitewashing, an example of what Giandomenico Majone has characterised as the European élites' "political culture of total optimism".[41] The Pillar is soft indeed. This softness contrasts markedly not only with the above-mentioned jurisprudence of the CJEU and the imposition of internal devaluation in Europe's austerity politics, but even, as Francesco Costamagna underlines, with the implementation of the European Semester.[42] His observations document that the perception of a great diversity of socio-economic conditions, to which the semester responds, is counteracted by the uniformity of neoliberal recipes which orient the management of the semester. These tensions are an acid test for our assumptions on the resilience of national economic cultures. Two contributions are illuminating here. As Marcel Hadeed, in his analysis of the Reception of the "Social Pillar" shows, the weight attributed by the German government and its *Fachbürokratie* to this noble initiative, is "*en quelque façon nul*".[43] This seems, in the sphere of social policy, all the more remarkable as Minister for Labour and Social Affairs, Hubertus Heil, is a Social Democrat and by no means from the right wing of that party. Hadeed cites the German Finance Minister, also a Social Democrat, assuring us that "a German finance minister is a German finance minister regardless of his party card". The agenda of the Minister for Labour and Social Affairs is not

33 Alan Milward, *The European Rescue of the Nation State*, New York: Routledge 1992.

34 Bo Stråth, "Still the Europe of Milward? On the Need for a New Long-Term Historical Understanding of Today's Europe", UCL Working Paper No. 1/2011, London 2011.

35 "A New Start for Europe", Strasbourg, 15 July 2014, available at http://europa.eu/rapid/press-release_SPEECH-14-567_en.htm.

36 "A 'more political' leadership for the President of the Commission? A mixed-methods language based analysis."

37 Ibid.

38 Proclamation of the European Pillar of Social Rights, Gothenburg, 17 November 2017.

39 "An Alternative to the Constitution of the EU's Single Market"?

40 "The EU Political Culture of Total Optimism is not Dead: The Case of the European Pillar of Social Rights."

41 "The Deeper Euro-Crisis or: The Collapse of the EU Political Culture of Total Optimism," Working Paper, 2015, available at: http://cadmus.eui.eu//handle/1814/35281.

42 "Industrial Relations and Labour Law in the EU Economic Governance Mechanisms: The Cases of Italy and Germany".

43 "What to Expect from Germany for the European Pillar of Social Rights?"

that of the conservative coalition partner, but it is entirely German in the definition of its priorities. An important determinant in Germany is its fiscal federalism which has institutionalised a low-wage equilibrium. The Italian pattern is characterised by conditions which favour the toleration of inflationary wage increases. Is it at all conceivable that Europe can create the "institutional determinants of balanced wage growth"? The fundamental dilemma of national political autonomy is a risk for the priorities of European governance that have been established. The control of these conditions, however, would require extremely complex and demanding responses. And a recipe that may work for the German-Italian case, will hardly work in the entire Union.

E) The Demise of Law

A little more than two decades ago, just a few years after a, then, young post-Ernst Haas generation of political scientists, had (re-) discovered the integration process as a worthwhile academic topic, Christian Joerges urged these newcomers "to take the law seriously".[44] Those years witnessed a "golden age" of interdisciplinary studies, with legal scholarship exploring more curiously then ever the operation of legal actors, the context, and the impact of legal prescriptions; political scientists were - often enough - inspiring such innovative endeavours. By now, these times are gone. The reasons or this are complex and somewhat paradoxical. The earlier interdisciplinary co-operation rested on the implicit transdisciplinary assumption that integration was a good thing which deserved to be promoted. After a decade of financial crisis, this seems no longer so unquestionable. The prevailing attitude in other disciplines is quite similar. Lawyers observe and meticulously document the establishment of a new "crisis law". Political scientists observe and document with great precision the growth of European powers and governance practices. Both disciplines hesitate to confirm that this new constellation is here to stay and would deserve this quasi-constitutional importance. These new uncertainties are accompanied by another tectonic shift in the contest of disciplines. Thanks to the preoccupation of European élites with the financial crisis, economists occupy the driver's seat when it comes to providing practical advice. The paradigms and rationality criteria of economics, however, are distinct and not really reconcilable with those of the social sciences, let alone, the normative concerns of lawyers, and certainly not akin to the kind of agenda which we are pursuing.[45]

Both the disciplinary composition of our participants and the substance of their comments mirror this constellation quite faithfully. Only three economist attended the conference.[46] The number of lawyers still seems considerable. There is not much left, however, of the once widespread belief that law would be both "the agent and the object of integration".[47] The contributions that we have assembled in section F are anything but affirmative. Katharina Mangold's[48] comments on the role of the Commission touch upon a very sensitive issue of general importance. She takes issue with Commissioner Oettinger's comments on Italian politics. This is well argued. However, the Commission is, next to the ECB, the most important example for what Paul Tucker characterises as an "unelected power".[49] The Commission has to compensate for its democratic deficit by expertise and objectivity. And yet, even where it acts as a

44 "Taking the Law Seriously: On Political Science and the Role of Law in the Process of European Integration", *European Law Journal*, 2 (1996), 105-135.

45 The only transdisciplinary approach we are aware of is "Constitutional economics" as inspired by James Buchanan and defended in particular by the "third generation" of the Freiburg school; see most prominently Lars Feld, "Eine Europäische Verfassung aus polit-ökonomischerSicht", *ORDO – Jahrbuch für die Ordnung von Wirtschaft und Gesellschaft*, 54 (2003), 289-317.

46 Frederik Traut, see Section C 3.

47 Dehousse, R., and Weiler, J.H.H., "The Legal Dimension", in: Wallace, W. (ed.), *The Dynamics of European Integration*, London: Pinter, 242-260.

48 "The EU Commission as 'Honest Broker'? German and Italian Perspectives on an Administrative Body".

49 Tucker, P. (2018), *Unelected Power. The Quest for Legitimacy in Central Banking and the Regulatory State*, Princeton NJ-Oxford: Princeton University Press, 2018.

"guardian of the Treaty", it cannot avoid exerting power and should, precisely for this reason, act more prudently than Oettinger did. The other lawyers address more general discrepancies between the legal design of the integration project and its actual functions and performance. Their object is the transformation of the Union in the course of the financial crisis. They all diagnose the failings of the "integration through law" agenda. These failings have a long history. They became dramatically apparent, when the Union undertook its "turn to governance", which was essentially meant to overcome the limits of European powers where the need to take action seemed urgent.[50] President Mario Draghi's proclaimed readiness to do "whatever it takes"[51] is evidence of the same strategy.[52] Nicole Scicluna[53] underlines the authoritarian and coercive mode of the European crisis management and adds that the imposed integration strategy may end up in disintegration through the erosion of the legitimacy of the European project. Both Christian Joerges[54] and Karl-Heinz Ladeur[55] address the same concerns, albeit in different ways. In Joerges' understanding, the democratic deficiency of Europe's crisis politics stems, in the last instance, from its disregard of the legitimate political ordering of "the economic" in constitutional democracies.[56] Ladeur's account is less "legalistic". He underlines the interdependence of formal rules and "social norms", which, only in their complementarity, ensure the functioning of economic and political systems. His conceptualisation is an exercise in sociological jurisprudence with great affinities to Hien's notion of economic cultures.[57] And it should be apparent that there is no contradiction between such perceptions of an erosion of legalism and a disintegration of European studies with the insistence of the contributors to section D on the viability of legal protection against marketisation processes which threaten the social existence of workers.

F) Justice, Security, Finances and Solidarity

Throughout all of the contributions we observe concerns about the future of Europe which explicitly or at least implicitly assume that the present state of the Union should not be petrified as its new normalcy. The pertinent suggestions, however, all operate in the shadow of *Hegel's Ohnmacht des Sollens* (powerlessness of the ought). Where we imagine the contours of a better European future, we are plagued by scepticism. Does it really make sense to come up with proposals which seem so obviously unrealistic? We suggest that it does. We believe that even "unrealistic" proposals can help us to understand Europe's present better; we also believe that Europe's presence is characterised by such high uncertainties that complacency with regard to the presence is anything but comforting.

The three contributions in the present section F pursue very different strategies.

Libraries have been filled with literature on the democratic deficit of the EU. Glyn Morgan,[58] however, focuses on another issue, the problem of justice. Constitutionalists tend to address this issue in the context of the powers of the EU either in the realm of labour law and welfare politics, or in the context of constitutional commitments, such as the *Sozialstaatsklausel* of the German Basic Law. Both the debates on welfare politics

50 Joerges, C, "Integration through de-legislation? An irritated heckler", European Governance Papers (EUROGOV) No. N-07-03, available at: http://www.connex-network.org/eurogov/pdf/egp-newgov-N-07-03.pdf.

51 *Verbatim* at https://www.ecb.europa.eu/press/key/date/2012/html/sp120726.en.html.

52 Draghi wisely added that this occurred "within our mandate".

53 "Integration-through-crisis as a distinct integrative mode: Placing expediency ahead of democracy"?

54 "The Challenge of Socio-Economic Varieties to the Law of European Integration".

55 "The End of the Universality of Norms as a Model for Europe –The Error of "Seeing like a State" (J. S. Scott) in the Postmodern Condition".

56 The diagnosis of a crisis of law is compatible with Scicluna's findings; see, also, C. Joerges and C. Kreuder-Sonnen, "European Studies and the European Crisis: Legal and Political Science between Critique and Complacency", *European Law Journal*, 23 (2017): 118-139.

57 A 4.

58 "Is the EU Unjust"?

and the debate between Habermas and Streeck, as re-constructed by Joerges,[59] testify to a difficulty of fundamental importance: Is a European *Sozialstaat* at all conceivable or can *Sozialsaatlichkeit* be realised only by nation states? Morgan's shift to "justice" bypasses this dichotomy. The European project, he submits, can be and should be justified by the security that it ensures for the citizens of the Union. This is a defence of "deep" integration, albeit an unconventional one. Members of a polity which ensures their security "owe each other the duty to guarantee the conditions of security. This duty will have distributive implications, but different distributive implications than within a nation-state".

Tiziano Zgaga's essay departs from a dense and instructive re-construction of the Commission's proposal for a European Minister of Economy and Finance.[60] Whoever remembers the remark of the former President of the *Bundesbank*, Helmut Schlesinger, in the proceedings on the Maastricht Treaty before the *Bundesverfassungsgericht* "that a currency union, especially between States which are oriented towards an active economic and social policy, can ultimately only be realised in common with a political union (embracing all essential economic functions) and cannot be realised independently thereof or as a mere preliminary stage on the way to it",[61] will remain impressed but disappointed. There is enormous ingenuity in the Commission's proposals. There are also unsettled constitutional and political issues such as the growth of ever more "unelected power".[62] Zgaga addresses these in the second section of his essay. His own views are close to Schlesinger's position. Of particular interest in the present context is his re-construction of the German and the Italian position. Unsurprisingly, these diverge drastically. Zgaga's analysis of the reasons is revealing with respect to the importance of the cultural determinants of economic policy. There is a strong touch of ordoliberalism in the German resistance, interestingly one which is not identical with party affiliations: "Everywhere in Europe I said: a German finance minister is a German finance minister…"[63]

The distinction between justice "within" and justice "between" the Member States, which Morgan underlines, was of no concern in the homogeneous world of the old EEC. This changed with the enlargements of the Union. What emerged as a concern then became dramatic after the establishment of the EMU and the discipline imposed on the members of the Eurozone. We have to (re-) solidarise Europe in order to defuse the still virulent crisis and its impact - both within and between the Member States, argue Maurizio Ferrera and Carlo Burelli.[64] Their finding is that EMU has created interdependencies and dynamics which are beyond our control. Their notion capturing this state of affairs is the "complex adaptive system (CAS)". The tragedy is that the "properties of a CAS are not merely causally active but become irreducible and irreversible". "Solidarity" is a commitment enshrined in Article 2 TEU. It has to be fleshed out – and then implemented in a Union of ever deepening diversity and conflicts.

59 F 3.

60 "A European Minister of Economy and Finance: Assessing the Commission's Proposal and Comparing Germany's and Italy's Position".

61 2 BvR 2134/92 & 2159/92, BVerfGE 89, 155. English translation: *Manfred Brunner and Others* v. *The European Union Treaty* [1994] 1 *Common Market Law Reports* 57 (para. 92).

62 See n. 50 above.

63 Social Democrat Olaf Scholz (minister of finance) on 22 March 2018, cited in Hadeed, D 4.

64 "Re-solidarising Europe and Defusing the Crisis".

G) Annex

We have included in this Annex, two contributions which were not presented at the Vigoni conference. They represent, in our view, the spectre of options which we have to face. Claus Offe and Maurizio Ferrera's opt for a turn to solidarity. Such a turn, they add, is unlikely to occur deliberately; Europe will nevertheless be forced into it.[65] Di Carlo closes the Annex, showing how Germany is quietly re-balancing its economy.[66]

65 "Order in the Eurozone". Claus Offe has elaborated his views in: *Europe Entrapped*, Cambridge: Polity Press, 2015, and "Europe Entrapped. Does the EU have the Political Capacity to Overcome its Current Crisis?", *European Law Journal* 19 (2013): 595-611.

66 "Germany is quietly Rebalancing its Economy – But this will not Fix the Eurozone's Flaws."

CONTRIBUTORS

Agnes Blome is a post-doctoral fellow at the Otto-Suhr-Institute of the Free University Berlin. Blome is interested in comparative welfare state research, women's political representation, and the relationship between people's attitudes and policy-making. She received her Ph.D. from the Humboldt-University Berlin and worked at the WZB Berlin Social Science Center. Her most discussed book is *The Politics of Work-Family Policies in Germany and Italy*.

agnes.blome@fu-berlin.de

Vladimir Bogoeski is a PhD Candidate at the Hertie School of Governance and affiliated member of the doctoral programme "Unity and Diversity in the European Legal Area" at the Humboldt University (European Law School). His Ph.D. studies are funded by the German Academic Merit Foundation (Studienstiftung des Deutschen Volkes). He holds degrees in Law from Ss. Cyril and Methodius University of Skopje (LLB) and University of Bremen (LLM). In 2018, Bogoeski was visiting research fellow at Fordham Law School in New York. His thesis focuses on the ever growing tension between economic and social rights in the enlarged EU. The research analyses judicial and legislative responses to the clashes between free movement rights and (national) social regulation in the aftermath of the *Viking* and *Laval* cases.

v.bogoeski@phd.hertie-school.org

Federico Bruno is Ph.D. candidate at the Network for the Advancement of Social and Political studies of the University of Milan. He has previously studied at La Sapienza and Roma TRE universities in Rome. His research focuses on the influence of the ordoliberal ideology on the reform of the Eurozone in the years of the crisis.

federico.bruno@unimi.it

Francesco Costamagna is Associate Professor of EU Law at the Law Department of the University of Turin. He is Affiliate at the Collegio Carlo Alberto. He has been faculty member of the Center for Transnational Legal Studies (Georgetown University) and Guest Professor at the Goethe University Frankfurt. He is currently serving as national expert of MoveS (Free Movement of Workers and Social Security Coordination), a network funded by the European Commission. His research mainly deals with the relationship between economic integration and social protection systems in the EU legal order, with a specific focus on the relationship between the European economic governance and the EU social dimension. Moreover, he has worked extensively on intra-EU mobility and free movement of workers. He is the author of a book, articles and book chapters, both in English and Italian, on these and other related topics.

francesco.costamagna@unito.it

Donato Di Carlo is a Ph.D. Candidate at the Max Planck Institute for the Study of Societies, in Cologne. He works in European comparative political economy with a focus on models of capitalism, wage setting systems and public administrations. In his Ph.D. he studies the political and institutional determinants of public sector wage-setting in Germany and Italy, in relation to processes of structural divergence in the EMU. He has been visiting researcher at the European University Institute and has obtained his MSc in Political Economy of Europe from the London School of Economics and Political Science. His most discussed article is *Does Pattern Bargaining Explain Wage Restraint in the German Public Sector?* (MPIfG Discussion Paper).

dicarlo@mpifg.de

Margarita Estévez-Abe is political science professor in Maxwell School of Citizenship and Public Affairs, Syracuse University, and Co-Director of the Center of European Studies at Syracuse University. Her research focuses on social policy and gender issues in advanced industrial societies. She is known as the first scholar who "gendered" the Varieties of Capitalism. Her book on the Japanese variety of welfare capitalism and its politics, Welfare Capitalism in Post-war Japan, was the winner of the Masayoshi Ohira Memorial Award in 2009. From 2012 to 2015, she held the Chair of Public Policy at Collegio Carlo Alberto in Turin, Italy. She's currently working on a book manuscript, *Women, Immigrants and the Elderly: Politics of Demographic Aging in Germany, Italy, Japan, Spain and South Korea*.

Mestev02@maxwell.syr.edu

Maurizio Ferrera is Professor of Political Science at the University of Milano, Italy. His research focuses mainly on comparative politics and public policy, the welfare state and European integration. He has taken part over the years in many commissions and Working Groups set up by the Italian government, the European Union, the OECD and the ILO and currently sits on the *Exzellenzkommission* of the *Deutsche Forschungsgemeinschaft* (DFG). He is President of the Network for the Advancement of Social and Political Studies (NASP) among the universities of Lombardy and Piedmont and a member of the Board of Directors of the *Centro di Ricerca e Documenzazione Luigi Einaudi* of Turin. Since 2004, he has been an editorialist on the *Corriera della Sera*. His latest book in English is *The Boundaries of Welfare*, (Oxford University Press, 2005). In 2013, he received an Advanced Grant from the ERC, to carry out a five-year project on "Reconciling Economic and Social Europe" (REScEU).

maurizio.ferrera@unimi.it

Josef Hien is a post-doctoral fellow at the REScEU project. Funded through a European Research Council advanced grant and hosted at the University of Milan, REScEU aims at reconciling social and economic Europe. Hien is interested in the ideational and cultural foundations of European political economies. He received his Ph.D. from the European University Institute and has worked as a post doc at the Max Planck Institute for the Study of Societies (Cologne), at the Collegio Carlo Alberto (Moncalieri/Turin) and the Berlin Social Science Centre (WZB, Berlin). Hien is currently a visiting fellow at the Institute for Future Studies (IF) in Stockholm. His most discussed article is The Religious Foundations of the European Crisis in the *Journal of Common Market Studies*. He edited his most recent book together with Christian Joerges: Ordoliberalism, Law and the Rule of Economics by Hart Publishing, Oxford 2017.

josef.hien@unimi.it; josefhien@googlemail.com

Matteo Jessoula is Associate Professor of Political Science at the University of Milan. He is also Director of the Welfare Laboratory, Director of the International Observatory on Social Cohesion and Inclusion, Coordinator of LPF-Comparative Politics and Public Philosophy Lab and National coordinator within ESPN-European Social Policy Network. His current research focuses on pensions, social assistance and employment policies, minimum income protection in comparative perspective, European social governance. Among his publications, the volumes: *Fighting poverty and Social Exclusion in the EU. A Chance in Europe 2020*, Routledge, 2018 (co-edited with I. Madama), *Labour Market Flexibility and Pension Reforms. Flexible Today, Secure Tomorrow?*, Palgrave, 2012 (co-edited with K. Hinrichs); and the articles: "'Selective Flexicurity' in Segmented Labour Markets: The Case of Italian Mid-siders", (with P. Graziano and I. Madama) in *Journal of Social Policy*, 2010; and "Europe 2020 and the Fight against Poverty: Beyond Competence Clash, Towards 'Hybrid' Governance Solutions?", in *Social Policy & Administration*, 2015.

matteo.jessoula@unimi.it

Christian Joerges is Professor em. for Law and Society at the Hertie School of Governance in Berlin and Co-Director of the Centre of European Law and Politics at the University of Bremen. Until 2007, he held the chair for European Economic Law at the European University Institute, Florence. In 2009, he was awarded an honorary doctorate from the University of Fribourg i.Ue. His research focuses on European and international economic law and the legitimacy problems of pertinent government arrangements and practices. His most discussed book is the *Darker Legacies of Law in Europe: The Shadow of National Socialism and*

Fascism over Europe and its Legal Traditions, (ed. with Navraj Singh Ghaleigh).

joerges@hertie-school.org

Sebastian Kohl is a researcher at the Max-Planck Institute for the Study of Societies. He holds a Ph.D. from Sciences Po Paris and the University of Cologne. His research interests include economic sociology, political economy, housing, insurances and the philosophy of the social sciences. He has published in *Socio-economic Review*, *Urban Studies, Politics & Society* and the *Review of International Political Economy.* His recent book is *Homeownership, Renting and Society: Historical and Comparative Perspectives*, published with Routledge.

kohl@mpifg.de

Hanspeter Kriesi holds the Stein Rokkan Chair in Comparative Politics at the European University Institute in Florence. Previously, he has been teaching at the universities of Amsterdam, Geneva and Zurich. His wide-ranging research interests include the study of various aspects of democracy, political communication, political mobilisation and opinion formation. His recent books include (together with Edgar Grande, Swen Hutter and colleagues), *Politicizing Europe. Integration and Mass Politics* (2016), *Political Conflict in Western Europe* (2012), and *West European Politics in the Age of Globalization* (2008), (together with Monica Ferrìn and colleagues), *How Europeans View and Evaluate Democracy* (2016), (together with Takis S. Pappas and colleagues), *European Populism in the Shadow of the Great Recession* (2015), (together with Pablo Beramendi, Silja Häusermann, Herbert Kitschelt and colleagues), *The Politics of Advanced Capitalism* (2015), and (together with Lisheng Dong, Daniel Kübler and colleagues), *Urban Mobilizations and New Media in Contemporary China*.

hanspeter.kriesi@eui.eu

Karl-Heinz Ladeur is Professor (Emeritus) at the Faculty of Law in Hamburg. In 2011, he was awarded an honorary doctorate from the University Freiburg i.Ue. Ladeur's research areas and interests are theory of law, public law with a focus on national, European and global administrative law, media and environmental law. He has published widely in all these fields. Recent publications include: "The Significance of General Administrative Law for European Administrative Law" in: *Conflict of Laws and Laws of Conflict in Europe and Beyond*, ed. by Rainer Nickel (Intersentia, 2010) and *Public Governance in the Age of Globalization* (ed.) (Ashgate Publishing, 2004).

karl-heinz.ladeur@uni-hamburg.de

Ilaria Madama is Associate Professor of Political Science at the University of Milan, Senior Researcher in the REScEU project, funded through a European Research Council advanced grant and hosted at the University of Milan, and Coordinator of the EuVisions Observatory. Her current research focuses on the reform of minimum income protection in comparative perspective, the transformation of family policy, and European social governance. Among her publications: *Fighting Poverty and Social Exclusion in the EU: A Chance in Europe 2020*, Routledge, 2018 (co-edited with M. Jessoula); "The Right(s) and Minimum Income in Hard Times: Southern and Eastern Europe Compared", in *European Societies*, 2018 (with M. Natili, M. Jessoula and M. Matsaganis); "Beyond Continuity? Italian Social Assistance Policies between Institutional Opportunities and Agency", in *International Journal of Social Welfare*, 2013.

ilaria.madama@unimi.it

Anna Katharina Mangold is a associate professor (*Privatdozentin*) and Schumpeter Fellow (VW Foundation) at Goethe-University Frankfurt/ Main. The Schumpeter project analyses possible legitimation strategies for anti-discrimination law. Mangold works in public law, including European Union law, in legal philosophy, contemporary legal history and feminist legal theory. She received her Dr. jur. from the Albert-Ludwigs-University Freiburg/Brsg. and has delivered her habilitation thesis docent at Goethe-University Frankfurt aM.

Currently, Mangold works as an interim professor for public law at the University of Konstanz. Her most discussed book is *Gemeinschaftsrecht und deutsches Recht: Die Europäisierung der deutschen Rechtsordnung in historisch-empirischer Sicht* (*Community Law and German Law: The Europeanisation of the German Legal System in Historico-empirical Perspective*).

mangold@jur.uni-frankfurt.de

Philip Manow is Professor of Comparative Political Economy at the University of Bremen in the Department of Political Science. He held Professorships at the universities of Konstanz and Heidelberg and was director of a research group at the Max-Planck Institute or the Study of Societies, Cologne. He was visiting scholar at the Center for European Studies, Harvard, Sciences Po, Paris, and the Institute for Advanced Studies, Berlin. His research interests include comparative political economy, in particular comparative welfare state research, the German political system, European integration and political theory. He has published, amongst others, in the *British Journal of Political Science*, the *European Journal for Political Research*, *Politics and Society*, *Legislative Studies Quarterly*, *Comparative Political Studies*, and *Socio-Economic Review*. He is editor (with Kees van Kersbergen) of *Religion, Class-coalitions and Welfare States*, (Cambridge University Press, 2009), and author of the forthcoming book: *Social Protection, Capitalist Production: The Bismarckian Welfare State and the German Political Economy, 1880-2010*.

manow@uni-bremen.de

Manos Matsaganis is Professor of Public Finance at the Polytechnic University of Milan. He studied at the Athens School of Economics and Business, the University of York, and the University of Bristol. He previously worked at the London School of Economics, the Greek Prime Minister's Office, the University of Crete, and the Athens University of Economics and Business. He has held visiting positions at the Center for European Studies at Harvard, at the Center for Equitable Growth at UC Berkeley, and at the Center for the Study of Europe at Boston University. His current research focuses on the distributional implications of the Eurozone crisis, the political economy of austerity in Southern Europe, and the implications of technical change for the future of work and social protection. His article on "The Political Economy of Austerity in Southern Europe", (with Sofia Perez) was published in *New Political Economy* in 2018.

emmanuel.matsaganis@polimi.it

Pamela Pansardi is currently Postdoctoral Researcher at the University of Pavia and Principal Investigator of the two-year research project "Gender and Power in Italian Politics". Until December 2017, she was Postdoctoral Researcher at the University of Milan, working for the project REScEU "Reconciling Economic and Social Europe: Values, Ideas, and Politics", led by Prof. Maurizio Ferrera. She is a regular contributor for the EuVisions Observatory on Social Europe and editor (with Ilaria Madama) of its Social Policy Pillar. Her works in EU studies concentrate on the exploration of the EU value-sphere through the tools of the (quantitative and qualitative) analysis of language in political speeches, and have appeared in the *Journal of European Integration* and in the *European Journal of Political Research*.

pamela.pansardi@unipv.it

Alessandro Pellegata is currently a research fellow at the University of Milan where he is involved in the REScEU project ("Reconciling Economic and Social Europe"). For REScEU he supervised the conduction of a cross-national mass and elite survey. Furthermore, he coordinates the Public Opinion section of the EuVisions observatory (EuVisions.eu). Before joining REScEU, Alessandro held a research fellowship at the University of Siena. His main research interests are in the field of comparative politics, focusing especially on electoral competition and government alternation, political representation, public opinion, EU support and political corruption. His latest research has appeared, among others, in the *European Political Science Review*, *International Journal* *of Public Opinion Research*, *International Political Science Review*, *Italian Review of Political Science* and *Journal of European Public Policy*.

alessandro.pellegata@unimi.it

Lucia Quaglia is Professor of Political Science at the University of Bologna. She was awarded research fellowships from the Hanse-Wissenschafts Kolleg, the University of Bremen, the Fonds National de la Recherche in Luxembourg, the Max Planck Institute in Cologne, the Scuola Normale Superiore and the European University Institute. Her most recent books are: (2016) *The Political Economy of Banking Union*, Oxford University Press (with D. Howarth); (2014) *The European Union and Global Financial Regulation*, Oxford University Press. She has guest co-edited 4 special issues of highly ranked academic journals. Her work has been published in several academic journals, such as *Regulation and Governance*, *Governance*, *Public Administration*, *Review of International Political Economy*, *New Political Economy*, *European Journal of Political Research*, *Journal of Public Policy*, *Journal of European Public Policy*, *Journal of Common Market Studies*, and *West European Politics*.

lucia.quaglia@unibo.it

Florian Rödl is Professor for Private Law, Labour Law and Social Law at Freie Universität Berlin. He received his Ph.D. from the European University Institute (Florence) where he learned about the fundamental tension between European integration and the democratic social state. He wrote his second dissertation ("Habilitation") at Goethe-Universität (Frankfurt aM), then serving as director of a junior researcher group at the Cluster of Excellence "Formation of Normative Orders". His recent study on "The European Pact on Social Progress - the alternative to the liberalistic constitution of the EU's single market" will be published soon.

florian.roedl@rewiss.fu-berlin.de

Nicole Scicluna is a Visiting Lecturer in International Relations at the University of Hong Kong. Prior to that, she was a Lecturer in Political Science and International Studies at the University of Birmingham, UK, and a postdoctoral fellow in Social Sciences at Collegio Carlo Alberto, Turin, Italy. Dr Scicluna received her Ph.D. in International Relations from La Trobe University, Melbourne, Australia in 2013. Her teaching and research interests include European integration, the law and politics of the EU, and the relationship between international law and international politics. Dr Scicluna's monograph, *European Union Constitutionalism in Crisis*, was published by Routledge in 2015. Her most recent article, "Integration through the Disintegration of Law? The ECB and EU Constitutionalism in the Crisis", was published by the *Journal of European Public Policy* in 2017.

Scicluna@hku.hk

Alexander Spielau is a post-doctoral researcher at the Max-Planck-Institute for the Study of Societies in Cologne in the research group on the Political Economy of European Integration. He received his Ph.D. in 2016 from the University of Cologne and was a doctoral fellow at the IMPRS-SPCE. He was a visiting researcher at Columbia University in New York and the MaxPo Centre at Sciences Po Paris in 2014. He is interested in the politics of macroeconomic adjustment and comparative capitalism. His most discussed article is "Better than the Euro? The European Monetary System, 1979-1998", in: *New Political Economy* (with Martin Höpner).

spielau@mpifg.de

Filippo Taddei is Associate Professor of International Economics at the Johns Hopkins School of Advanced International Studies (SAIS) where he teaches international finance and macroeconomics. He is also Director of the Bologna Institute for Policy and Research (BIPR) and the Master of Global Risk (MAGR) at SAIS. He received his Ph. D. in Economics with distinction from Columbia University and his degree in Economics from the University of Bologna. He has worked as Economic Advisor to the Italian

Prime Minister and he has been one of the main designers of the Italian labour market reform, *i.e.*, the *Jobs Act*. His research deals with macroeconomics, international finance and the relationship between the labor market and the pension system. Taddei was awarded the Lamfalussy Fellowship by the European Central Bank, and the Young Economist Award by the European Economic Association. His most discussed articles are "Intergenerational Altruism and House Prices: Evidence from Bequest Tax Reforms in Italy", with Giorgio Bellettini and Giulio Zanella, in the *European Economic Review*, and "International Capital Flows and Credit Market Imperfections: A Tale of Two Frictions", with Alberto Martin, in the *Journal of International Economics*.

ftaddei@jhu.edu

Frederik Traut is a Ph.D. candidate in political economics at the Hertie School of Governance in Berlin. He has studied economics and international affairs at the University of Bonn, the University of Hong Kong and the Hertie School of Governance. His research interests include the international political economy of banking regulation, international finance, and the Economic and Monetary Union. He also worked on these topics as a parliamentary advisor for members of the German Bundestag concerned with European economic affairs.

f.traut@phd.hertie-school.org

Visnja Vukov is assistant professor at the Department for Political and Social Sciences at the Pompeu Fabra University and a senior researcher at the joint Johns Hopkins University and Pompeu Fabra University Public Policy Centre in Barcelona. She holds a Ph.D. in political and social sciences of the European University Institute in Florence. Before coming to the UPF she worked as a post-doctoral research fellow at the MAXCAP project at the European University Institute. Her research interests include comparative and international political economy, European integration, globalization and development, and she focuses in particular on the challenges and governance of core-periphery integration in Europe. Her recent publications include "Making States for the Single Market: European Integration and the Reshaping of Economic States in the Southern and Eastern Peripheries of Europe", in *West European Politics*, "Governing Market Integration and Development - Lessons from Europe's Eastern and Southern Peripheries", in *Studies in Comparative International Development*, and "The Rise of the Competition State? Transnationalization and State Transformations in Europe", in *Comparative European Politics*.

visnja.vukov@upf.edu

Tiziano Zgaga is a Ph.D. candidate and teaching assistant at LUISS Guido Carli University in Rome and academic coordinator at LUISS School of Government. He holds a Bachelor's degree in Political Science, a Master's degree in International Relations and a Master of Arts (MA) in Law and Government of the European Union. In 2018, Zgaga was visiting researcher at the Hertie School of Governance in Berlin. His dissertation focuses on European Union (EU) fiscal and budgetary policy from a comparative federal perspective. Drawing a comparison with established federations, the research analyses the relationship between the EU and its Member States in fiscal and budgetary policy.

tzgaga@luiss.it

A THE POLITICAL ECONOMY OF GERMANY AND ITALY

THE GERMAN POLITICAL ECONOMY UNDER THE EURO - AND A COMPARISON TO THE "SOUTHERN MODEL"

Philip Manow[67]*

Bremen – Konstanz

1. Germany in the Euro Area - A New Equilibrium?

In this paper, I ask how German wage setting and, more generally, how Germany's production regime functions in the euro area. This also allows me to compare the German export-led growth model with the French or Italian models. The paper primarily covers the first decade of the new millennium, a time that not only saw the creation of the euro area and, with it, a fundamental transformation of the basic economic parameters within which the German model previously functioned. Starting in 2008 and triggered by the insolvency of Lehman Brothers, the world economy also experienced a profound economic crisis—the Great Recession. Although the comparisons with the Great Depression of the late 1920s and early 1930s that are frequently drawn (Eichengreen 2012; O'Rourke and Taylor 2013) appear a bit exaggerated, the depth and impact of the financial crisis seem to render it largely unrivalled by most other post-World War II crashes. The deep economic slump in the wake of the Lehman bankruptcy subsequently spilled over into a dramatic challenge to the euro area, manifested in the severe sovereign debt crisis of some of its member countries and, consequently, in a persistent recession (Scharpf 2011; Hall 2012; De Grauwe 2013; Hancké 2013; Streeck and Schäfer 2013; Iversen, Soskice et al. 2016; Iversen and Soskice 2018). This crisis shook and continues to shake the foundations of an economic structure to which Germany had adapted over the previous ten years.

A break-up of the currency zone, today less likely than in 2009–2011 but still a possible scenario, would have fundamental and unpredictable repercussions for the German economy and the country's public finances. Currently, the crisis lingers on and is expected to remain with us in the coming years, since European recovery would presuppose that the euro area's serious structural defects (EMU as an "incomplete" currency union; see De Grauwe 2012) be repaired. As long as this does not occur, any "return to normalcy" remains unlikely. A high level of government debt and a low level of competitiveness in southern Europe apparently either require a complete change of the euro area's institutional set-up - possibly a split into two different currency zones, one representing the northern export-led growth model under a strong euro, the other the southern demand-driven, consumption-based economic model with continuous depreciations - or will be resolved in a drawn-out process of structural adjustment and a prolonged recessive period in the periphery, possibly eased by massive transfers from the euro area's less burdened northern members (Iversen and Soskice 2018). As gloomy as both scenarios appear in economic terms, it remains wholly uncertain whether either option would even find enough support to render it politically sustainable

The paper addresses the question of how the German economy has fared in these new and profoundly challenging times. In this context, I will address the following more specific puzzles.

- If the interplay between an independent central bank with a non-accommodating monetary policy, on the one hand, and a quasi-corporatist system of wage coordination, on the other, was so central to the functioning of *Modell Deutschland* after the breakdown of Bretton Woods (Scharpf 1987; Hall 1994; Hall and Franzese 1998), how have unions and employers responded to the new environment

67* Paper prepared for presentation at the "Responses of European Economic Cultures to Europe's Crisis Politics" Conference at Villa Vigoni, 25-27 June 2018. The paper draws on the manuscript *Social Protection, Capitalist Production. The Bismarckian Welfare State in the German Political Economy, 1880-2015*, forthcoming with OUP.

where the ECB's monetary policy could no longer be exclusively targeted at German wage settlements, but was set with euro area-wide inflation in mind (Hancké 2013)?

- If the generous German welfare state is designed in such a way that the "social partners" could use or, for that matter, often abuse it for their particularistic needs (Streeck 2009), how did this close production-protection nexus survive the fundamental reform of the Bismarckian welfare state through what was known as the Agenda 2010 under Chancellor Schröder? How has Germany managed to avoid the emerging low-wage sector undermining the country's high-skill/high-productivity/high-wage regime—as unions always had feared? In other words: Can the German system function under conditions of dualisation (Palier and Thelen 2010; Emmenegger, Häusermann et al. 2012)? Apparently the answer is yes, but how exactly?[68]
- Finally, how can we explain Germany's initial economic troubles, which prevailed until around 2005, its quite spectacular subsequent comeback, *plus* its almost complete mirror image—namely the impressive boom in most southern member countries of the euro area up until the financial crisis (Italy seems to be an exception here since the Italian economy already stagnated since the early 2000s) and the bust ever since? What can the framework proposed here contribute to such an explanation, particularly with its emphasis on the interaction between social protection and capitalist production in the continental political economies (see Section 4)?

68 I will only briefly touch on the political fallout of these developments. One of the political consequences/outcomes of the profound welfare reforms was the rise and then firm establishment of a new radical alternative to the left wing of the SPD. This affected the "strategic configuration of parties" (Kitschelt) in the German party system (Schumacher 2011) (Schumacher 2011; Arndt 2013). See also (Schwander and Manow 2016).

In my attempt to answer these questions, I use the label "supply-side corporatism" (Wolfgang Streeck) to help me describe the deeply ingrained mechanisms by which the German political economy adjusts to a high interest rate environment. These mechanisms were employed when the German economy experienced its first adjustment crisis in response to the new monetary regime under the euro. I then address in some detail the profound welfare and labour market reforms that were a central part of this adjustment process (together with wage moderation), namely what was known as the Agenda 2010 (see Section 2). Subsequently, I analyse the changes in Germany's wage bargaining system under the new monetary opportunity structure, and how the welfare reforms have been conducive to the adjustment of wage coordination (see Section 3). Lastly, this gives me the opportunity to compare the *two* political economies in the euro area (the continental and the southern growth models) and to sketch how they function under the single currency (see Section 4). I relate my description of the functioning logic of these two political economies to the argument developed in previous papers, i.e., to an account of the interplay between welfare states, types of capitalism, and party competition (cf. Kersbergen and Manow 2009; Manow 2009; Manow 2013; Manow 2015; Manow, Palier et al. 2017). This enables us to locate the German political economy in a broader comparative framework.

2. The Agenda 2010 – The End of the "Bismarckian Promise"

Probably the most significant reform of the German welfare state in recent years was the groundbreaking Agenda 2010 reform, including the highly controversial labour market reforms (Hartz reforms) enacted under the red/green (SPD/Greens) coalition with Gerhard Schröder as Chancellor (Hassel and Schiller 2010; Arndt 2013: 99; cf. 99-126). Given that the relatively peaceful industrial relations in Germany have always been predicated on the welfare consensus between both Social and Christian Democracy, for many Germany in the early 2000s represented the European country where social reform was least likely (Kitschelt 2001)—despite the apparent malfunctioning of the German economy, as was manifested in low growth and high unemployment. Therefore, the comprehensive welfare reforms enacted by the red/green coalition in 2002 and 2003 came as a surprise to many observers.

In the early 2000s, Germany struggled with low growth and high unemployment. It was a time when Germany was labelled the "sick man of Europe." Real GDP growth had plummeted from 2 percent in 1998 and 1999 to 0.5 and 0.4 percent in 2002 and 2003, respectively. In 2005, the German economy was almost stagnant at 0.2 percent. In 2004/2005, unemployment came close to a staggering 12 percent and, in absolute terms, reached the critical five-million threshold.

The fact that Germany faced economic problems almost immediately after the introduction of the new currency was no coincidence, but rather the consequence of the high real interest rates that accompanied the Euro(see Krugman and Obstfeld 2012: 767, Figure 20.8): "Before 1999, Germany had not only the lowest nominal interest rates, but also the lowest real interest rates. With entry into the Monetary Union, however, these comparative advantages were lost. Since nominal interest rates converged whereas German inflation rates continued to be lower, real interest rates in Germany actually became the highest in the euro area. As a consequence, economic growth was lower in Germany than almost any other EMU member country, unemployment increased dramatically from 2000 to 2005, as did social expenditures, whereas tax revenues fell by 2.4 percentage points between 2000 and 2004" (Scharpf 2011: 13). In the rest of the euro area, credit-fueled higher demand, higher growth, and a housing bubble, particularly in Spain and Ireland, drove inflation and thereby forced real interest rates down (Krugman and Obstfeld 2012). The divergence between higher- and lower-inflation countries that had already been predicted as early as 1992 in the famous Walters Critique of the common currency evolved exactly as anticipated (Walters 1992; Carlin 2013).

The crisis could also be explained by the fact that German capital flowed to the south immediately after the introduction of the common currency. Today we are aware that this movement was driven by the mistaken belief that capital within the euro area—with its uniform interest rate, common fiscal rules, and lack of exchange rate risks—could be safely shifted to where the "economic action" was, *i.e.*, where high growth rates and therefore high returns on investments prevailed.[69] The consumption and construction boom in southern Europe was fuelled by what, from the perspective of the periphery, were exceptionally low interest rates and this attracted German capital, thus reinforcing the boom. The ECB, forced to pursue a "one size fits all" monetary policy in a currency area where both an overheated economy (Spain or Ireland, for instance) and an economy in recession (such as Germany) soon existed side by side, inevitably selected an interest rate that was too low to dampen the Spanish or Irish construction craze, but that was already too high for Germany's bleak economy (and has subsequently been dubbed a "one size fits none" rate). At a time when high growth rates, high employment, and rising real wages in the south seemed to be signs of exactly the economic convergence process that optimists had expected from the single currency - evidence of what is known in economics as the Balassa-Samuelson effect (Illing, Jauch et al. 2012) - Germany had to undergo a politically and economically painful process of structural reform.

At that time, however, Germany's economic slump in the year 2000 was not perceived as having much to do with the euro. Further, even if political actors had been aware of the underlying causes (which in all likeliness they were not), they still had to avoid at all costs de-legitimising the new currency, which had been introduced against the will of the majority of Germans. Instead, the dominant discourse held the prevailing labour market inflexibility and high non-wage labour costs, a dysfunc-

69 Martin Wolf dryly comments: "Why anybody should have imagined that Greek and German government debts were equivalent is not easy to comprehend" (Wolf 2014: 47).

tional welfare state, and, in general, a significant political reform gridlock (*Reformstau*) responsible for the poor state in which Germany's economy found itself at the start of the new millennium.

Of course, not all of Germany's poor economic performance at the time can be blamed on the new currency. It is quite apparent that Germany's GDP growth had been sluggish and its labour market performance poor even before the introduction of the euro. This was primarily part of the long-term economic fallout of a set of circumstances that were to repeat themselves after 1999 for the entire country, namely, the entry of the former East German states into the new currency zone of unified Germany at an exchange rate that was far too high.[70] It was also due to the fact that the German production model in general and the German welfare state in particular were tailored to the needs of a manufacturing sector that now, at best, produced stagnant employment, while the German growth model seemed much less well adjusted to the needs of the increasingly important service economy (Wren 2013).

When unemployment finally surpassed the four-million mark in 2002, politicians and the public were alarmed. Yet unemployment continued to increase: in 2005, 4.86 million people were without employment. This was the annual average, but in the early months of that year the total number of unemployed had actually passed the symbolically important five-million mark. What is more, long-term unemployment was also a pressing problem. This pointed to the need to reform the job placement program of the unemployment insurance and to reconsider whether the passive character of German labour market policies did not actually provide the unemployed with rather perverse incentives: "A full 32.8 percent of jobless workers between 1995 and 1999 had been on the rolls for more than a year, reflecting the ineffectiveness of the BA's [Federal Labour Office's] job placement services" (Vail 2010: 104) and also reflecting the dependency trap inherent in generous benefit levels and long drawing periods so typical of Germany's social insurance system, a system tailored to insider interests and specifically to preserving their labour market and income status. Moreover, poorly camouflaged by the fact that many jobseekers were channeled through expensive work-creation schemes or training courses of highly dubious usefulness was the fact that not only was unemployment high, but employment was also low. The high number of early retirees completes this rather gloomy picture.

Various labour market stimuli failed to tackle these problems. Efforts to find solutions in tripartite negotiations with the social partners - the traditional corporatist approach that both the outgoing Kohl government and the incoming Schröder government had attempted - proved wholly inadequate. Kohl's belated and half-hearted reform attempts were a far cry from the "radical retrenchment" as which it has been labelled in the literature (Beramendi, Häusermann et al., 2015: 40), anyway. The social partners were more interested in protecting their position within Germany's corporatist political economy than in responding to the virulent labour market crisis. During the red/green coalition's second term (after a narrowly won election in 2002), the failure to confront these problems within a tripartite framework was ultimately the catalyst for a bold attempt to enact profound labour market and welfare reforms without the social partners' consent. The reforms were designed to "wrest authority from neo-corporatist labour market institutions, which had failed to devise effective responses" to the severe employment and unemployment problems of the times (Vail 2010: 102). This is what the Agenda 2010 and the Hartz reforms accomplished. They therefore decisively withdrew from the corporatist model that had dominated the German political economy for the last 50 years and in important respects reneged on the "Bismarckian promise" that had prevailed in the previous five decades.

70 What subsequently developed was high unemployment, a massive increase in public spending (active and passive labour market policies), a unification boom, and the *Bundesbank*'s harsh monetary reaction, which led to a prolonged period of poor economic growth and low employment .

I refrain here from providing a detailed account and full evaluation of the Agenda 2010 measures - given that there are already a plethora of detailed assessments (Clasen 2005; Clegg and Clasen 2006; Clegg and Clasen 2006; Eichhorst and Kaiser 2006; Hassel and Schiller 2010; Vail 2010; Arndt 2013; Carlin, Hassel et al. 2014; Hassel 2014; Schwander and Manow 2016). A simple outline of the major reform measure must suffice. The first two Hartz laws, enacted in 2003, placed a stronger emphasis on labour market activation through the introduction of personnel service agencies (*Personal service Agenturen*, PSA), and opened activation measures, previously limited to recipients of earnings-related benefits, up to everyone (Carlin, Hassel et al., 2014: 63). At the same time, benefit requirements were tightened: once a spell of unemployment lasts longer than 18 months, the unemployed are now forced to accept any available job, regardless of their qualifications and previous pay (Koch, Kupka et al. 2009). Availability and entitlement criteria were also tightened, and the annual adjustment of benefits was abolished (Eichhorst and Kaiser 2006). Additionally, the reforms comprised a number of smaller policy measures promising to increase labour supply and to make accepting employment worthwhile. Measures included the reduction of social contributions on low-paid jobs and marginal employment (what were known as "minijobs"). Another activation measure was the introduction of what were dubbed "Me Inc." or "Ich-AGs", *i.e.*, a measure facilitating the creation of small (also single person) enterprises. The third Hartz law reformed the public placement agency (Public Employment Service) in order to improve its case management and the placement of jobseekers.

The last and by far the most controversial and important part of the reform, the Hartz IV law, sharply reduced the drawing period for the generous earnings-related unemployment benefit (*Arbeitslosengeld I*) from a maximum of 32 to 12 months (18 months for older unemployed persons). After this period, the unemployed have to rely on the flat-rate, means-tested benefit, *Arbeitslosengeld II* (also known as Hartz IV), which corresponds roughly to the level of the former social assistance, i.e., it does not take the level of prior earnings into account, and by consequence also not the length of the prior period of employment and contribution payment.

As a consequence, the reform fused the previously separated systems of social assistance and unemployment insurance. "This meant that status protection of the long-term unemployed was abolished in favour of a joint flat-rate benefit for all jobseekers not entitled to unemployment insurance benefit, *i.e.*, with prior employment shorter than the waiting period or after expiry" of *Arbeitslosengeld I* (Eichhorst and Kaiser 2006: 9). It cannot be stressed too much that this represented a very substantial attack on insider interests. At the same time, due to the reform, benefit recipients have to accept any job offer to prove their willingness to work, even jobs paid so poorly that the wage will remain below the social assistance level. Wages are then topped up by transfer payments.

Considering that the "old" welfare system had been geared primarily to the protection of status, income, and the qualifications of skilled workers, these measures clearly represented a major break with Germany's "Bismarckian tradition" and violated the interests of the workers in the industrial core - a traditional SPD support base. The reform qualifies as a "dramatic shift from the status-preserving earnings-related principle to the means-tested basic-income principle for the long-term unemployed" (Carlin, Hassel et al. 2014: 63). These reforms therefore represent a significant break with cherished principles of Germany's welfare system. It is no surprise then that they met with vehement union protest and were highly contested within the Social Democratic Party. In fact, they were enacted against a sizeable intraparty opposition of "traditionalists" clinging passionately to Germany's established Bismarckian ways. From this it also becomes clear that one of the key aims of the Agenda 2010 was precisely *not* to "sharpen the lines between social *insurance* (for those who had paid the social contributions) and social *assistance* and in-work benefits for those excluded from the normal labour market and for whom the state was asked to take responsibility" (Palier and Thelen 2010: 122). The objective was the exact opposite, namely *to blur* these lines. To interpret the welfare reforms, as Thelen and Palier do, as an attempt to protect the industrial core model of the German political economy is therefore wholly misguided (see also Carlin, Hassel et al. 2014: 66; Beramendi, Häusermann et al. 2015: 40).[71]

Despite the reforms—or because of them (see below)—Germany violated the Maastricht three-per-cent budget deficit criterion in the years 2002 to 2005, in the midst of the recession. "There was not just a little irony in this fact, since in the early 1990s it had been German negotiators who had pushed to include an Excessive Deficit Procedure in the Maastricht Treaty" (Eichengreen 2007: 372). In the ensuing conflict with the European Commission, Germany and France successfully negotiated a less restrictive application of the Stability and Growth Pact. In retrospect, many interpret this as the euro area's "original sin" (cf. James 2012: 18), which paved the way for a period of low fiscal discipline and which ultimately - in the wake of the financial crisis in 2008/2009 - allegedly led to the profound sovereign debt crisis that threatened and still threatens to tear the euro area apart. Although Greece's entry into the euro area, based on grossly forged budget data, is certainly a serious contender for the "original sin" award, and although the crisis of the Eurozone in its essence never has been a sovereign debt crisis (Baldwin and Giavazzi 2015), it is true that the outcome of the conflict between France and Germany, on the one side, and the Commission, on the other, made future sanctions against other euro area members who violate the Maastricht criteria hard to justify and quite unlikely to be imposed. In fact, in 2005 "the disciplinary mechanism was softened, many processes became merely discretionary, and new procedural provisions made it harder to take action against noncompliant states" (James 2012: 18). As Paul De Grauwe dryly states: "For all practical purposes, the Pact had become a dead letter" (De Grauwe 2014: 227).[72]

Politically, the German government saw its violation of the Stability and Growth Pact as the *consequence* of the pending welfare state reforms. As Chancellor Schröder later explained, the red/green coalition was confronted with a dilemma:[73] embarking upon a policy of structural reform by pursuing a highly unpopular welfare reform *and* simultaneously aggravating the recession with a strict policy of fiscal consolidation would have simply spelt political disaster and certain electoral suicide. Forced to choose, the Schröder government opted for the long-term structural change: welfare reform. In retrospect, it is probably fair to say that Schröder was proven right - economically, if not politically - since he was voted out of office in 2005 anyway.

71 The fact that unions/works councils and employers/firms in fact frequently protected the core workforce through plan-level agreements is another issue.

72 De Grauwe (2013) also caustically comments on the regulations of the old and the new Stability and Growth Pact: "Up to now, these sanctions have never been applied. The reader will be surprised at so much political naiveté from the drafters of the Stability and Growth Pact when they believed that such sanctions could ever be enforced" (De Grauwe 2014: 217).

73 SPIEGEL: "The ECB accuses you of having softened the criteria of the Stability and Growth Pact." Schröder: "This critique has to be taken seriously. But one has to put it into perspective. We strengthened the growth aspect of the Pact with that reform. Specific burdens, such as the costs related to German reunification, now had to be taken into account. More importantly however, countries which undertook difficult structural reforms had more leeway to stimulate growth. For us Germans, this was key, since we had initiated the Agenda 2010. In Germany, we were confronted with a stagnating economy. At the same time we were very determined to push this reform through and to adjust the welfare state to the changed circumstances. Hence, we needed to emerge from stagnation with the help of an economic stimulus package. In this situation we were forced, also because of the welfare reforms, to emphasize the growth component of the Pact. In the end this proved to be successful. We did our homework with the Agenda 2010. This is one of the reasons why we came through the crisis better than others. Countries such as France or Italy are now forced to catch up under much more unfavorable circumstances" (Spiegel, "Europa muss aufwachen," 5 September 2011.

The combination of structural reforms, rationalization in firms, and the wage moderation practiced by unions ultimately led Germany out of the recession, particularly in combination with the much higher growth and more specifically the much higher wage growth in Europe's south. German GDP grew at an impressive rate of 4.1 and 3.1 per cent in 2006 and 2007, respectively, before the financial crisis hit the German export-based economy unusually hard. However, even the Lehman crisis only temporarily interrupted the revival of *Modell Deutschland*. As soon as global demand returned, German companies were able to overcome the massive external shock caused by the financial crisis. The country came out of the recession much faster than the UK or most other euro area members - although the subsequent recession in Europe's periphery did not leave German growth unaffected, of course (see Figure 3).

The labour market also weathered the storm remarkably well (Burda and Hunt 2011; Eichhorst and Tobsch 2014: 3). The level of unemployment sank steadily and today (September 2017) is at around 5.5 per cent (national figures; according to the ILO definition the German unemployment rate is 3.7 per cent) - less than half of the 12 per cent unemployment that was recorded at the peak of the crisis in 2005. Today's figure of around 2.45 million unemployed and 800,000 open jobs prompt German labour market experts to consider a full employment scenario to be possible in the foreseeable future (see Figure 2).[74]

Significantly, the higher labour market flexibility resulting from the Agenda 2010 reforms did not - as reform critics had claimed - come at the cost of undermining the "normal" segment of the labour market. In the private sector there is a relatively high probability that people will transfer from the non-standard segment of the labour market to its regular core. This regular core appears to have been strengthened rather than weakened by the reform.

74 Of course, the massive influx of almost one million immigrants in the second half of 2015, most of them poorly qualified, changes this picture substantially.

The number of "regularly employed," meaning those subject to mandatory social insurance contributions, even increased significantly from its low point of slightly more than 26 million in 2005 to 32.1 million in September 2017 (cf. Figure 1). Inequality, which had been steadily increasing since the 1990s, has been on the decline since 2006 and poverty rates have decreased, too. For instance, the GINI coefficient fell from 32.8 (2006) to 30.1 (2011) and has dropped further since, and the poverty rate fell from 9.1 to 7.8 between 2007 and 2013 (e.g., OECD 2015: 56).[75] The claim that the reform increased "German inequality quite dramatically" (Blyth 2015: 269) is wholly unsubstantiated.

Total employment is also at a record high of around 44.5 million people. With an employment rate of 76 per cent, in Europe, Germany is now second only to Sweden, and quite unlike its conservative homologues, France and Italy (Eichhorst and Tobsch 2014: 6-7). It was this high employment rate which then also helped fuel domestic demand during the crisis when export demand collapsed. Full-time, non-temporary employment is still the dominant form in the German labour market, specifically for 40 percent of working-age individuals and for 60 percent of those in gainful employment (Eichhorst and Tobsch 2014: 10). The overall job growth, however, came at the cost of a significant increase in non-standard employment. Yet, if we want to bemoan this development, we should bear in mind how high structural unemployment had been previously. We also should take into account that "non-standard jobs contribute to better labour market access and additional job creation, which generates additional income from work. Flexible types of contracts also contribute to wage moderation in collective agreements and to overall competitiveness" (vgl. Klinger, Rothe et al. 2013; Eichhorst and Tobsch 2014: 4). Moreover, for many, particularly mothers, part-time employment is the preferred form of employment, and does not lead to an accumulation of social risks (Böhnke, Zeh et al. 2015).

75 See for instance, World Bank: http://data.worldbank.org/indicator/SI.POV.GINI?locations=DE or (OECD 2015).

With these more flexible forms of employment the Agenda 2010 managed to reduce the inactivity rate, which was their biggest achievement (Klinger, Rothe et al. 2013). Inactivity, widespread in the 1990s, "is no longer a problem of the German labour market" (Hassel 2014: 68). While the overall flexibility of the labour market has clearly increased, average job tenure has not only remained stable but also even increased, from 10.3 to 11.5 years between 2000 and 2011 (Eichhorst and Tobsch 2014: 13) - mainly due to the fact that the Agenda 2010 and subsequent reforms rendered many routes to early retirement much less attractive, but also because in 2007, another deeply unpopular reform measure raised the retirement age to 67. It is important to note, however, that high employment, low inactivity etc. were as much due to a favourable economic climate (weak euro, eastern enlargement of the EU, and low interest rates) as to the flexibility of the labour market promoted by the reforms.

At the same time, the rapidly increasing low-wage sector (see Rhein 2013) is the more worrying development for many, but even here opinions vary. Some emphasise that "the liberalization of non-standard contracts has contributed to the expansion of overall labour market inclusion and job growth in Germany and that at least some forms of non-standard work provide stepping stones into permanent regular jobs. Atypical contracts do not necessarily undermine the dominance of standard employment relationships and job quality in this primary segment but rather form a supplementary part of employment in sectors that depend on more flexible and maybe cheaper forms of labour" (Eichhorst and Tobsch 2014: 2). Not surprisingly, the reforms also created the need for some re-regulation, and the introduction in 2014 of a binding wage floor (minimum wage) for many labour market sectors is one of these re-regulating measures. Interventions like these moved the German political economy further away from one of its formerly sacred principles - that of *Tarifautonomie* or autonomy of the social partners in wage bargaining. Germany became less corporatist.

There is no doubt that the welfare reforms created real "losers" - in fact, they were designed to do precisely that, but those were, contrary to the expectations of many, rather the labour market insiders. Some categories of households benefit substantially from higher transfers (Koch, Kupka et al. 2009: 249-50) and overall spending on social assistance significantly increased after the reform: "Hartz IV - widely considered the harshest of the recent reforms - actually provided a boost for an estimated one-third of those who were previously in the lowest tier of the old social assistance system," particularly single mothers (Palier and Thelen 2010: 138).[76] Whereas these former 'outsiders' benefited, insiders also lost out considerably. Against all conclusions of "dualization," the reform "clearly and most drastically cut the benefits for well-insured labour market insiders" (Beramendi, Häusermann et al. 2015: 41).

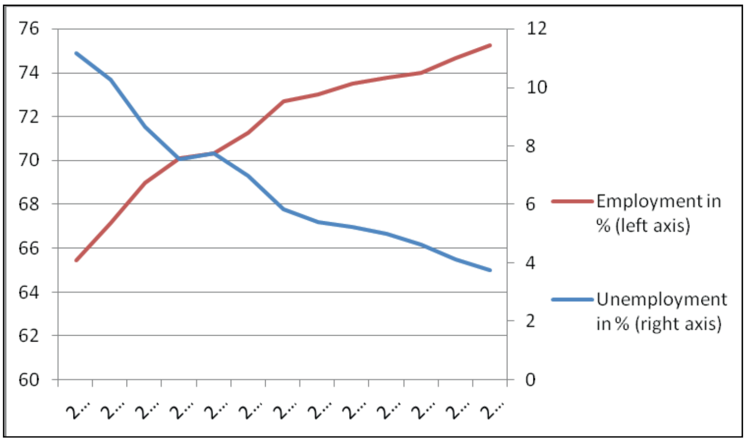
Not surprisingly, the reforms were highly controversial, and this is reflected in the conflicting assessments of these reforms still found in the literature today. Whatever might be the final assessment of the reforms, given the substantial pathologies of Germany's prior "welfare without work" model even critics of the Agenda 2010 can hardly deny the urgent need for reform in the early 2000s. Labour market performance since then also tends to discredit some of the initially very critical assessments of the Agenda: higher flexibility apparently *did* contribute to the employment growth that reformers had wished for, and so far without undermining the core of regular employment. It therefore appears rather questionable to

76 Combining unemployment insurance and Germany's social assistance scheme involved a huge cost shifting game between the municipalities, which were responsible for social assistance, and the social insurance schemes (Hassel and Schiller 2010). The process conformed to the pattern described in Chapter 6 above: the political incentive to substitute social insurance contributions for taxes. Municipalities had an incentive to declare as many recipients of social assistance as "employable" as possible. In some instances, comatose patients miraculously turned into active "jobseekers." Whereas the federal government had anticipated less than 3.5 million employable recipients of ALG II/Hartz IV, in the end it was more than 5 million. The welfare state "retrenchment measure," the Agenda 2010, increased social assistance spending dramatically to 25 billion euros —11 billion more than anticipated.

accuse the Agenda 2010 of having strengthened "dualization" (Thelen 2014) without at the same time referring to the disheartening and unacceptable exclusion of a very high number of long-term unemployed under the *status quo ante*. To put it more specifically: a prior "dualization" between those in and those not in employment has been substituted by today's "dualization" between those in stable and those in marginal employment, and it seems strange to assess the one without alluding to the other (or to describe only the latter as "dualization"). Moreover, most labour market indicators prove the higher employment dynamics today as compared to pre-reform times.

In an evaluation of the reforms from a political point of view, both critics and proponents would probably concur that the labour market after the Agenda 2010 reforms is in a situation that is "fundamentally different from the situation in the late 1990s and early 2000s" (Eichhorst and Tobsch 2014). According to established performance criteria such as employment and unemployment, youth unemployment, female labour market participation, and average retirement age, it can be stated that Germany today is no longer "adjusting badly" (Manow and Seils 1999). Again, this overall assessment would not only have to make reference to the domestic reforms, but also be put into the context of the new monetary environment, which became much more favourable for the German political economy after 2005 (see below).

Figure 1: Employment and Unemployment rate, 2005-2017, in thousands



Source: OECD (https://data.oecd.org)

However, the return of growth, the turnaround of the German economy, and the substantial reduction in the number of unemployed and inactive persons came too late for the red/green government. In 2005, Schröder was forced to call new elections after having lost the large state of North Rhine-Westphalia, which had been traditionally Social Democratic. With this state now in the hands of the oppositional Christian Democrats, a two-thirds majority of the opposition in the *Bundesrat*, Germany's second chamber, became a likely scenario. With such a majority, the CDU/CSU-FDP opposition would have been able to block *any* government initiative (according to Article 77, Section 4 of the Basic Law for the Federal Republic of Germany, *i.e.*, the German constitution).[77] Schröder decided that attack was the best form of defence. In the early federal elections of 2005, the share of the vote of the red/green coalition suffered. However, the opposition, which in the meantime had decided to rally around an even more radical reform platform than what the Agenda had brought, also lost vote shares (see Table 1).

Table 1 Bundestag elections, overview of results, 1994-2013, in per cent

	1994	1998	2002	2005	2009	2013
SPD (Social Democrats)	36.4	40.9	38.5	34.2	23.0	25.7
CDU/CSU (Christian Democrats)	41.5	35.1	38.5	35.2	33.8	41.5
FDP (Liberals)	6.9	6.2	7.4	9.8	14.6	4.8
Grüne (Green)	7.3	6.7	8.6	8.1	10.7	8.4
PDS/die Linke (ex-Communists)	4.4	5.1	4.0	8.7	11.9	8.6
Turnout	79.0	82.2	79.1	77.7	70.8	71.5

Numbers indicate the share of valid votes.

Source: www.bundeswahlleiter.de (Federal Returning Office).

While voters apparently punished the Social Democrats for their reform agenda, they showed little enthusiasm for the CDU's attempt to posi-

77 Parliament can only override a two-thirds majority veto of the second chamber by finding/securing a two-thirds majority itself, which is a completely unrealistic prospect.

tion itself as even more "de-regulative" than the Schröder government. As a consequence, the race was extremely close, and neither a centre-right (CDU/CSU/FDP) nor a centre-left (SPD and Greens) coalition gained a majority of seats. The upshot was that a Grand Coalition then ruled from 2005 to 2009. The Christian Democrats, however, had learned their lesson: in 2009, Chancellor Angela Merkel moved the Christian Democrats' program back to the centre. Given that in 2009 the genuine "left-wing", orthodox anti-reform position was occupied by *Die Linke*, a party which had easily surpassed the German legal five-percent threshold in the 2005 election thanks to the lack of popularity of the Agenda 2010 in the traditionalist left milieu, the Social Democrats were crushed from two sides. There was little room left in the political centre for a Social Democracy that under Schröder had once claimed - in imitation of Blair's New Labour - to represent the New Centre (*Die neue Mitte*) after Merkel ultimately decided to abandon her short flirt with a neoliberal agenda.

In hindsight, the SPD's electoral disaster was predictable, partly because a Social Democratic minister of labour had not only been responsible for important labour market reforms between 2002 and 2005, but also for another hugely unpopular measure: the decision in 2007 to increase the retirement age to 67. However, the onset of the global financial crisis in 2009 also played into the hands of the CDU chancellor, since German voters are known to become more conservative in times of economic crisis (Anderson and Ward 1996).

3. German Wage Bargaining within the Euro Area

In order to put the Agenda 2010 reforms into a broader economic context, we need to examine them in relation to the changed monetary incentive structure in the euro area. With respect to the nexus between monetary policy and industrial relations, it is important to note that relatively high interest rates and their recessive consequences had not been perceived as the sole cause of Germany's economic troubles in the early 2000s. High interest rates were interpreted as responses (of an independent central bank) to inflationary tendencies, possibly provoked by exaggerated wage increases. It appeared that poor economic performance pointed instead to the lack of competitiveness of German firms and products as the root cause of all the country's economic troubles.

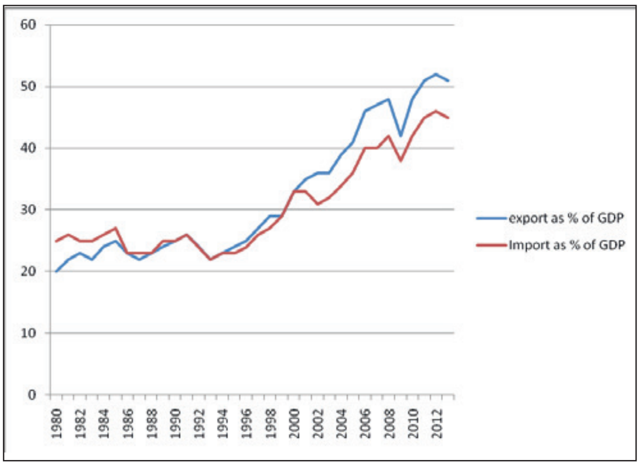
Having been "socialized" with the implicit supply-side logic of *Modell Deutschland* in the post-Bretton Woods world where the *Bundesbank*'s independence and its hard currency policy ruled supreme (Scharpf 1987; Hall and Franzese 1998; Franzese 1999), the relevant German actors, both in the political and economic spheres, believed that interest rates were not too high, but wages and welfare benefits were. Subsequently, monetary policy did not have to be adjusted, but German wage costs did. Adjusting monetary policy was considered a taboo, at any rate, given the independence of the European Central Bank, which had been modelled on the *Bundesbank* (James 2012).

Initially, the immediate post-euro recession thus seemed to present German unions, employers, and politicians with a familiar challenge. The well-established interplay between wage bargaining and monetary policy could not be continued under the new circumstances of the euro, given that the ECB would not and could not target its monetary policy exclusively on pilot agreements between German employers and unions – as the *Bundesbank* had done in the past. However, in the high interest rate environment of the early 2000s, German social partners felt that the circumstances they found themselves in were, if not comfortable, then at least familiar (Hall and Franzese 1998). What has been succinctly labelled Germany's "supply-side corporatism" (Wolfgang Streeck) kicked in: Germany experienced wage moderation and productive company-level pacts concluded by the social partners, productivity-enhancing rationalization and, in part, relocation of firms, and finally the welfare reforms enacted by a Social Democratic government. It is worth highlighting that this latter aspect of the adjustment process, namely the profound welfare reform enacted by the red/green coalition, was a rather new element, something from which the CDU under Helmut Kohl had largely shied away. Thus it signified a major deviation from the course of earlier politics and also from the established approaches of social policy.

By creating space for the emergence of a large low-wage sector, the labour market and welfare reforms themselves subsequently exerted pressure on the unions and thereby further contributed to the wage restraint of the social partners. Of course, the boom in Europe's periphery and the ensuing significant increase in labour unit costs there helped restore the cost competitiveness of German industry as well - while the cost pressures stemming from eastern enlargement also helped keep German wages under control. The new, much poorer members of the European Union provided Germany with new product markets, but in particular with a supply of cheap production factors. Business relocation to the East or the threat of it helped German firms to keep their wage costs under control, as did the import of cheap labour under the EU Posting of Workers Directive.

The monetary parameters for the German model changed profoundly again when the banking crisis eventually translated into a sovereign debt crisis for some of euro area member states. The subsequent expansionary policy of the European Central Bank, the low interest rate environment, the (from a German perspective) undervalued euro, the massive repatriation of capital from the periphery to the centre: taken together, all this boosted German investment and production substantially (Wolf 2014: 63). Germany's recent record-high trade surplus (see Figure 2) is therefore to some extent the *result* of the euro crisis, not its cause, which also means that it cannot be explained by only referring to superior economic performance.[78] Just as everything that was wrong with *Modell Deutschland* in the early 2000s could not be blamed on the new currency, it is also impossible to explain today's spectacular economic revival of the German economy by exclusively citing the inherent strengths of *Modell Deutschland*.

Figure 2 German Exports and Imports as a percentage of GDP, 1980–2013



One component of this situation is undoubtedly that German euro area partners can no longer devaluate their currency in order to rebalance their current accounts *vis-à-vis* Germany - rendering strategies of wage moderation by German employers and unions now even more effective than they had been under the flexible or fixed, but adjustable exchange rates of the past (Höpner and Lutter 2014). Painful and unpopular "internal devaluation" is the only option left to Germany's euro partners (De Grauwe 2013; De Grauwe 2014; Iversen and Soskice 2018: 12). While countries like France or Italy had hoped

78 To the extent that the German current account surplus has to be explained by interest rates that were too low and a euro that was undervalued, at least from a German perspective, both of which were the result of the ECB's rather accommodating monetary policy, the European critique of Germany's current account imbalances appear contradictory. The fact that a euro that is "too weak" for German industry is still "too strong" for the French or Italian exposed sectors has more to do with the low external value of the US dollar, the yen, and the British pound due to the massive quantitative easing programs of their banks.

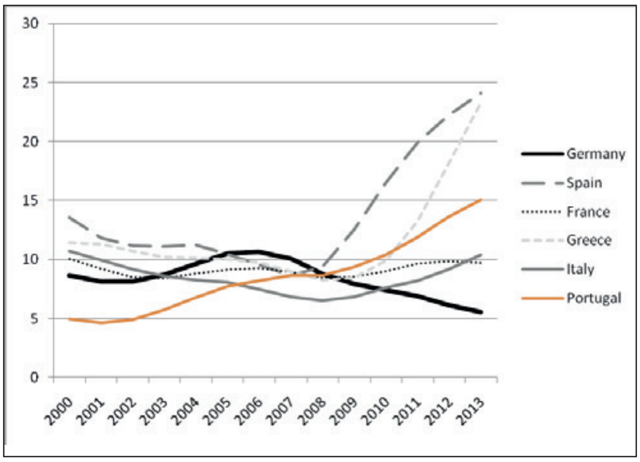
that the EMU would replace the *Bundesbank*'s *de facto* monetary hegemony within the EMS with a more lenient European monetary policy, at the same time, the common currency exposed their economies to full, unfettered competition from German industry and foreclosed the devaluation option in response to inflationary wage settlements at home.

Yet, it is important to emphasize that this very situation had been an anticipated, intended, and welcome consequence of monetary union. Italian and French government representatives hoped that the disciplinary effects of the common currency would help them keep wage inflation under control, given that national monetary and political authorities in the past had tended to give in too quickly to unions' aggressive wage demands (see De Grauwe 2012). These self-binding effects of the currency union were quite obvious from the beginning, as, for instance, Daniel Gros and Niels Thygesen had already remarked in 1998 in what was to become one of the classic textbook on monetary union: "In sum, labour market flexibility is always useful and if EMU forces labour market reforms that are needed anyway, the economy of EU can only gain" (Gros and Thygesen 1998: 288). Bemoaning the euro's de-regulatory effect on southern European industrial relations seems therefore to be rather a case of "dynamic inconsistency."

The absence of a devaluation instrument within the euro area certainly made German (Nordic) wage restraint more effective. Wage constraint, "combined with heavy investment in training … propelled northern Europe - Germany in particular - to a hegemonic trade position within Europe" (Iversen and Soskice 2018: 12). This has contributed to an erosion of the industrial base in the euro area periphery, the converse being the slight reversal of the long-term decline of employment in manufacturing in Germany. German industrial production increased by 8.7 per cent from 2010 to 2014, whereas in Italy and Spain, it declined over the same period by 7.7 and 7.2 per cent, respectively. The manufacturing sector in 2013 accounted for 22 per cent of German GDP and 10 per cent of French GDP, and for 28 and 22 per cent of total employment in Germany and France, respectively.

Generally, since the introduction of the common currency, the labour markets in the centre and in the periphery developed in a counter-cyclical fashion. German unemployment was high when it was low in the rest of the euro area and started to decline when it rose in the south—one of the many asymmetries indicating that the euro area is anything but an Optimal Currency Area (see Figure 3).

Figure 3 Standardised unemployment rates in euro area member countries, 2000-2013



As we have seen, during the first years of the euro area the monetary environment for German unions and employers' associations was not completely unfamiliar. The traditional German model could work reasonably under the ECB's high interest rate regime (that is, high for sluggish Germany). What about the period after 2005 though, when the ECB's interest rates became too low and accordingly the euro too weak for the booming German economy? If the German export-led growth model presupposes wage moderation, but the ECB cannot substitute the *Bundesbank*'s disciplinary monetary policy, how do unions and employers secure a moderate development of wages? The answer to these questions can be divided into several components. First, it is possible that the erosion of the German wage bargaining system

(Streeck 2009), *i.e.*, its increasing devolution to the company level, actually explains its continuing capacity to deliver wage moderation. Second, the disciplining effect of the Agenda 2010 labour market reforms is also worth mentioning. Further, the moderating effect of eastern enlargement and of the currency union itself, and finally the disciplinary consequences of crisis-induced immigration should also be acknowledged. Let me briefly elaborate on these points.

Ironically, the more limited coverage of wage negotiations, due to the erosion of membership both of the unions and the employers' associations, could turn out to be an explanation for the continuing capacity of the German political economy to moderate wages. Since the 1990s, German collective wage agreements have been largely substituted with company-level agreements or what are known as firm-level "productivity pacts" (Rehder 2003). They replace employment guarantees by employers with workers' consent to rationalization, partial relocations, increased labour flexibility, and so on. If we are looking for an explanation for how the German economy continued to deliver wage moderation during times when the familiar strategic interaction between social partners and the central bank had ceased to function, it is important to emphasize the fact that the "control of labour costs in the German industrial relations system shifted over time from the dominance of coordinated wage setting institutions to competitiveness-driven plant level adjustment" (Hancké 2002; Hassel 2014: 26; Hassel 2017 (forthcoming)). The erosion of Germany's wage coordination system would then not be an indication of a fundamental change of *Modell Deutschland*(Streeck 2009), but a necessary precondition for the model to function as it had previously, albeit under profoundly different circumstances.

This insight helps us to explain a second, *prima facie* puzzling aspect of Germany's economic recovery after 2004. Whereas the poor labour market dynamic in the 1990s was due to particularly weak job growth in the (low-skill, low-productivity) service sector, the recent strong increase in the employment rate (Germany's job miracle) and the corresponding low degree of inactivity were to a large extent due to the striking expansion of the low-wage labour market segment, primarily in services. This labour market dynamic had previously been hindered by union wage coordination, restrictive employment protection rules, and the high "replacement rates" implicit in the generous regulations of the unemployment insurance scheme, which were tailored to insider interests (Rueda 2005; Rueda 2006). Once the Agenda 2010 reforms removed these protective features removed, low union density and low productivity in the service sector combined to bring about unforeseen job growth in the third sector, keeping the costs of living down and thereby supporting wage moderation in manufacturing, too.

The result was a *sectoral* dualization of the German political economy - that is, the maintenance of the traditional German model in manufacturing and simultaneously the "deregulation" of the service sector - which many observers, including the author, (cf. Manow and Seils 1999) for many years considered quite unlikely, if not outright impossible. The "frozen landscape" that Esping-Andersen described when analysing the conservative political economies of continental Europe in the 1990s (Esping-Andersen 1999) has given way to a political economy with employment rates very similar to the high Scandinavian levels. Given that Germany's Bismarckian welfare state is still based on employment and payroll taxes, today's quasi full employment scenario also helps to control the welfare state costs.

Further, the wage discipline of German workers in the 2000s is certainly also due to monetary union itself, since regional economic integration, admittedly evolved over many decades, substantially intensified under the EMU and further increased with European enlargement in 2004. Both events lend momentum to the establishment of a new economic region that integrates new member states from Central and Eastern Europe with the German economy, but also increases integration with the Baltic and Benelux states. German trade "with the new member states of the EU increased from 2 percent to more than 7 percent of GDP between 1994 and 2006. During that period, intra-firm trade represented about 21.6 percent of imports from Eastern Europe" (Hassel 2014: 63). Some observers even maintain that the new ways of "organising production by slicing up the value chain has been more important for Germany's lower unit labour costs than German workers' wage restraint. According to estimates, German off-shoring to Eastern Europe boosted not only the productivity of its subsidiaries in Eastern Europe by almost threefold compared to local companies, but it also increased the productivity of the parent companies in Germany by more than 20%" (Marin 2010).

Wage development within this emerging, larger economic region *could* be taken into account by the ECB's monetary policy. To the extent that the ECB *did* take German wages into account, while "Germany's neighbours effectively targeted [these German wages] to hold down their own wages … the northern European countries could pursue the export-led growth strategies to which they had long been accustomed with considerable success" (Hall 2012: 358-359). This pattern was considerably strengthened in the first decade of the euro.

Now that (relatively) high growth and low unemployment have returned to Germany, we should not expect that unit labour costs will increase as steeply as they did during the boom in southern Europe. They will increase, but it seems safe to predict that they will remain largely in line with productivity and international competitiveness. We can therefore assume that the German wage setting regime is still able to deliver wage moderation quite effectively, since functional equivalents to the monetary signals of the *Bundesbank* and the traditional system of pattern wage bargaining seem to have been put in place: competitive firm-level pacts, the relocation and regional economic integration of firms, the liberalization of the service sector, the price pressure of international markets, etc. With the anticipated inflation firmly anchored around two per cent or lower, German unions do not need strong monetary signals to figure out which wage hikes are likely to harm the international competitiveness of industries, sectors, or companies.

Finally, the crisis itself appears to contribute to German wage restraint: while the labour inflow from Europe's periphery in the wake of the crisis is insufficient to bring relief to southern labour markets, it is apparently enough to ensure that labour supply meets Germany's increased labour demand. In 2013, Germany welcomed around 400,000 new immigrants, a number only surpassed by the US - and in 2015 more than a million migrants arrived, with similarly high numbers in 2016.[79]

In sum, even if the ECB were to pursue a much more accommodating monetary policy, this would be unlikely to result in German wage inflation to the extent that the boom in southern Europe did after 2000. It is more likely that the strength of German industry would be reinforced under a lax monetary policy (due to what would then be a weak external value of the euro). This points to the systematic differences in wage setting regimes in the coordinated "hard currency" north of the euro area as compared to the largely uncoordinated "soft currency" south (Hancké 2013; Höpner and Lutter 2014; Iversen and Soskice 2018), which have been at the heart of the crisis. I will now analyse these differences.

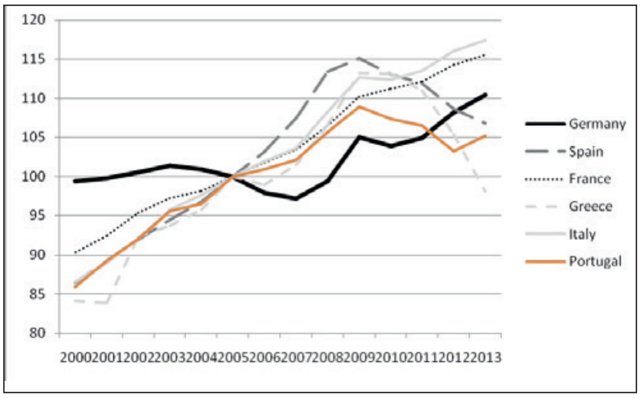
4. One Currency, Two Political Economies

The fact that in pre-crisis times German unit labour costs remained stagnant or even decreased (see Figure 4), whereas in most other countries

79 In this respect, a parallel between the early 1950s and the 2010s can also be observed/identified: a steady inflow of qualified workers enabled Germany to combine full employment with low inflation. However, the massive inflow of refugees in 2015 (estimated at 1.3 million) is quite another issue. This will translate into a huge quasi-Keynesian push for domestic demand - and integration into the labour market of these mainly poorly skilled people will take an extremely long time.

of the euro area they increased, was something that had initially been interpreted as a welcome economic convergence, given that wage levels in the south were way below the German level at first (Illing, Jauch et al. 2012). In retrospect, Germany's European neighbours have severely criticized the country's economic and political adjustments to the slump of the early 2000s as a strategy of unfair labour cost dumping. The adjustments are not considered a solution to the problem but are accused of being a cause of the widening competitiveness gap between the centre and the periphery in the currency zone.

Figure 4: Unit labour costs, 2000-2013 (index with 2005 = 100; source: ECB)



From a "northern" perspective, in turn, Italian, Spanish, or French labour had simply become too expensive, a trend concealed for some time by massive capital inflows (Hall 2014). Unable to moderate wages, fragmented and militant unions in these countries successfully pushed for wage settlements significantly above productivity growth plus inflation, thereby steadily undermining their industry's competitiveness. Because of their incapacity to correct for this through (nominal) currency depreciations within the euro area, countries in the periphery are now forced to pursue a painful process of real depreciation.

Whether German wages are "too low" or southern wages "too high" is a debate in which it is not necessary to take sides (in fact, both assessments are accurate and tautologically have to be accurate if the comparison is restricted to the euro area only). With very different degrees of export dependency, German employers (and policy-makers) have to be much more sensitive about German wages than, say, French or Italian employers and policy-makers (Scharpf 2017). However, what is more central to my argument is the fact that the discussion about deflation in the south or reflation in the north points to profound differences in the two political economies, particularly with respect to their different abilities to deliver wage moderation. In fact, these differences explain why countries such as France and Italy pushed for a single European currency in the first place - it was intended to represent the ultimate credible commitment to break with the inflationary cycles inherent to their political economies.[80]

Before the euro, the "typical situation in the high-inflation countries usually involved powerful (or, at the very least, highly militant) labour unions that managed to extract high wages from employers, both in the public and in the private sector (high wages are defined here as wages that grow faster than labour productivity). Since employers passed on these wage increases through higher prices (or rising budgets), higher wages led into the next inflationary cycle, where they would be raised again to reflect higher inflation, and so on, ad infinitum" (Hancké 2013: 16). High inflation rates then regularly triggered devaluations to regain price competitiveness. Yet these devaluations could only provide temporary relief. A weaker currency translates into increased costs of living through higher prices for imported goods, and unions, both strong and militant ones, are then eager to compensate for the decrease in workers' real wages with higher (nominal) wages, which, in turn, initiates the next round of inflationary wage-price dynamics (Carlin and Soskice 1990, Chapter 12; De Grauwe 2013). The competitive advantage of each devaluation quickly dissipated in the next inflationary wage-price spiral.

80 It is therefore not true that the founders of the EMU were insufficiently aware of the profound differences between the political economies of the EMU members (see Hall 2014). They were simply overoptimistic about how smoothly the anticipated adjustment process would take place.

It was the desire to break out of this inflationary cycle and to credibly commit to a low inflation equilibrium, with the anticipated consequences for domestic wage bargaining regimes, that motivated countries such as Italy and France to pursue the single currency strategy, since the EMS, already described by Stanley Fisher as an "arrangement by France and Italy to accept German leadership, imposing constraints on their domestic monetary and fiscal policies" (quoted in James 2012: 208), had failed to fully deliver low inflation and exchange rate stability (cf. Eichengreen 2007: 283).[81] Instead, France and Italy were forced to devaluate the Franc and the Lira several times, something which - apart from the fact that depreciations provided only temporal economic relief - was perceived as damaging national prestige.[82] The view that periodic devaluations were (and are) an essential precondition for the functioning of the soft currency political economies in Europe's south does not seem to be fully accurate, therefore (Scharpf 2011). It was precisely the intention to overcome these recurrent episodes that motivated key Italian and French actors to opt for a common currency. It is unsurprising then that these actors have not proven to be particularly eager to regain the devaluation option, but are more interested in expanding their *fiscal* leeway (Iversen, Soskice et al., 2016).

What the relevant political actors in the south did not anticipate, however, was that the much stricter constraint, the "irrevocable" commitment to a common currency, would still not be sufficient to constrain domestic wage bargaining - at least not instantly. This commitment would only become binding at a later point and then with much more harmful consequences, namely, only *after* the southern economies had gone through a spectacular boom period. This then made the necessary real devaluation, particularly the wage decreases, much more painful than before, both economically and politically.

The initial surge in the south was indeed just the complement of the later crisis: with little capacity for wage moderation, with higher wages and therefore higher inflation, the southern euro area benefited from very low, partly negative real interest rates in the first five years of the monetary union. As wages then increased at a consistently higher rate than wages in the north (Höpner and Lutter 2014), southern industry quickly lost its cost competitiveness.[83] This translated into growing current account deficits, which could only be sustained by massive capital inflows. Once these stopped in the wake of the Lehman bankruptcy and capital even started to flow in the reverse direction, the crisis fully and dramatically materialised.

With respect to wage bargaining, the southern high-inflation equilibrium and the German low-inflation equilibrium seem to be opposites (Iversen, Soskice et al. 2016; Iversen and Soskice 2018). In this context, Bob Hancké speaks of the "two Europes", "one with orderly wage-determination systems, where low wage and price infla-

81 That the effects of the EMU for/on domestic wage bargaining regimes were not only anticipated, but also intended, is indicated, for instance, by the view of monetary economist Niels Thygesen, member of the Delors Committee. Monetary union, he stated, would be "a way of 'reducing the scope for the kind of lax and divergent monetary policies' that characterized Europe in the 1970s" (James 2012: 7).

82 Of course, it is important to emphasize that devaluations were not always due to wage growth differentials, but sometimes also reflected domestic imperatives of Germany's monetary policy. One example of this was the increased interest rates with which the Bundesbank wanted to cool down an overheating economy in the wake of Germany's post-unification boom. Also, the status of the deutschmark as a reserve currency sometimes forced the French or the Italians to devalue *vis-à-vis* the deutschmark during periods when the US dollar was weak.

83 In fact, every year since the introduction of the euro, unit labour costs have increased more dramatically in Italy and France than in Germany (Höpner and Lutter 2014). The lack of wage moderation is partly due to unions' strategies, partly due to highly inflexible labour markets: "productivity growth was correspondingly weak …. The most important reason for the relatively inflexible labour markets of southern Europe was legislation, which made it extremely difficult to lay-off long-term workers" (Wolf 2014: 63). But it "really did *not* make sense for countries whose industries were competing with those of China to allow their labour costs to rise faster than in countries like Germany, whose industries were complementary to those of China" (Wolf 2014: 293-294). The role of wage inflation in the public sector in Italy is well described in (Di Carlo 2018).

tion targets were internalised by the trade unions by means of inter-sectoral wage coordination, and another, where wages rose faster relative to productivity, competitiveness collapsed, and trade balances deteriorated sharply" (Hancké 2013: 13; Hassel 2014; Iversen and Soskice 2018).[84] The challenge, therefore, is not to explain why the euro area is not an optimal currency area, but why it is almost the exact opposite, why the single currency binds together two rather different types of political economies—a hard currency, export-led growth model, on the one hand, with a soft currency, *i.e.*, inflation-prone, consumption-based growth model, on the other (Iversen, Soskice et al. 2016). One key motive for currency union was a geopolitical consideration: committing unified Germany irreversibly to the European project. In addition, the currency union represented a *quid pro quo* of low inflation and low interest rates for the south and therefore a boost of credit-based growth there, in exchange for abandoning the option of devaluating in order to level out the wage restraint and productivity growth in the northern export industry (Iversen, Soskice et al. 2016). Apart from these two decisive factors, EMU came about not *despite* the profound differences between the northern and the southern political economy, but *because* of them: as a commitment of the south to the "German" low inflation equilibrium in order to break with the inflationary tendencies inherent in the southern model.

This explanation of the euro crisis and its specific dynamic starts with a focus on national wage bargaining systems. It is also in line with several other recent explanations for the crisis (Hancké 2013; Hassel 2014; Höpner and Lutter 2014; Iversen, Soskice et al. 2016; Iversen and Soskice 2018).[85] Differences between the continental and the southern wage bargaining regimes can explain both the political motives behind the strong push for a common currency in the 1990s - as a means of breaking the domestic inflationary cycles in the soft currency countries (mainly Italy and France) and as the ultimate proof of reunified Germany's commitment to Europe - and what were then divergent dynamics of the two political economies under the euro, which finally culminated in the dramatic crisis of 2008/2009 and the subsequent recession and sovereign debt crisis. Somehow ironically, or tragically, therefore, the export of the German low-inflation regime to the European level, triggered the real divergence between the north and the south of the currency zone (Palier, Rovny et al. 2018), and it rather reinforced than weakened central traits of the German political economy, in particular its strong export dependence.

84 This bifurcation into two groups of countries had already occurred in the 1970s under the European Monetary System: "The first group, made up of Germany, the Benelux countries, and Denmark, had succeeded in limiting inflation to the mid to high single digits and in keeping their exchange rates stable …. In fact, this was a deutschmark-based arrangement, since Germany was the lowest-inflation country and accounted for more than two-thirds of the collective GDP of this group. The second set of countries - France, Italy, and the United Kingdom, and Ireland - had more difficulty restraining inflation and were therefore unable to keep their currencies within the margins of the Snake" (Eichengreen 2007: 283).

85 This contradicts Martin Wolf's diagnosis, however: the euro crisis is not (or at least no longer) a "financial crisis with fiscal consequences" (Wolf 2014: 302), but has since turned into a competitiveness crisis with fiscal consequences. My position also diverges from Scharpf's analysis, in which he emphasizes the fiscal problem of euro member states running a public debt in a "foreign" currency. With Draghi's "whatever it takes" guarantee the ECB has, in fact, become lender of last resort. Further, with historically low interest rates, debt service is cheaper than ever before. However, (the lack of) private competitiveness remains a problem and, with sluggish growth, these states then also inevitably have a fiscal problem.

References:

Anderson, C. J. and D. S. Ward (1996). "Barometer Elections in Comparative Perspective." Electoral Studies**15**(4): 447-460.

Arndt, C. (2013). The Electoral Consequences of Third Way Welfare State Reforms: Social Democracy's Transformation and Its Political Costs. Amsterdam, Amsterdam University Press.

Baldwin, R. and F. Giavazzi, eds. (2015). The Eurozone Crisis. A Consensus View of the Causes and a Few Possible Solutions. London, CEPR Press.

Beramendi, P., S. Häusermann, et al. (2015). Introduction: The Politics of Advanced Capitalism. The Politics of Advanced Capitalism. P. Beramendi, S. Häusermann, H. Kitschelt and H. Kriesi. New York, Cambridge University Press**:** 1-64.

Blyth, M. (2015). Austerity: The History of a Dangerous Idea. Oxford, Oxford University Press.

Böhnke, P., J. Zeh, et al. (2015). "Atypische Beschäftigung im Erwerbsverlauf: Verlaufstypen als Ausdruck sozialer Spaltung?" Zeitschrift für Soziologie **44**(4): 234-252.

Burda, M. C. and J. Hunt (2011). "What explains the German Labour Market Miracle in the Great Recession?" Brookings Papers on Economic Activity **Spring**.

Carlin, W. (2013). "Real Exchange Rate Adjustment, Wage-Setting Institutions, and Fiscal Stabilization Policy: Lessons of the Eurozone's First Decade." CESifo Economic Studies**59**(3): 489- 519.

Carlin, W., A. Hassel, et al. (2014). The Transformation of the German Social Model. European Social Models From Crisis to Crisis: Employment and Inequality in the Era of Monetary Integration. J. E. Dolvik and A. Martin. Oxford, Oxford University Press**:** 50-105.

Carlin, W. and D. Soskice (1990). Macroeconomics and the Wage Bargain. A Modern Approach to Employment, Inflation and the Exchange Rate. Oxford, Oxford University Press.

Clasen, J. (2005). Reforming European Welfare States: Germany and the United Kingdom Compared. Oxford, Oxford University Press.

Clegg, D. and J. Clasen (2006). "Beyond activation: reforming unemployment protection systems in post-industrial labour markets." European Societies**8**(4): 555-581.

Clegg, D. and J. Clasen (2006). New labour market risks and the revision of unemployment protection systems in Europe. The Politics of the Post-Industrial Welfare State. K. Armingeon and G. Bonoli. London, Routledge**:** 192-210.

De Grauwe, P. (2013). "The Political Economy of the Euro." Annual Review of Political Science**16**: 153-170.

De Grauwe, P. (2014). Economics of Monetary Union. Oxford, Oxford University Press.

di Carlo, D. (2018). The Political Economy of Public Sector Wage setting in Germany and Italy. Responses of European Economic Cultures to Europe's Crisis Politics: The Example of German-Italian Discrepancies. C. Joerges and J. Hien. Villa Vigoni, Como.

Eichengreen, B. (2007). The European Economy since 1945: Coordinated Capitalism and beyond. Princeton, Princeton University Press.

Eichengreen, B. (2012). Hall of Mirrors: The Great Depression, the Great Recession, and the Uses-and Misuses-of History. Oxford, Oxford University Press.

Eichhorst, W. and L. C. Kaiser (2006). "The German Labour Market: Still Adjusting Badly?" IZA Discussion Paper(2215).

Eichhorst, W. and V. Tobsch (2014). "Flexible Arbeitswelten." IZA Research Report**59**.

Eichhorst, W. and V. Tobsch (2014). "Not So Standard Anymore? Employment Duality in

Germany." IZA Discussion Paper(8155).

Emmenegger, P., S. Häusermann, et al., Eds. (2012). The Age of Dualization. The Changing Face of Inequality in Deindustrializing Societies. Oxford, Oxford University Press.

Esping-Andersen, G. (1999). Social foundations of post-industrial Economies. Oxford, Oxford University Press.

Franzese, R. J. J. (1999). "Partially Independent Central Banks, Politically Reponsive Governments, and Inflation." American Journal of Political Science**43**(3): 681-706.

Gros, D. and N. Thygesen (1998). European monetary integration: from the European monetary system to economic and monetary union. London, Prentice Hall.

Hall, P. A. (1994). "Central Bank Independence and Coordinated Wage Bargaining: Their Interaction in Germany and Europe." German Politics and Society**31**: 1-23.

Hall, P. A. (2012). "The Economics and Politics of the Euro Crisis." German Politics**21**(4): 355-371.

Hall, P. A. (2014). "Varieties of Capitalism and the Euro Crisis." West European Politics**37**(6): 1223-1243.

Hall, P. A. and R. J. Franzese, Jr. (1998). "Mixed Signals: Central Bank Independence, Coordinated Wage Bargaining, and European Monetary Union." International Organization**52**(3): 505-535.

Hancké, B. (2002). The Political Economy of Wage-setting in the Eurozone. Wage Policy in the Eurozone. P. Pochet. Brussels, Peter Land**:** 131-148.

Hancké, B. (2013). Unions, Central Banks, and EMU: Labour Market Institutions and Monetary Integration in Europe. Oxford, Oxford University Press.

Hassel, A. (2014). "Adjustments in the Eurozone: Varieties of Capitalism and the Crisis in Southern Europe." Manuscript, Hertie School of Governance.

Hassel, A. (2014). "The Paradox of Liberalization - Understanding Dualism and the Recovery of the German Political Economy." British Journal of Industrial Relations**52**(1): 57-71.

Hassel, A. (2014). "Three sources for Germany's export dependency: Industrial relations, social insurance and fiscal federalism." Manuscript.

Hassel, A. (2017 (forthcoming)). "No way to escape imbalances in the Eurozone? Three sources for Germany's export dependency: Industrial relations, social insurance and fiscal federalism." German Politics.

Hassel, A. and C. Schiller (2010). Der Fall Hartz IV: wie es zur Agenda 2010 kam und wie es weitergeht. Frankfurt am Main, Campus.

Höpner, M. and M. Lutter (2014). "One Currency and Many Modes of Wage Formation. Why the Eurozone Is Too Heterogeneous for the Euro." MPIfG Discussion Paper**14**(14).

Illing, G., S. Jauch, et al. (2012). "Die Diskussion um den Euro." Leviathan**40**(2): 156-172.

Iversen, T. and D. Soskice (2018). A structural-institutional explanation of the Eurozone Crisis. Welfare Democracies & Electoral Politics. Explaining Electoral Dynamics in Times of Changing Welfare Capitalism. P. Manow, B. Palier and H. Schwander. Oxford, Oxford University Press**:** 257-280.

Iversen, T., D. Soskice, et al. (2016). "The Eurozone and Political Economic Institutions." Annual Review of Political Science**19**.

James, H. (2012). Making the European Monetary Union. Cambridge, Belknap Press.

Kersbergen, K. v. and P. Manow, Eds. (2009). Religion, Class Coalitions and the Welfare State. Cambridge Series on Social Theory, Politics and Religion. New York, Cambridge University Press.

Kitschelt, H. (2001). Partisan Competition and

Welfare State Retrenchment. When Do Politicians Choose Unpopular Policies? The New Politics of the Welfare State. P. Pierson. Oxford, Oxford University Press: 265-302.

Klinger, S., T. Rothe, et al. (2013). "Makroökonomische Perspektive auf die Hartz-Reformen: Die Vorteile überwiegen." IAB-Kurzbericht**11/2013**: 1-8.

Koch, S., P. Kupka, et al. (2009). Aktivierung, Erwerbstätigkeit und Teilhabe. Vier Jahre Grundsicherung für Arbeitssuchende. Bielefeld, Bertelsmann.

Krugman, P. and M. Obstfeld (2012). Internationale Wirtschaft. Theorie und Politik der Außenwirtschaft. München usw., Pearson.

Manow, P. (2009). "Electoral Rules, Class-Coalitions and Welfare State Regimes - or how to explain Esping-Andersen with Stein Rokkan." Socio-Economic Review**7**(1): 101-121.

Manow, P. (2013). "Religious Cleavages, Divisions on the Left and the Political Economy of Southern Europe." International Journal of Social Quality**3**(2): 78-105.

Manow, P. (2015). "Workers, Farmers, and Catholicism: A History of Political Class Coalitions and the South-European Welfare State Regime." Journal of European Social Policy**25**(1): 32-49.

Manow, P., B. Palier, et al., Eds. (2017). Worlds of Welfare Capitalism and Electoral Politics. Oxford, Oxford University Press.

Manow, P. and E. Seils (1999). Adjusting Badly: The German Welfare State, Structural Change and the Open Economy. From Vulnerability to Competitiveness: Welfare and Work in the Open Economy. F. W. Scharpf and V. A. Schmidt. New York, Oxford University Press: 264-304.

Marin, D. (2010). "Germany's super competitiveness: A helping hand from Eastern Europe." VOX - CEPR's Policy Portal **20 June 2010**: http://www.voxeu.org/article/germany-s-super-competitiveness.

O'Rourke, K. and A. M. Taylor (2013). "Cross of Euros." Journal of Economic Perspectives **27**(3): 167-192.

OECD (2015). In it together - Why less inequality benefits all. Paris, OECD.

Palier, B., A. Rovny, et al. (2018). The Dual Dualization of Europe: Economic Convergence, Divergence, and their Political Consequences. Welfare Democracy and Party Politics. Explaining Electoral Dynamics in Times of Changing Welfare Capitalism. P. Manow, B. Palier and H. Schwander. Oxford, Oxford University Press: 281-297.

Palier, B. and K. A. Thelen (2010). "Institutionalizing Dualism: Complementaries and Change in France and Germany." Politics & Societies **38**(1): 119 - 148.

Rehder, B. (2003). Betriebliche Bündnisse für Arbeit in Deutschland. Mitbestimmung und Flächentarif im Wandel. Frankfurt am Main, Campus.

Rhein, T. (2013). "Erwerbseinkommen. Deutsche Geringverdiener im europäischen Vergleich." IAB Kurzbericht - Aktuelle Analysen aus dem Institut für Arbeitsmarkt- und Berufsforschung **15**.

Rueda, D. (2005). "Insider - Outsider Politics in industrialized Democracies: The Challenge to Social Democratic Parties." American Political Science Review **99**(1): 61-74.

Rueda, D. (2006). "Social Democracy and Active Labour-Market Policies: Insiders, Outsiders and the Politics of Employment Protection." British Journal of Political Science **36**: 385-406.

Scharpf, F. W. (1987). Sozialdemokratische Krisenpolitik in Europa. Frankfurt, Campus.

Scharpf, F. W. (2011). "Monetary Union, Fiscal Crisis, and the Preemption of Democracy." MPIfG Discussion Paper 11/11. Max-Planck Institute for the Study of Societies, Cologne.

Scharpf, F. W. (2017). "Vom asymmetrischen

Euro-Regime in die Transfer-Union – und was die deutsche Politik dagegen tun könnte " Leviathan **45**(3): 286-308.

Schumacher, G. (2011). 'Modernize or Die'? Social Democrats, Welfare State Retrenchment and the Choice between Office and Policy. Amsterdam, University Amsterdam.

Schwander, H. and P. Manow (2016). "'Modernize *and* Die'? German Social Democracy and the electoral Consequences of the Agenda 2010." Socio-Economic Review **forthcoming**.

Streeck, W. (2009). Re-Forming Capitalism. Institutional Change in the German Political Economy. Oxford, Oxford University Press.

Streeck, W. and A. Schäfer, Eds. (2013). Politics in the Age of Austerity. London, Wiley & Sons.

Thelen, K. (2014). Varieties of Liberalization and the New Politics of Social Solidarity. New York, Cambridge University Press.

Vail, M. I. (2010). Recasting Welfare Capitalism. Economic Adjustment in Contemporary France and Germany. Philadelphia, Temple University Press.

Walters, A. (1992). Walters Critique. The New Palgrave Dictionary of Money and Finance. P. K. Newman, M. Milgate and J. Eatwell. Basingstoke, Hampshire, Palgrave Macmillan.

Wolf, M. (2014). The Shifts and the Shocks. What we've learned - and have still to learn - from the financial crisis. New York, Penguin.

Wren, A., Ed. (2013). The Political Economy of the Service Transition. Oxford, Oxford University Press.

THE POLITICAL ECONOMY OF PUBLIC SECTOR WAGE-SETTING IN GERMANY AND ITALY

Donato Di Carlo

Max Planck Institute for Studies of Societies

Setting the Scene

The chance to write this brief contribution stems from the invitation that I received to attend the Villa Vigoni conference. The general topic of the conference revolves around discrepancies in the German and Italian responses to the multiple crises affecting Europe.

Specifically, the subject matter of this paper pertains to the domain of public sector employment relations and wage policies in the European Economic and Monetary Union (EMU). The aim is to look at the political and institutional determinants of public sector wage policies in Germany and Italy over the period 1991-2015. In so doing, I ask the following interrelated questions: What were the political and institutional determinants of Germany and Italy's divergent public sector wage trajectories before the crisis? And, while Italy underwent severe post-crisis austerity measures which led to public sector wage deflation, why have public sector wages not risen consistently in Germany notwithstanding the budget surplus and low unemployment?

The empirical basis of the argument developed here is provided by research pursued in the context of my doctoral project at the *Max Planck Institute for the Study of Societies*, in Cologne. Besides the analysis of macroeconomic data and primary institutional sources, the essay draws on extensive fieldwork carried out in both countries. I have conducted interviews (24 in Germany and 17 in Italy) with key policy-makers in the top echelons of the Finance ministries, trade unions, associations for the representation of public employers (*TdL*[86] for Germany, and *ARAN*[87] for Italy), national courts of auditors (*Corte Dei Conti*) and academic/policy experts close to the field of interest.

In preview, the main argument of this paper is the following: while Germany pursued public sector wage restraint throughout the period 1994-2007, during the years 2002-2006, Italian public employers deliberately pursued a policy of public sector wage inflation for strategic political purposes. After the crisis, wage restraint in Italy was the result of unilaterally implemented wage cuts and freezes in the public sector. In Germany, wages are, instead, prevented from rocketing - notwithstanding favourable material conditions - by the peculiar structure of public sector wage-setting, which brings together rich and poor *Länder* (and municipalities) into a structured decisional process which produces a low wage equilibrium. In both the *TVöD* and *TV-L* contracts, wage increases have to be set as a lowest common denominator to take into consideration the ability of the poor *Länder* (in *TV-L*) and municipalities (*TVöD*) to pay. Italy, in contrast, experienced a pro-cyclical pattern of public sector wage inflation and restraint. During the good times of the Euro, public sector wages increased beyond macroeconomic fundamentals, driven by the political motivations of the "Southern *bloc*" (composed of the parties such as *Alleanza Nazionale* and *Unione Di Centro*) inside the Berlusconi-led centre-right coalition. The pattern of wage inflation had started to be reversed before the crisis occurred, when Tommaso Padoa-Schioppa was finance minister, under the centre-left coalition led by Romano Prodi in 2006-2007. Eventually, however, when the crisis unfolded, wage restraint was unilaterally imposed by the finance minister Giulio Tremonti in 2009 and was then continued by the subse-

86 TdL (*Tarifgemeinschaft deutscher Länder*) is the association of finance ministers of the German Laender in charge of negotiating public sector wage contracts.

87 ARAN (*Agenzia per la Rappresentanza Negoziale delle Pubbliche Amministrazioni*) is the Italian independent agency in charge of representing the government during negotiations with trade unions.

quent governments. Overall, Italy had seven years of wage freezes which substantially contributed to deflate its economy pro-cyclically.

In sum, discrepancies in public sector wage-setting in the two countries can be attributed to different institutional structures for the determination of public sector pay and interest representation. A system of soft fiscal constraints in Italy allows for the *political willingness* of sovereign employers *to pay* inflationary wages in good times. In Germany, instead, a system of hard fiscal constraints for sub-national governments precludes the pursuit of a policy of wage inflation. In the former country, the structure of public sector wage-setting leads to the politicisation of wage determination processes. In the latter, wage policy choices are constrained *ex ante* by the fiscal constitution of the state.

The implications of this argument for comparative political economy (CPE) are manifold. Contrary to what is usually believed (Hancké 2013; Höpner and Lutter 2014; Johnston 2016; Johnston and Hancke 2009; Johnston, Hancke, and Pant 2014), wage restraint in the German public sector is *not* due to effective/defective inter-sectoral wage co-ordination imposed by the export sector upon sheltered sector wage-setters (Di Carlo 2018). Nor was or is it pursued to protect export price competitiveness in the interests of an "hegemonic social coalition" between employers and skilled labour in the export industries (Baccaro and Benassi 2016; Baccaro and Pontusson 2016; Hassel 2014). Public sector wage-setting is, first and foremost, a public finance problem. It involves state actors located at different levels of the public administration, representing heterogenous institutional interests (very diverse from those of the German export industry). Furthermore, public sector wage policies do not come uncontested. Studying the *politics of fiscal policy* teaches us that significant conflicts can emerge inside the sovereign employers bloc: for example, between finance ministers with diverse vested interests across different state levels (as in Germany) or between politicians (who make promises) and the finance ministers of their governing coalition (who have to pay for them).

CPE research interested in studying public sector wage-setting should, instead, look at the institutional constellation shaping processes of public sector wage-setting proper and stop understanding the working of the public sector solely as a function of export-sector interests. This constellation, I posit, is composed of three key elements; first, the structure of the *public administration* determines the distribution of *administrative competencies* among the layers of the public administration – and therefore the distribution of personnel costs; second, the structure of the *taxation system* determines the *ability to pay* of sovereign employers located at the different levels of the public administration; and, third, the characteristics of *public sector employment relations* determine legal rights and the structure and modes of interest representation.

The remainder of this paper is organised as follows; Section 1 engages with the problem of public sector wage divergence in the EMU; Section 2 provides a summary of the German case study, while Section 3 deals with the Italian one. Due to space constraints, I will skip a thorough review of the literature[88] and provide only stylised accounts of the case studies.

1. The Problem of Divergent Public Sector Wage-setting in the EMU

Joining the EMU entails losses of national sovereignty *vis-à-vis* the policy tools available for the macroeconomic stabilisation of the economy (De Grauwe 2016). Of the four standard policy tools available for the control of the economy (Scharpf 1991), monetary policy is delegated to a supranational independent central bank; fiscal policy is *de jure* constrained by national and supranational Fiscal Compacts, while exchange rates are relinquished. In this scenario, wage policies remain the most important pillar of macroeconomic policy-making for domestic social partners in the EMU.

88 For a more detailed discussion on public sector wage setting in the German context, see Di Carlo (2018) and Keller (2011).

While private sector wage policies are often beyond the remit of governmental authorities (e.g., *Tarifautonomie* in Germany), public sector wage policies are of particular interest, given that their implementation necessarily coincides with the fiscal stance of the sovereign employers in charge of earmarking fiscal resources for wage contracts. Thus, looking at public sector wage trajectories is a fundamental way of looking at the fiscal trajectories of governments. Public sector wage-setting matters in the EMU, both with regard to the co-ordination of the fiscal policies of euro Member States, but also, and especially so, for the impact that wage inflation can have on macroeconomic imbalances *via* divergent unit labour costs (ULC) and price inflation[89] (Baccaro and Tober 2017; Hancké 2013; Johnston, Hancke, and Pant 2014).

From the perspective of the EMU's macroeconomic regime - an economic system rooted in price stability - relatively stable ULC inflation is required in order to avoid structural divergence of Members' price inflation in the medium to long run. The trade imbalances to which this divergence leads can, in fact, no longer be absorbed through adjustable exchange rates (Carlin and Soskice 2014, Ch. 12).

In this context, the European Commission had adopted what is understood as the *Golden Rule of Wage Bargaining*[90] as the formal policy guideline for national social partners: wage-setting is to be based upon the European Central Bank's (ECB) inflation target plus average productivity in the economy. Given the absence of pan-European wage co-ordination, this was meant to engineer a virtuous interaction between national wage policies and the supranational monetary policy and, at the same time, avoid inflation differentials and the rise of macroeconomic imbalances in the monetary union. In an abstract world, three types of wage policies are thus available to national public sector wage-setters.

89 See Höpner and Lutter (2014) for a review of the empirical literature.

90 For a more detailed description, see Collignon (2009).

Starting from the Golden Rule:

WP= 1,9% + Δ avg. LP

Where:

WP = wage policy implemented

ECB inflation target = 1,9%

Δ Avg. LP = % change (yoy) in total labour productivity in the economy

Sovereign employers can then adopt three alternative types of wage policies:

i. Policy of wage inflation > Golden Rule

ii. Policy of wage restraint < Golden Rule

iii. Policy of the Golden Rule = Golden Rule

Ideally, in order to avoid a rise of macroeconomic imbalances, trajectories of nominal wages would have had to develop in line with national productivity rates and the supranational price target. Reality has proven different from theory. Panel *a* in Figure 1 shows the divergent trajectories of nominal wages in the public sectors of the EMU participants during the good times of the Euro. Three clusters can be observed. At the two opposite extremes, we find Germany (alone) pursuing a policy of remarkable public sector wage restraint and the so-called GIIPS[91] countries experiencing substantial public sector wage inflation. The core countries of the EMU, interestingly, have had wage developments almost perfectly in line with the Golden Rule.

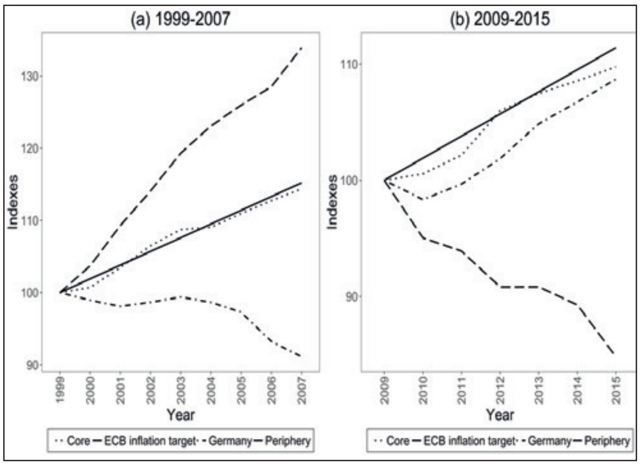
Not surprisingly, public sector wage developments have mirrored quite faithfully the trajectory of real exchange rates (REER) (Figure 2) since the launch of the single currency. The connection between public sector wage inflation/restraint, REER appreciations/depreciations and current account imbalances is evident. Research has, in fact, shown that current account imbalances in the EMU had their root cause primarily in sheltered sector wage inflation (Baccaro and Tober 2017; Hancké 2013; Johnston, Hancke, and Pant 2014), of which the public sector constitutes the bulk.

On average, public sector employment in the

91 Greece, Ireland, Italy, Portugal, Spain.

EMU accounts for more than 15 per cent of total employment. The sovereign employers are the single biggest, political and economic, employers in every advanced economy. Since public wages are paid out of taxpayers' money, wage policy in the public sector cannot but be a subset of fiscal policy. With regards to the latter, studies by the European Central Bank (Holm-Hadulla et al. 2010, 4) also find that "government wage expenditure is subject to a pro-cyclical bias in most euro area countries and at the euro area aggregate level". A pro-cyclical policy of wage inflation in the public sector can thus lead to losses of REER competitiveness, underpin excessive imports, and contribute to an overall expansionary - procyclical - fiscal stance in the economy. *Vice versa*, in hard times, public sector wages are hardly hit by the fiscal authorities.

Figure 1: Indexes* of hourly wages in the public sectors of EMU countries (1999-2015).



Source: EU KLEMS Growth and Productivity Accounts, September 2017 release.

*Indexes are discounted by labour productivity in the total economy. In (a), 1999=100. In (b), 2009=100.

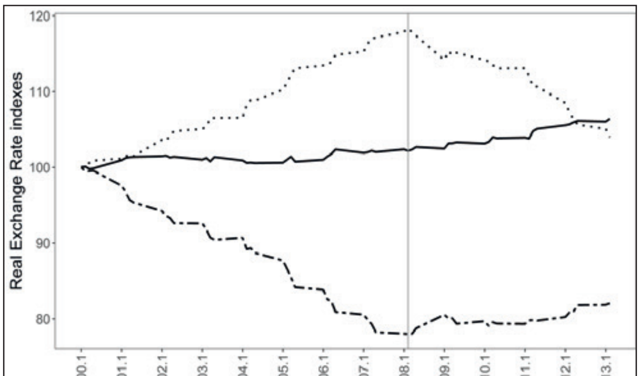
EMU Core = Austria, Belgium, Finland, France, The Netherlands.

EMU Periphery = Greece, Ireland, Italy, Portugal, Spain.

This is particularly evident when observing developments in public sector wages in the aftermath of the crisis. Panel *b* in Figure 1 shows the policies of public sector wage restraint pursued in the GIIPS countries after 2009. The countries which had undergone wage inflation in the good times of the single currency all experienced post-crisis restraint, as part of the harsh austerity measures which followed. Arguably, public sector wage-setting is the first and most accessible policy domain from which governments glean resources in hard times. Germany, in contrast, did not perform the eagerly awaited symmetric adjustment (Bibow 2012) through an expansionary public sector wage policy. It continued along the trajectory of moderate public sector wage increases inaugurated in the aftermath of re-unification (Di Carlo 2018; Keller 2016; 2014).

Thus, overall, the wage trajectories in the Italian and German public sectors develop asymmetrically in both good times (panel a) and hard times (panel b). In the first decade of the EMU, Italy experienced public sector wage inflation, while Germany pursued wage restraint. In hard times, Germany continued its pattern of moderate public sector wage increases (despite slightly expanding public sector employment in some sectors such as education and care), while Italy underwent remarkable wage restraint.

Figure 2: Real Effective Exchange Rates (REER) of EMU members (2000-2013), based upon unit labour costs (ULCs), weighted against 14 EU trading partners. Quarterly data (.1=1st quarter)



Source: Bruegel Datasets, REER for 178 countries, a new database (Latest update: June 6,2017).

EMU Core = Austria, Belgium, Finland, France, Netherlands.

EMU Periphery = Spain, Greece, Ireland, Italy, Portugal.

Notwithstanding the relevance of public sector wage policies for the smooth functioning of the single currency, very little research is available on the topic. The public sector has been neglected both by industrial relations scholars and the comparative political economists – not to mention scholars of European affairs.

In industrial relations, a set of works exists that studies the structures of public sector employment relations and patterns of institutional change (Bach and Bordogna 2016; 2013; L Bordogna, Dell'Aringa, and Della Rocca 1999; Keller 2016; 2011; Keller and Seifert 2015). These studies are highly informative, but remain mostly at a descriptive level. In CPE, the public sector has always been treated as a satellite of the export sector's interests.[92] The perspective adopted in these studies was always that of inter-sectoral wage co-ordination between the exposed sectors and the sheltered ones. Surprisingly enough, no attention was ever paid to the structure of the public administration, the role of the state as a sovereign employer (Hyman 2008; Traxler 1999), the characteristics of public sector employment relations or the fiscal constitution of the state. The study of public sector wage bargaining remains a neglected and misunderstood aspect in the discipline. The status quo in the literature is not satisfying and a clear-cut understanding of the political and institutional determinants of public sector wage setting in missing in both industrial relations and CPE.

92 Di Carlo (2018) provides a thorough literature review of this literature in the context of European CPE. It also provides an empirical falsification of the thesis according to which wage restraint in the German public sector is the result of export-sector-led pattern bargaining.

2. The Political Economy of Public Sector Wage Restraint in Germany: *die öffentlichen Kassen sind immer leer*

2.1 The 1990s: blühende Landschaften hit the EMU fiscal constraints

With regard to public sector wage-setting in Germany, it needs to be distinguished between public employees and civil servants (*Beamten*). Collective bargaining regulates wage-setting for the former. Unilateral legislation by the Government sets employment and pay conditions for the latter. Given the structure of the German public administration, three levels of employment exist: the Federation (*Bund*), the states (*Länder*), and the municipalities (*Gemeinden*). Public employers at each level are responsible for their employees and can choose whether to employ personnel as civil servants or as public employees. At the federal level, the sovereign employers are represented in negotiations by the ministry of the interior, flanked by the finance minister. At the *Länder* level, the regional finance ministers are grouped together in the so-called *Tarifgemeinschaft deutscher Länder* (TdL). At the municipal level, municipalities are grouped into a state level association *Kommunaler Arbeitgeberverband* (KAV). The 16 associations from each *Land* are then represented together by the *Vereinigung der kommunalen Arbeitgeberverbände* (VKA). Overall, until 2002, the three employers corresponding to the three public administration levels negotiated jointly with the trade unions under the leadership of the federal minister of the interior (a practice termed *Tarifgemeinschaft*).

Given that the German Constitution (*Grundgesetz*) attributes most of the competencies to the sub-national governments, the *Länder* and the municipalities are the entities which bear the costs for administrative personnel disproportionately. While for the *Länder* expenditure for personnel amount to around 40-45 per cent of their total expenditure, the municipalities spend 25 per cent of the budget on personnel, while the federal level spends only around 9-10 per cent (Destatis data).

Given this cost structure, personnel costs (a *stock*) (and hence wage increases (a *flow*)) constitute a major concern for the finance ministers of the *Länder* and municipalities. Most importantly, the states and municipalities act as tax collectors for the federation, with whom they share tax revenues according to vertical and horizontal fiscal equalisation grants which are enacted via pre-determined formulae. Given the taxation structure, the *Länder* and municipalities simply *cannot* readily manipulate their *marginal tax revenues*. The only way that the *Länder* have to increase their tax revenues is through changes in legislation via the *Bundesrat*, which would require the consensus of all the *Länder*. The result of this joint-decision trap (Scharpf 2005) is that the fiscal structure in which lower levels of government are embedded puts enormous pressure on the expenditure side – of which the personnel costs are among the most significant items – leaving not much choice other than to keep the personnel expenditure in check - disproportionately so for the *Länder*. This tense situation worsened after the absorption of the poor new *Länder* into the fiscal equalisation system in 1995.

In fact, wage restraint in the German public sector started both before (and in relation to) the EMU, and as a consequence of the fiscal costs of reunification. The *blühende Landschaften* promised by Helmut Kohl to his fellow Germans, inevitably came to clash with the fiscal constraints set in the Maastricht Treaty and the following Stability Growth Pact (forcefully insisted upon by the German finance minister Theo Weigel). Public sector wage restraint first emerged in 1994 via a wage freeze for civil servants unilaterally imposed by the government, together with a moderate wage settlement collectively negotiated for public employees. It was then pushed through decisively via a *Spaarpaket* before the fiscal year of 1997 - in order to comply with the Maastricht *vincolo esterno*. In the 1990s, public sector wage restraint occurred out of concerns for fiscal deficits by the federal finance minister Theo Waigel. The consolidation measures implemented in 1996 are effectively summarised by the IMF fiscal consolidation dataset:

> "Fiscal consolidation in 1997 was primarily motivated by deficit reduction and meeting the Maastricht deficit criteria … To shore up the public finances, the authorities adopted in late 1996 substantial discretionary fiscal measures as part of the budget for 1997, which were heavily weighted on spending cuts … With these measures, the authorities expected that the general government deficit would decline to 2% of GDP in 1997, safely under the Maastricht reference value. Spending cuts in the 1997 budget amounted to 1% of GDP and were based on wage restraint and retrenchments, spending limits imposed at the federal and state level, reducing sick pay coverage and restricting spa visits, and tightening eligibility for unemployment benefits."

2.2 The Early 2000s: The *Länder* Offensive

In the early 2000s, the drivers for restraint were different. Wage restraint was the result of a process of institutional change which overhauled the old *Tarifgemeinschaft*. The process was driven and wanted by the finance ministers of the *Länder*. At the core of *Länder* finance ministers' preoccupations was the concern about keeping the personnel cost of their state administrations under control. They also started a controversy with the unions, in 2003, on extending working hours (Dribbusch 2006). For them, keeping costs down is of disproportionate importance given their cost structures and, especially, given the impossibility of freely manipulating their marginal tax revenues. To achieve this end, they opted to free themselves from the (expensive) leadership of the federal level in public sector wage negotiations. Also, they wanted to separate themselves from the (troublesome) municipal level in which public employees potentially have the highest disruptive power to affect negotiating dynamics thanks to their strength in basic community services (e.g., in local transport and waste disposal).

Negotiations to reform the system started after the signature of the 2002 collective/national contract and were concluded in 2005 with the creation of the *Tarifvertrag für den Öffentlichen Dienst (TVöD)* contract which regulates public employees at federal and municipal level. Wage restraint emerged as a combination of extended working hours, a rationalisation of special bonuses and a moderate lump-sum compensation of €300 per year in the years 2005, 2006 and 2007. The unions exchanged restraint for participation in reforming the old bargaining structure.

TdL did not want to be part of *TVöD*, and, after very tense negotiations and strike actions, throughout 2006, they reached an agreement with the unions on the creation of the new *Tarifvertrag für den Öffentlichen Dienst der Länder* (TV-L). The agreement envisaged lump sums of various amounts depending on the pay grades, to be paid out to employees in July 2006, January 2007 and September 2007, a rationalisation of special bonuses and the extension of working hours.

As a parallel development, the reform of the fiscal federalism system in 2006 has restored to the *Länder* the competence to legislate on the employment and wage conditions of their own civil servants. This has introduced an element of competitive federalism and created an horizontal diversification of wage conditions across the states, with Berlin and Bavaria located at the opposite extremes of the continuum (DGB 2016).

2.3 Public Sector Wage-setting in the Age of Prosperity

Germany is living through times of budget surpluses and almost full employment. Also, there is increasing difficulty in recruiting public employees (especially teachers and nurses). Public opinion also appears to be in favour of expanding public employment. Yet, one can barely notice an upward trajectory of wage increases. Why?

To be sure, increases in public employment in the categories mentioned are indeed visible. Yet, I argue that public wages are structurally prevented from increasing in Germany because of the unique public sector wage-setting regime.

With regards to the *TV-L* contract, *TdL* negotiators are forced to take into consideration the ability of the finance ministers from the poor *Länder* to pay. The poor states greatly value the benefits of collective bargaining coordinated through the *TdL*, especially in order to avoid direct wage competition with the richer *Länder* and to avoid setting up costly bargaining units to handle negotiations and internecine conflict. Moreover, they still have to make sure that the rich *Länder*, with a higher ability to pay, do not push up wage settlements driving them into bankruptcy. In the internal politics of *TdL*, it does not take much to convince the finance ministers of the rich states to hide behind the poor ones: they have, so to speak, an interest in being outvoted. Personnel costs are, on average, higher in the books of the old *Länder*, when compared to the new ones, which underwent a massive re-structuring after re-unification. Setting wages calibrated as a lowest common denominator decreases their *fiscal opportunity costs - i.e.*, frees fiscal resources can be spent on other items (or hoarded as budget surpluses, which the finance ministers of accountable states seem to value considerably). At the same time, richer *Länder* can blame the restraint on the poor finances of the others. *TdL* itself has an organisational interest in keeping the 15 state finance ministers together (Hesse is not in the *TdL*). The rich states would most probably have to pay higher wages than they currently pay (without upward competition) and would see their transaction costs in negotiations increase. The poor *Länder* would find themselves in a fully competitive federal system, in which they would be net losers. The system is granted some flexibility for diversification and competition via the possibility for the states of hiring civil servants and thus can unilaterally decree wage settlements.

With regard to the *TVöD* contract, a similar logic applies, although without the cleavage rich vs poor states. This is because poor municipalities are widespread also in West Germany. Substantial wage increases are prevented from the necessity to avoid bankruptcy of poor municipalities and/or a likely increase of transfers from the Federal level. Negotiators in the *VKA*, together with the federal finance and interior ministers, are aware of the necessity to avoid costly settlements which risk endangering the finances of lower levels.

Thus, in the German system, key explanatory factors for public sector wage restraint are the structure of the public sector wage-setting regime, the direct accountability of *Länder* finance ministers and their isolation from political influence.

3. The Political Economy of Public Sector Wage Inflation and Restraint in Italy: *We will Find the Money, if we Like*

3.1 The 1990s: Depoliticisation of Public Sector Collective Bargaining?

Until the end of the 1960s, pay and employment relations in Italy were unilaterally set by the sovereign employer through laws or administrative acts. In this system, public employees enjoyed the employment status of civil servants, which guaranteed employment security and seniority careers (Rusciano 1978). Over time, collective bargaining rights were granted and, during the 1970s, the practice spread throughout the branches of the public sector, until the 1983 *Legge Quadro* introduced collective bargaining as a primary mode of pay determination – although contracts still needed to be transformed into administrative acts to come into effect. The introduction of collective-bargaining rights in conjunction with civil servant status gave birth to a regime of "double guarantee", or, as scholars have put it, "pluralism without markets" (Lorenzo Bordogna 1994; Giugni 1992). During the 1980s, this public sector wage-setting regime led to uncontrolled wage inflation and politically-tolerated, leapfrogging dynamics in a context of union fragmentation and recurring disputes (Cella 1991).

The public sector wage-setting regime of the first republic consisted of a highly fragmented system in which smaller trade unions (*sindacati autonomi*), independent of the peak level confederations, the CGIL, CISL and UIL, had established a dense network of clientelistic relations with political referents in parliament (Ricciardi 2013, 120-27). This network led to what was termed "wage jungle" (*giungla retributiva*) (Gorrieri 1973) to indicate the practice of setting public sector wages regardless of any economic or administrative logic. Wage-setting in the public sector simply responded to the political logic of (re-) producing consent. Political actors in parliament were thus able to pass specific laws (*leggine settoriali*)[93] hiding them from the scrutiny of public opinion, delivering favourable provisions (income and non-income related) to their affiliated sub-groups of workers in the public sector (Talamo 2009b).

Major reforms of the system of public sector pay determination were passed in 1992-1993 with the ambition to make the process "apolitical" and to contain public expenditure. The public law status of public employees was abolished and the employment relationship was "privatised" (*privatizzazione del pubblico impiego*). Collective bargaining became the legal method[94] to regulate terms and conditions of employment. The reform of the summer of 1993 introduced a two-tier wage-bargaining system in which the main pillar

93 This practice was unveiled also by a Parliamentary Commission (Commissione Coppo) in 1977 and later denounced in the famous "Report on the fundamental problems of the State" by Professor Massimo Severo Giannini in 1979.

94 Approximately 80% of public employees were subjected to the reform. Core functions of the state were not privatized, such as judges, police, the army, *etc.*

consisted of nationally agreed and uniform wage increases negotiated between the newly-created independent agency (*Agenzia per la Rappresentanza Negoziale delle pubbliche amminstrazioni* - ARAN) and the trade unions. The second pillar regarded wage increases at the decentralised level to be negotiated by individual administrations and the workplace personnel representation bodies in a context of "organised decentralisation" (Lorenzo Bordogna 2012; L Bordogna, Dell'Aringa, and Della Rocca 1999).

The wage contracts were to last for a two-year duration (*biennio contrattuale*) and the wage increases were to be decided according to three criteria. First, wage increases at national level were to be calculated according to the rate of "expected inflation" (*Tasso di Inflazione Programmata, TIP*) for the subsequent two-year contract. This rate would have to be negotiated in a concerted manner between the government, employers and the unions during two sessions (one in the spring and one in the autumn) throughout the preceding year. Second, in the event of a discrepancy between the expected and the actual inflation, the subsequent two-year contract would have to incorporate resources *ex post* on order to compensate for lost purchasing power. This provision would be calculated upon the basis of the difference between the expected rate of inflation and the actual rate. To these criteria for centrally determined wage increases, local administrations could add resources to the central contracts according to productivity increases. These additional resources would have to be paid in part by resources granted from the central level and in part by the finances of the local administrations.

The creation of the independent agency, ARAN, as the monopolistic representative of all public administrations in national level negotiations had the purpose of insulating wage bargaining from the incursions of party politics. The technical body, in a principal-agent relationship with the government, was meant to prevent the distortions of the previous model. After the *Mani pulite* scandal(s) in the 1990s, the political establishment came to be held inadequate to continue handling wage negotiations for political purposes. However, the creation of ARAN could not circumvent the political nature of public sector wage-setting in which the fiscal costs for the determination of wage increases had to be earmarked in budget laws. The way in which Italy reformed its system did not shelter the finance ministers from party politics. ARAN would negotiate with the trade unions on how to distribute resources, while the *quantum* of the fiscal resources to be earmarked before the government's mandate remained fully in the hands of the government.

During the 1990s, the trade unions acted responsibly in the determination of the public sector pay. In a context of weak political parties, the unions played a major role in tripartite consultation for the reform of collective bargaining and, above all, the production of public sector wage restraint. The unions exchanged wage restraint with political influence on the determination of legislation related to the re-structuring of public sector employment relations (Talamo 2009a, 4-5). Unions also shared in the objective of complying with the external constraints imposed on public finances by the accession phase to the EMU in 1999[95] (Hancké and Rhodes 2005).

3.2 The Early 2000s: The Return of (Political) Incomes Policies

The scenario for public sector wage-setting changed substantially with the advent of the centre-right coalition (2001-2006) led by Silvio Berlusconi. Although, formally speaking, the institutions for public sector collective bargaining were not changed during the years of inflation (mostly 2002-2006), the function of pay determination was re-oriented towards a logic of political consent. This was made possible by the inconsistencies of the structure created in 1993, which made room for the return of the politicisation of public sector wage determination.

95 Confirmed in interviews with heads of public sector branches of CGIL, CISL, but also confirmed in interviews with decision makers in the top echelon of ARAN. Interviews carried out in winter 2017/2018.

According to the legal structure, the government would decide the fiscal resources to be earmarked in the budget law which preceded the beginning of the two-year contract. These resources, inserted in the budget law, were decided *ex ante* by the sovereign employer and would be publicly known to all actors. Since resources are already earmarked before the beginning of negotiations between ARAN and the unions - and unions know the exact amount already granted - this becomes the "point of non-return" in the bargaining cycle. Instead of serving as a ceiling for wage setting, the determination of the *quantum* by the government makes room for political contestation. The unions, in fact, contest the amount of available resources, oppose the beginning of negotiations with ARAN, and exploit the already-agreed upon number in order to increase the resources required by lobbying the government.

The capability of the unions to obtain greater resources depends on the willingness of the government to reach a compromise with them. The centre-right government was not united behind a policy of public sector wage inflation. In fact, the House of Freedoms (*La Casa delle Libertà*), as the coalition was named, was not united at all. It consisted of four very heterogeneous parties geographically and sociologically rooted in different parts of the country (Diamanti 2003). After the end of the first republic, the centre-right had been formed in 1994 (and reformed in 2001) by Berlusconi's capacity to bring together, into a unique political space, parties with strongholds in different parts of the country.

In the North, Berlusconi had secured a pact with the *Lega Nord* (Northern League) centred on the middle classes' quest for a neo-liberal agenda comprising tax cuts, fiscal federalism, a clampdown on immigration, and reduced state intervention. After the disastrous experience of the mid-1990s, the House of Freedoms campaigned together again and won the elections in 2001, opening a new era for the centre-right. Although *Alleanza Nazionale* (AN) was the second political force in the coalition (12%), and Gianfranco Fini, its leader, had been appointed deputy prime minister, Berlusconi saw, as the driving force of the coalition, a special alliance with Umberto Bossi, Northern League's leader, and Giulio Tremonti, the appointed finance minister acting as the guarantor between the two leaders. This special relationship came to be known as the "Northern axis" (Diamanti and Lello 2005, 22-23). Proof of the close ties between Berlusconi and Bossi was the recurring practice of dining together at Berlusconi's villa in Arcore every Monday evening to discuss the interests of the Northern middle classes, small- and medium-sized enterprises, and freelance professionals.

As representatives of the South - and the centre - the coalition included the post-fascist *Alleanza Nazionale* (AN) and the post-Christian-Democratic *Unione di Centro* (UDC). These parties were rooted in the Southern areas of the country which were characterised by high levels of unemployment and in which public sector employment (and wage inflation therein) has historically played a key role as a socio-economic stabiliser in the local economies (Cassese 1977; Santoro 2014). The remaining forces of the coalition, AN and UDC, thus came to constitute the "Southern bloc" - inspired by the values of the Social Right (*destra sociale*), representing the lower classes of the South and employees in the public administration. As the leader of UDC put it to me, the Southern bloc "represented all those people which were not taken care of by the Arcore tablemates" (interview with the then leader of the UCD. Rome, 9 February 2018). AN and UDC strongly, and vocally, supported public works and infrastructure building in the South, as well as resources for public employment, with a special eye on the Lazio region where most of the central administrations are based and where AN has historically been strongly rooted.

The bargaining cycles which led to public sector wage inflation in Italy are the two-year contracts of 2002-2004 and 2004-2006. On both occasions, the direct mobilisation of political capital by Gianfranco Fini, the deputy prime minister and leader of AN and the Southern bloc, was of fundamental importance for increasing fiscal resources previously granted through budget laws. With regard to public sector wage policy, Fini has been repeatedly capable of imposing the interests of the Southern bloc on the whole coalition, especially against the will of the finance minister Tremonti. AN and UDC, in coalition with the trade union confederation CISL (the most representative union in the public sector), have always been open with respect to their interest in representing the vast constituency of public employees for whom they forcefully obtained the increase in the resources available for public sector contracts.

Politically, allowing for public sector wage inflation served two inter-twined purposes. For Berlusconi's *Forza Italia*, conceding inflationary wage increases in the public sector had the purpose of dividing the unions (the CISL from the irksome CGIL) during their open contestation regarding the government's reformist agenda. Berlusconi acted behind the scenes to support the political mediation of the deputy prime minister with the trade unions. For the Southern bloc of the coalition, Fini's political mediation came to serve their electoral interests perfectly. In courting their core constituency, the public employees, AN's leader Fini repeatedly proved himself capable of overcoming the opposition of the other coalition partner, the Northern League, which was opposed to generous public sector increases. Notwithstanding this opposition, Fini managed to exploit public sector wage increases in favour of political consent by successfully mobilising political capital to increase resources for public wages in subsequent budget laws. There has been, in this sense, a clear political willingness on the part of the Italian sovereign employers to grant inflationary wages for reasons other than the mere adjustment of the personnel expenditure to macroeconomic developments.

3.3 Public Sector Wage-setting in the Age of Sovereign Debt Crises: The Show must not Go on

The pattern of public sector wage inflation in Italy started to be reversed in the 2006-2008 wage bargaining cycle. This occurred under the pressure exercised by the finance minister Tommaso Padoa-Schioppa in the centre-left coalition in government. The finance minister strongly wished to enforce a wage freeze during the negotiations for the renewal of the 2006-2008 public sector contracts. This was meant to compensate for the wage excesses of the previous two bargaining cycles (2002-2004 and 2004-2006) which had occurred under the centre-right coalition in government. Wage freezes were only avoided at the very last minute thanks to the political mediation of the Prime Minister Romano Prodi during private negotiations with the heads of the public sector branches of the trade unions confederations (Interviews conducted with the then leaders of the public sector branch of CGIL (in Bologna, 20 November 2017) and of CISL (in Rome, 5 February 2018)). However, much less money was earmarked for public contracts and the result was a harsh conflict between the finance minister and the prime minister.

Measures for wage restraint were introduced unilaterally in 2008 (2009 budget law) written by Giulio Tremonti, before Italy came under pressure from the financial markets in summer 2011. Restraint was then strengthened by various governments (political and technocratic) in 2010 and 2011 and eventually extended in 2013 until, in spring 2015, a verdict of the Constitutional Court has declared the multi-year wage freeze pursued unilaterally by various governments since 2010 to be unconstitutional. The judgment forced the government to restart collective bargaining with the trade unions for the years ahead without, however, imposing compensation for lost purchasing power, which would have severely endangered the weak state of public finances. Legislation passed in 2008 had imposed a wage ceiling on the wage increases, declaring unlawful every wage agreement that went beyond the established ceiling. A decree law of May 2010 unilaterally cancelled wage rounds for 2010-2012. This freeze was then extended via administrative decision for the years 2013 and 2014 (Lorenzo Bordogna and Pedersini 2013).

Conclusions

Public sector wage-setting is an extremely interesting field in which to observe the discrepancies in policy-making between Germany and Italy. The relevance of public sector wage-setting in the political economy of European integration stems from two factors. Public sector wage policy coincides necessarily with fiscal policy. Given the enormous size of the public sector in advanced economies, divergent public sector wage trajectories can underpin discrepancies in the fiscal co-ordination of the EMU participants. Secondly, public sector wage-setting can produce negative spillovers for REER competitiveness, and underpin trade imbalances.

In Germany, the observable pattern of marked wage restraint started in the mid-1990s out of fiscal concerns by the federal finance minister. It was then driven by fiscal concerns of the *Länder* finance ministers, in the 2000s. As we observe the German public sector wage-setting regime today, after the reforms of the early 2000s, it emerges that *Länder* finance ministers are institutionally sheltered from political incursions and are locally accountable. Given the structure of its fiscal federalism and of the employers' interest representation, Germany is institutionally entrapped into a low-wage-increase equilibrium, which impedes a more inflationary stance in public sector wage-setting.

In Italy, the observable pattern of public sector wage inflation of the early 2000s can, first and foremost, be attributed to the political willingness of sovereign employers to tolerate inflation for strategic political advantages. Patterns of wage inflation in good times, followed by austerity and cuts in hard ones, resemble *hubris* and *nemesis* tragedies. For Italy to survive in a hard currency regime with Germany at its core, a re-structuring of its public sector wage-setting regime should be a priority so as to avoid de-stabilising wage/fiscal expansion and subsequent austerity measures. Cyclical developments in wage-setting are also likely to have a strong impact on the morale of public employees and the quality and efficiency of the public administration.

I wish to conclude with an important clarification. There is no pretension here to praise Germany and belittle Italy; nor should the reader see this paper as support for the austerity measures pursued as *nemesis* in the public sectors of the GIIPS. Rather, it is the opposite reasoning that motivates my inquiry: from the perspective of the EMU macroeconomic governance, both trajectories of marked restraint and inflation are equally deplorable.

Indeed, the core countries of the EMU have been able to produce stable public sector wage trajectories both before and after the crisis (Figure 1). This has contributed to stabilise their REERs (Figure 2). Hence, a more balanced approach to public sector wage policies exists, and not just in abstract terms. Future research could take off from this observation and ask what the institutional determinants of balanced wage growth in public sectors are. Looking at these countries' public sector wage-setting regimes should teach us something about how to design a set of institutional changes aimed at avoiding the problem of structural divergence when the good times return.

References

Baccaro, Lucio, and Chiara Benassi. 2016. “Throwing out the Ballast: Growth Models and the liberalization of German Industrial Relations.” *Socio-Economic Review*: mww036.

Baccaro, Lucio, and Harry Jonas Pontusson. 2016. “Rethinking Comparative Political Economy: The Growth Model Perspective.” *Politics & Society*.

Baccaro, Lucio, and Tobias Tober. 2017. “The Role of Cost and Price Competitiveness in the Eurozone.” Unpublished Manuscript, University of Geneva.

Bach, Stephen, and Lorenzo Bordogna. 2013. *Reframing Public Service Employment Relations: The Impact of Economic Crisis and the New EU Economic Governance*. Sage London: Publications Sage UK: London.

———. 2016. *Public Service Management and Employment Relations in Europe: Emerging from the Crisis*. Abigdon: Routledge.

Bibow, Jörg. 2012. *The Euro Debt Crisis and Germany's Euro Trilemma*. Levy Economics Institute of Bard College: Levy Economics Institute,

Bordogna, L, C Dell'Aringa, and G Della Rocca. 1999. “The Reform of Public Service Employment in Italy: A Case of Coordinated Decentralization”, in: Bach. S., Bordogna, L., Della Rocca, G., and Winchester, D.(eds), *Public Service Employment Relations in Europe: Transformation, Modernization or Inertia*.

Bordogna, Lorenzo. 1994. “Pluralismo senza mercato.” *Franco Angeli, Milano*.

———. 2012. “Employment Relations and Union Action in the Italian Public Services-Is There a Case of Distortion of Democracy.” *Comp. Lab. L. & Pol'y J.* 34: 507.

Bordogna, Lorenzo, and Roberto Pedersini. 2013. “Economic Crisis and the Politics of Public Service Employment Relations in Italy and France.” *European Journal of Industrial Relations* 19 (4): 325-40.

Carlin, Wendy, and David Soskice. 2014. *Macroeconomics: Institutions, instability, and the Financial System*. New York: Oxford University Press.

Cassese, Sabino. 1977. *Questione amministrativa e questione meridionale: dimensioni e reclutamento della burocrazia dall'unità ad oggi*. Giuffrè.

Cella, Gian Primo. 1991. “Nuovi attori nelle relazioni industriali.” *Milano, ed. Franco Angeli*.

Collignon, Stefan. 2009. “Wage Developments in Euroland or: the Failure of the Macroeconomic Dialogue.” *Sant'Anna School of advanced Studies, Pisa/Centro Europa Ricerche, Roma*.

De Grauwe, Paul. 2016. *Economics of Monetary Union*. Oxford: Oxford University Press.

DGB. 2016. “Besoldungsreport 2016. Die Entwicklung der Einkommen der Beamtinnen und Beamten von Bund, Ländern und Kommunen.”, published online May 2016. https://www.google.de/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&ved=0ahUKEwiUrPiSseDTAhXFKVAKHaQZDCAQFggpMAA&url=http%3A%2F%2Fwww.dgb.de%2F%2B%2Bco%2B%2Bcb6f18d4-15d5-11e6-a659-52540023ef1a%2FDGB-Besoldungsreport-2016.pdf&usg=AFQjCNF80mHJF_iqAcB2Z_IA2etIvEU7hw&cad=rja.

Di Carlo, Donato. 2018. *Does Pattern Bargaining Explain Wage Restraint in the German Public Sector*. 18/3. Cologne: Max Planck Institute for the Study of Societies,

Diamanti, Ilvo. 2003. *Bianco, rosso, verde... e azzurro. Mappe e colori dell'Italia politica*. Il mulino.

Diamanti, Ilvo, and Elisa Lello. 2005. “The Casa delle Liberta: a house of cards?” *Modern Italy*

10 (1): 9-35.

Dribbusch, Heiner. 2006. "Strike against increase in working time ends in compromise." published online 26 June 2006. https://www.eurofound.europa.eu/ga/observatories/eurwork/articles/strike-against-increase-in-working-time-ends-in-compromise.

Giugni, Gino. 1992. "La Privatizzazione del rapporto di lavoro nel settore pubblico." *Lavoro informazione* 11: 5-8.

Gorrieri, Ermanno. 1973. *La giungla retributiva*. Il mulino.

Hancké, Bob. 2013. *Unions, Central Banks, and EMU: Labour Market Institutions and Monetary Integration in Europe*. OUP Oxford.

Hancké, Bob, and Martin Rhodes. 2005. "EMU and Labor Market Institutions in Europe The Rise and Fall of National Social Pacts." *Work and Occupations* 32 (2): 196-228.

Hassel, Anke. 2014. "The Paradox of Liberalization—Understanding Dualism and the Recovery of the German Political Economy." *British Journal of Industrial Relations* 52 (1): 57-81.

Holm-Hadulla, Fédéric, Kishore Kamath, Ana Lamo, Javier J Pérez, and Ludger Schuknecht. 2010. "Public wages in the euro area: towards securing stability and competitiveness." *ECB Occasional Paper* (112).

Höpner, Martin, and Mark Lutter. 2014. "One Currency and Many Modes of Wage Formation. Why the Eurozone is too Heterogeneous for the Euro."

Hyman, Richard. 2008. *The State in Industrial Relations*. Sage Publications.

Johnston, Alison. 2016. *From Convergence to Crisis: Labor Markets and the Instability of the Euro*. Ithaca NY: Cornell University Press.

Johnston, Alison, and Bob Hancke. 2009. "Wage Inflation and Labour Unions in EMU." *Journal of European Public Policy* 16 (4): 601-22. doi:Pii 91115071210.1080/13501760902872742.

Johnston, Alison, Bob Hancke, and Suman Pant. 2014. "Comparative Institutional Advantage in the European Sovereign Debt Crisis." *Comparative Political Studies* 47 (13), published online Nov: 1771-800. doi:10.1177/0010414013516917.

Keller, Berndt. 2011. "After the End of Stability: Recent Trends in the Public Sector of Germany." *The International Journal of Human Resource Management* 22 (11): 2331-48.

———. 2014. "The Continuation of Early Austerity Measures: The Special Case of Germany." *Transfer: European Review of Labour and Research* 20 (3): 387-402.

———. 2016. "8 Germany: Retrenchment Before the Great Recession and its Lasting Consequences." *Public Service Management and Employment Relations in Europe: Emerging from the Crisis* 26: 191.

Keller, Berndt, and Hartmut Seifert. 2015. "Atypical Forms of Employment in the Public Sector–Are there any?".

Ricciardi, Mario. 2013. "La parabola: ascesa e declino della contrattazione collettiva in Italia."

Rusciano, M. 1978. *Il pubblico impiego in Italia*. Il Mulino, Bologna.

Santoro, Patrizia. 2014. *Deboli ma forti. Il pubblico impiego in Italia tra fedeltà politica e ammortizzatore sociale: Il pubblico impiego in Italia tra fedeltà politica e ammortizzatore sociale*. FrancoAngeli.

Scharpf, Fritz W. 1991. *Crisis and Choice in European Social Democracy*. Ithaca NY: Cornell University Press.

———. 2005. “No Exit from the Joint Decision Trap?: Can German Federalism Reform itself?”.

Talamo, Valerio. 2009a. “Gli interventi sul costo del lavoro nelle dinamiche della contrattazione collettiva nazionale ed integrativa.” *Lav. Pubb. Amm*: 3-4.

———. 2009b. “Pubblico e privato nella legge delega per la riforma del lavoro pubblico.” *Giornale di diritto amministrativo* 5: 3-14.

Traxler, Franz. 1999. “The State in Industrial Relations: A Cross-national Analysis of Developments and Socioeconomic Effects.” *European Journal of Political Research* 36 (1): 55-85.

GEO-POLITICS OF EXPORTING TOO MUCH: CONTRASTING TRAJECTORIES OF GERMANY AND JAPAN

Margarita Estévez-Abe

Maxwell School, Syracuse University

Collegio Carlo Alberto

"Ten times Trump asked [Ms Merkel] if he could negotiate a trade deal with Germany. Every time she replied, 'You can't do a trade deal with Germany, only the EU.'"[96]

I. Introduction: Going Beyond the North-South Problems inside the Euro Zone

The financial crisis—the Eurozone crisis in particular—initiated an important debate over the distributive implications of the EMU. Aside from questioning the wisdom of the austerity policies imposed by the Troika—the European Commission (EC), the European Central Bank (ECB), and the International Monetary Fund (IMF)—many people began to focus on what they perceived to be the structural problems of the EMU. The EMU, it was argued, structurally advantaged the Northern European economies at the expense of the weaker Southern European economies. The single currency rewarded the Northern European member states with a weak currency (much weaker counterfactually than in the absence of the EMU), while it punished the Southern European member states by robbing them of the policy tool they long relied upon to boost their competitiveness—i.e. currency devaluation (Hall 2012, Streeck 2015). The Euro thereby improved the terms of trade for the Northern European member states. As a consequence, the German economy boomed after the crisis, while the citizens of Greece, Italy and Spain suffered from austerity policies (Blyth 2012). This debate fed a morality play that portrayed the Greeks, Italians and Spaniards as the morally inferior lazy brethren of Northern Europeans. It appeared as if European solidarity was giving way to an ugly family feud over who owes what to whom.

The aim of this paper is to extend the discussion beyond Europe and the EMU. The consequences of the EMU go well beyond the Euro-zone borders. Not only did the Euro improve the terms of intra-EMU trade for the Euro-zone North; it also improved their competitiveness outside Europe. The first meeting between Chancellor Angela Merkel and the President Donald Trump focused attention on the importance of Germany's relatively advantageous trade terms. Trump bitterly complained about Germany—the largest economy in Europe. Trump took aim at the German trade surplus, and demanded a bi-lateral agreement to rectify the "unfair" trade imbalance between the two countries. While European elites shrugged off Trump's comments as the ramblings of an uncouth novice who did not understand how the EU worked, the reality was actually the other way around. It was European—and German—elites who had been too slow to realize that they could no longer free-ride on the Americans. Trump's statements about trade imbalances and NATO funding actually reflect an inconvenient truth for Europeans: the Marshall Plan era is over. Europe and the US can no longer count on the presence of a common enemy to unite them.

Germany is an exporting powerhouse. It is the third largest exporter in the world after China and the US. Germany exports almost as much as the US does. The volume of German exports is close to twice as large as that of Japan, the fourth largest exporter. Germany, however, stands out for its trade surplus. For an economy of its size, it imports relatively little. In fact, as Baccaro and Pontusson (2016) note, Germany relies on foreign—rather than domestic—demand to stim-

96 This is the report of the meeting between the Chancellor Angela Merkel and the President Donald Trump in March 2017. https://www.independent.co.uk/news/world/americas/us-politics/angela-merkel-donald-trump-explain-eu-trade-11-times-germany-chancellor-us-president-a7699591.html

ulate its economy. When a large wealthy economy relies on foreign demand to propel its economy, other countries must pay the price in trade deficits. Even within the EU, criticisms of this beggar thy neighbor policy emerged (Varoufakis 2017). Outside the EU, the same criticisms have led to serious geo-political tensions between the US and Europe.

This short paper argues that the dramatic rise in German exports would not have happened without the Euro, and that the EU has served as a cover to shield Germany from any bi-lateral trade disputes that might have emerged. Consequently, the German growth model has exacerbated geo-political problems between two sides of the Atlantic. This paper uses Japan as a counter-factual case to highlight the importance of the special advantages that Germany enjoys thanks both to the EMU and the EU.

II. Similar Pasts and Similar Challenges, but Charting New Paths

Germany and Japan provide us with a pair of similar cases—two economies that are alike in many ways except one had the protection of the EU and EMU while the other did not. This paper takes advantage of the initial similarities and divergences following the creation of the EMU. This particular combination of similarities and divergences makes Germany and Japan an ideal pair of comparative cases to explore the effects of the EMU. First, let me talk about their initial similarities before moving on to the discussion of their more recent divergent paths.

During the postwar period, Germany and Japan emerged as competitive economies that possessed distinctive characteristics. Their models of capitalism inspired a whole generation of comparative studies of economic/ production regimes in the 1980s and 1990s.[97] Wolfgang Streeck's work on the German production regime and Masahiko Aoki's work on the Japan firm provide pioneering examples of this scholarship.[98] Indeed, Germany and Japan became the real life models that helped the conceptualization of Coordinated Market Economies (CMEs) in the Varieties of Capitalism literature.[99] They both shared similar characteristics: neither was a neo-corporatist system, but both had developed organizational capacities to coordinate economic activities. Firms cooperated with one another, and employers did the same with their employees in their joint effort to innovate and navigate the ups and downs of business cycles. In both countries, banks and closely-knit corporate ownership patterns stood out.

Their economic success stories of the 1970s and 1980s notwithstanding, the 1990s brought daunting challenges to both countries. The German economy suffered after the re-unification and unemployment rates soared. This was the period when Germany was nicknamed "the sick man of Europe." Japan fared no better. After the burst of the so-called Bubble Economy in the early 1990s, Japan plunged into a long period of economic stagnation. Furthermore, the two countries also began to experience demographic problems. Their models of welfare capitalism assumed households with male-breadwinners. Their employment practices and welfare states had developed with traditional gendered divisions of labor in mind, whereby men were expected to become breadwinners and women were expected to become unpaid carers for their families (Daly 2011; Lister 1994; Leitner 2003; Sainsbury 1994). Comparatively strong employment regulation in Germany and Japan protected male breadwinners' jobs, and their welfare states mostly addressed the needs of male breadwinners. The other side of the coin was sex-discriminating employment prac-

97 The Varieties of Capitalism literature in many ways synthesized and built upon their contributions. See footnote 3.

98 Aoki (1983), Cole (1971, 1989), Dore (1973), Patrick (1976), Streeck (1984,1992) represent some of the most influential contributions that initiated firm-level comparative analyses of advanced industrial countries.

99 For instance, when Estévez-Abe et al (2001) distinguish CMEs that rely on firm-specific skills and industry-specific skills, this distinction heavily relies on the Japanese (firm-specific) and German (industry-specific) cases.

tices and underdeveloped services for working mothers—i.e. scarcity of work-family reconciliation policies (Estévez-Abe 2005, 2006). As a result, maternal employment rates in these countries remained lower than the OECD average. Given the fact that among the OECD countries fertility rates are higher where female labor force participation rates are high, it is not surprising that fertility rates plunged in Germany and Japan. It is no coincidence that they are the most "aged" OECD countries.

The economic fortunes of the two countries began to diverge in the 2000s and the pace of divergence accelerated after the financial crisis in 2008. While Germany recovered from its economic stagnation in the 1990s, Japan did not. In Germany, as the economy recovered and unemployment rate went down in the latter half of the 2000s, labor shortages became the new problem. Demographic aging means the shrinking of younger cohorts, and it directly affects the number of young male workers who are available in the labor market. There are two potential solutions: (i) to increase the activity rate of the native population; and or (ii) to increase immigration. Germany did both in the latter half of the 2000s. The Hartz Reforms and the pension reform removed work disincentives and pushed up male employment rates. Germany also began to promote female employment and immigration of skilled foreigners (Blome 2016: Constant and Bienvenue 2011; Hien 2013; Morgan 2013; Wiliarty 2010). Japan, in contrast, just stagnated. In spite of its shrinking workforce, Japan did not feel the labor market crunch as early as Germany because of its prolonged recession. This long recession motivated many women to enter the labor market, which in turn further depressed wages. What the Japanese initially referred to as "the lost decade" of the 1990s, eventually became the "lost decades." Japan could not export its way out of the economic recession as Germany had done, as its currency kept on strengthening against the dollar. Japan thus tried to boost domestic demand. This effort yielded a national public deficit of 237% of the GDP compared to 79% in Germany. Germany, in contrast, turned to foreign demand and overtook Japan as an exporting superpower. Furthermore, as demand for skilled labor increased, Germany increasingly recruited women and foreigners. In Japan, such changes are only occurring now—with a delay of ten years (Estévez-Abe and Naldini 2016).

III. Why Did Their Economic Fates Diverge?

Why did the trajectories of Germany and Japan come to diverge so much? Proponents of the Varieties of Capitalism might attribute the German economic success to its CME. By the same token, they might argue that Japan's relative decline is due to Japan not really being a CME any longer.[100] This explanation is too shallow. Baccaro and Pontusson (2016) are right to claim that a dichotomous taxonomy that omits so many countries does not provide the best model tool to understand the challenges facing super- aging mature economies. Baccaro and Pontusson (2016) pay greater attention to how mature countries manage "demand-side" factors in their effort to promote economic growth.[101] They argue that Germany explicitly chose to seek out foreign demand while neglecting to expand its own domestic demand. They point out how the German employers and unions made a pact to reduce wages when they joined the EMU in order to preserve their competitiveness in an effort to capture foreign markets.

I agree with the importance of examining the demand management particularly in the context

100 Iversen and Soskice dropped Japan from their list of CME as they shifted their analysis to the causal link between CMEs and proportional representation systems (see Cusack, Iversen and Soskice 2007). Others have continue to look at Japan as a form of highly organized capitalism (Estévez-Abe 2008; Streeck and Yamamura eds. 2005).

101 Baccaro and Pontusson (2016) criticize the VOC as being too "supply-side" in their justification of their demand-side approach. However, Michael Piore (2016) is correct to point out, in his commentary on Baccaro and Pontusson (2016), that the "macro" versus "micro" distinction might be more appropriate to describe how Baccaro and Pontusson situate themselves vis-à-vis the VOC rather than the contrast between "demand-side" and "supply-side."

of demographic aging. That said, Baccaro and Pontusson (2016) fail to pay attention to the specific advantages that Germany enjoyed under the umbrella of the EMU and the EU. As Baccaro and Pontusoon (2016) claim, Germany initially moderated its wage growth in its attempt to seize greater market shares in the new single market initially. But it would not have been able to capture so much of foreign demand had it not been for the EMU/EU framework.

The EMU—in combination with other advantages the EU provides—helped create extremely favorable conditions for German exporters. First, Germany benefited handsomely from the new single currency, which, because it reflects the macro-economic performance of all Euro-zone countries, including some quite dysfunctional ones, will always appreciate less than the Deutsch-Mark would have done. Second, the EU harmonized all key product regulations across the EU member states removing any trade barriers. Third, the EU shielded Germany from any possibility of having to engage in unfavorable bi-lateral negotiations, whether with any specific EU member-state or powerful non-EU trading partner such as the US. Four, the Schengen Agreement expanded the potential labor pool for Germany.

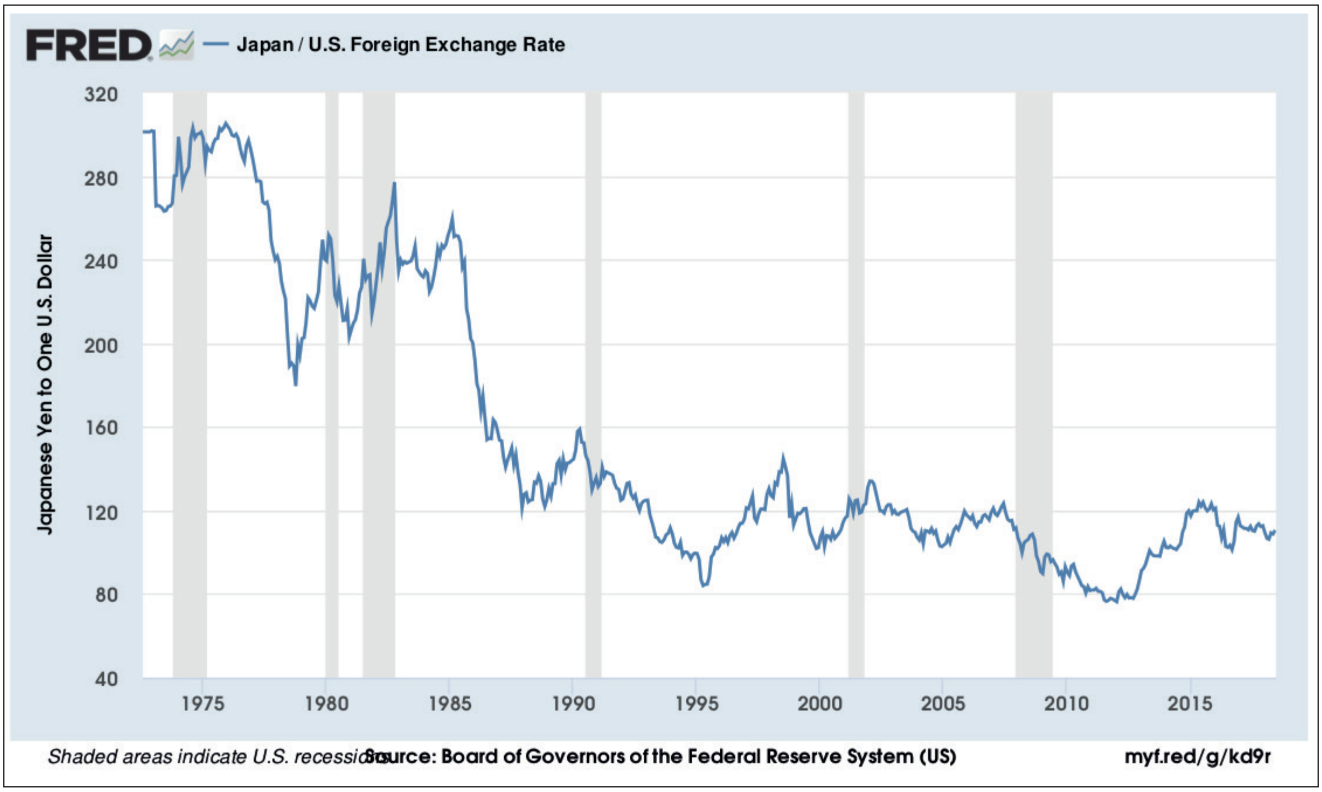
The first two conditions *de facto* turned the Euro-zone into a big domestic market for German exporters as they no longer faced any currency risk in trading within the Euro-zone. Because the monetary union also took away less competitive countries' capacity to devalue, more competitive countries were better-positioned to reap the benefit of the bigger single market. Germany was such a country—and a huge one by European standards. Germany enjoyed a scale of merit due to the size of its own domestic market, and now could enjoy an even bigger scale of merit thanks to the expanded *de facto* domestic market. Furthermore, Germany also had easy access to the markets in those EU member states outside the Euro-zone such as the UK. Given that the national currencies of non-Euro-zone member states tended to appreciate more, Germany again stood to gain from favorable terms of trade. In 2006, the combined economy of the EU28 was the largest in the world accounting for 30% of global GDP (Eurostat 2018). Ten years later, it fell to 25% and became the second largest after the US, but these numbers underscore the importance of the advantage that Germany gains from easy access to this market.

Furthermore, the third and fourth conditions removed potential bottlenecks for Germany's export-oriented strategy for growth. The EU shielded Germany from any trade sanctions. Indeed, if any sanctions were to be threatened, they would have to target the whole of the EU. No less importantly, Germany enjoyed access to a vast labor pool within the Schengen area. If Germany had not enjoyed the aforementioned four conditions, it would have struggled to manage its aging society and would have suffered similar economic problems to those facing Japan.

IV. Exposure to Currency Risk, Euro and the Distorted Geo-Politics of Trade: Germany Gains and Japan Loses

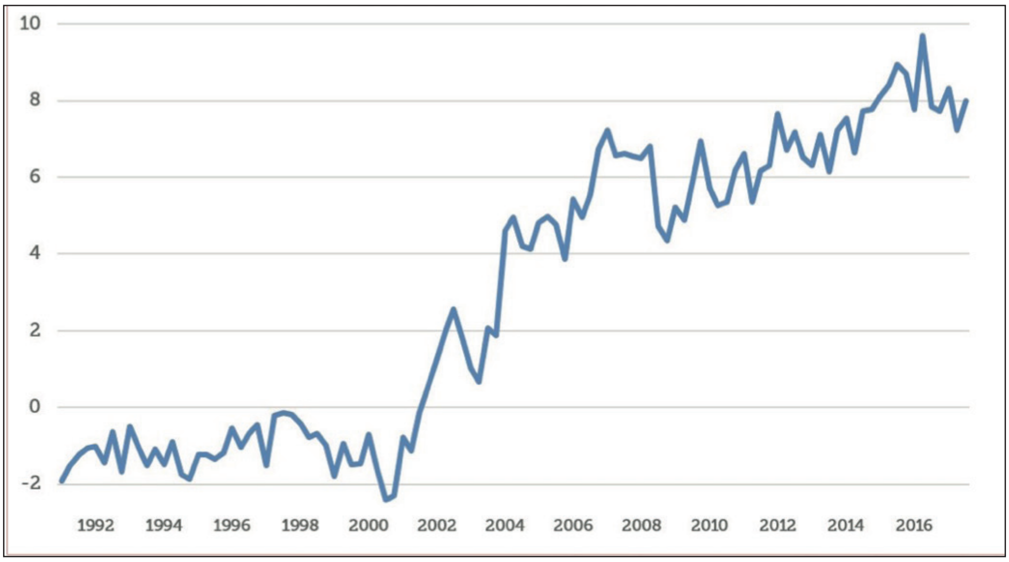
Let us now contrast Japan to Germany. Japan faced a completely different, significantly more volatile exchange rate environment. The first currency shock came in 1985, when the Finance Ministers from the G5 countries met in the Plaza Hotel in New York City and agreed to intervene in the currency market to raise the value of the Japanese yen. The so-called Plaza Accord was an action orchestrated by the US to correct Japan's allegedly unfair currency advantage, which allowed it to enjoy a large trade surplus with the US. Figure 1 shows the dramatic currency fluctuations against the dollar that Japan has experienced over the past forty years. Immediately after the Plaza Accord, the value of the US dollar nearly halved against the yen within a matter of months. This was the first of three drastic waves of currency appreciation that Japan was to experience: the second one in 1994/5, and then again in the late 2000s. Japan's off-shoring of productive facilities abroad had started in earnest in the mid-1990s increasing the relative share of foreign production of Japanese manufacturers. Given the fact that the US is its major export market, drastic currency appreciation meant losing price competitiveness in the US as well as suffering the earning losses as the earnings were calculated in the Japanese yen. The harsh currency environment made it indispensable for Japan to boost its domestic market. While private companies struggled to adjust their business models to the new currency environment, the public sector tried to compensate for the shortfall in demand due to recession and demographic aging. In the aftermath of the financial crisis, another wave of currency appreciation negatively affected Japanese exports in an already weak global market. In contrast, Germany enjoyed its biggest ever trade surplus—roughly 9% of its GDP in the post-crisis years.

Figure 1. Shifts in the Value of the US Dollar in Japanese Yen (1975-2018)



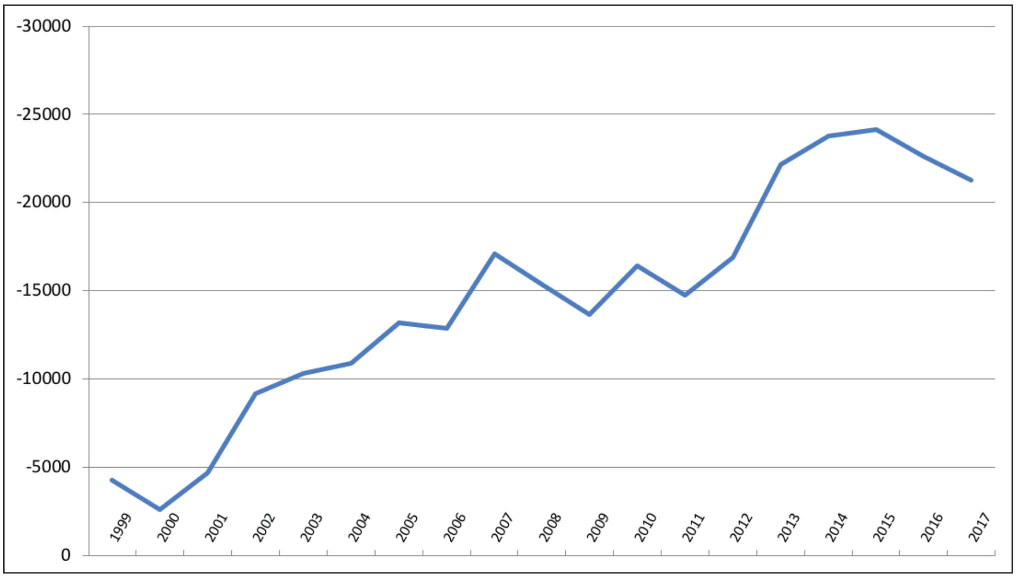
Both Germany and Japan faced different but similarly dramatic economic shocks in the 1990s and in the 2000s. However, the structural advantage provided by the Euro made it much easier for Germany to deal with its problems after 2000. As mentioned earlier, Germany faced the shock of the German re-unification, which sent its economy into a prolonged economic downturn. Germany's high levels of unemployment rates continued throughout the 1990s. The uptake in the exports occurred before the labor market and welfare reforms in the early and mid-2000s—the Hartz Reforms and the Pension Reform—and grew larger afterwards. Germany's current account surplus grew more or less steadily after joining the EMU (Figure 2). In addition to the increase in Germany's within the Euro-zone trade volume, Germany also gained a lot from non-Eurozone member states such as the UK. Again, Figure 3 shows how British trade deficit with Germany grew after Germany joined the EMU. When the Euro-crisis and the austerity policies in a number of largest member states suppressed the demand for German products, Germany turned to other export markets including China and the US. Figure 4 shows how German (as well as the overall European) trade surplus with the US rapidly increased as a combination of weak domestic demand in EU member states and reliance on foreign demand as the US economy recovered from the crisis.

Figure 2. Germany's Current Account Surplus



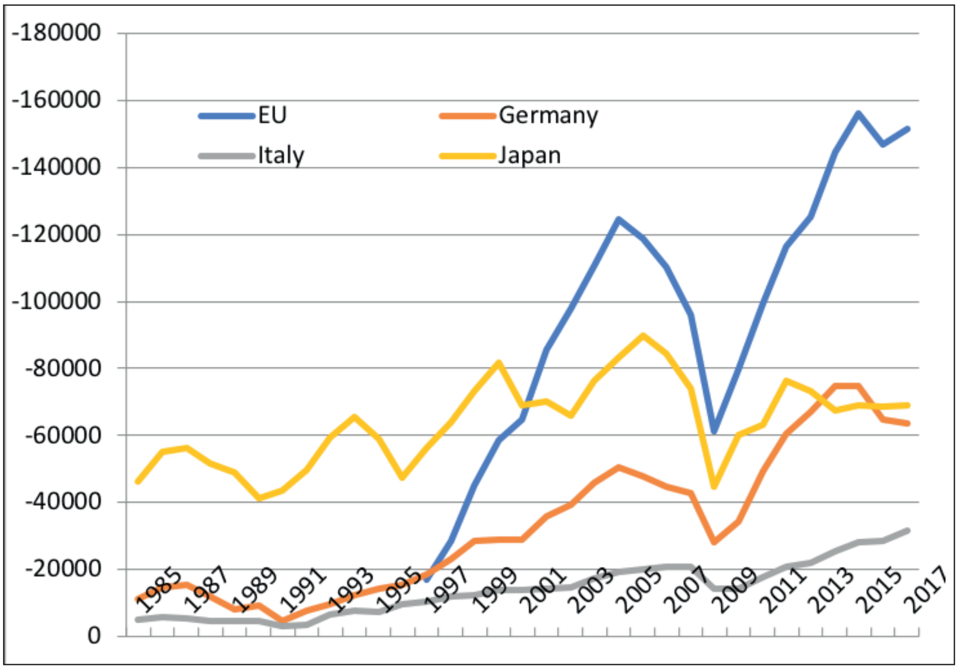
Source: Romano 2018, p.8.

Figure 3. British Trade Deficit in Goods and Services with Germany (in British pounds)



Source: https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/timeseries/lgmi/pb

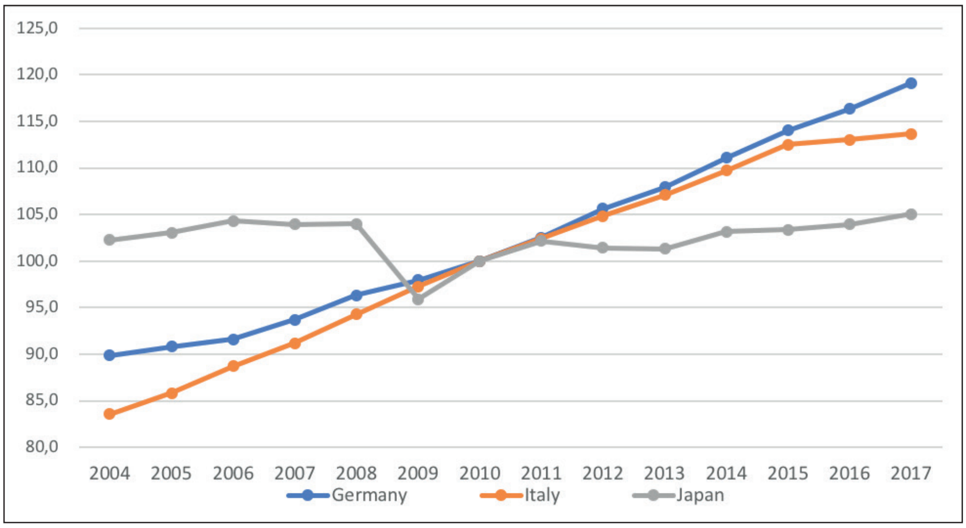
Figure 4. US Trade Deficit in Goods with Germany and Other Selected Trade Partners (in US dollars)



Source: The US Census Bureau, Foreign Trade Data. https://www.census.gov/foreign-trade/balance/index.html

Japan, in turn, faced two major financial shocks in the 1990s—the first was the burst of its own speculative bubble in the early 1990s and the second was the Asian Financial Crisis in 1997, which hit hard Japanese major banks since they were big lenders in many of the countries affected by the crisis. Unlike Germany, whose recovery was aided by the Euro, Japan was penalized by extremely unfavorable exchange rates. In the years immediately following the burst of the so-called bubble economy, Japan experienced another drastic currency appreciation in 1994/1995. The Japanese growth rate of multifactor productivity was higher than that of Germany throughout the 1990s, but Japan began to underperform relative to Germany in the 2000s.[102] A further blow to Japan was the third dramatic wave of currency appreciation, which came right after the 2008 Financial Crisis. Japanese export performance worsened and wage levels in manufacturing began to drop as shown in Figure 5.

Figure 5. Hourly Wages in Manufacturing (2010=100)



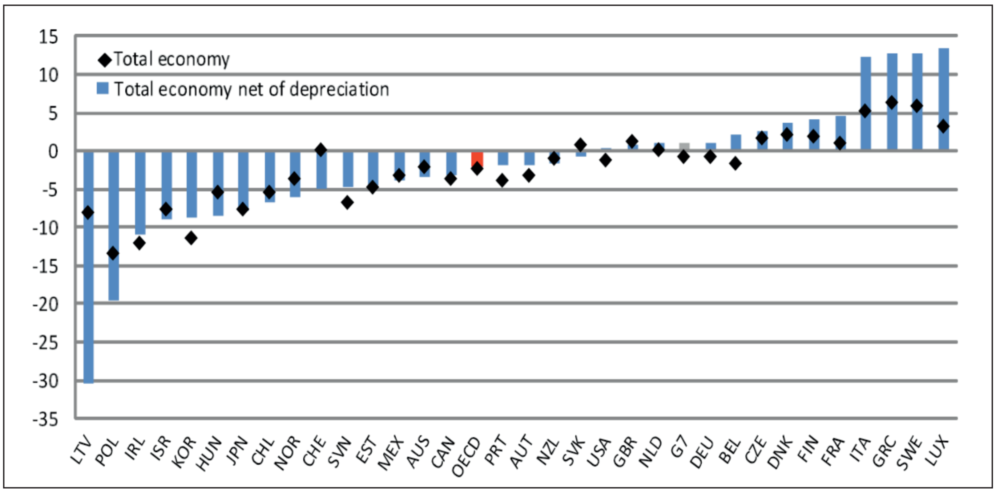
Source: OECD Statistics

As Figure 6 indicates, the drop in labor share was much bigger in Japan than in Germany. As in Germany, labor market deregulation led to a dualization of the labor market. However, unlike

102 OECD (2018), Multifactor productivity (indicator). doi: 10.1787/a40c5025-en (Accessed on 22 June 2018)

Germany, Japan had no access to an expanded Euro-denominated quasi-domestic market. In a shrinking market with strong currency, corporations maintained their profits by paying their workers less. In the absence of the advantages of Euro, the strong yen led Japanese manufacturers to off-shore most of their production, and the number of workers employed in manufacturing decreased more in Japan than in Germany and Italy. The new demand composition in Japan's aging society added low wage service sector jobs to the economy instead. Schwellnus et al. 2017 calculate that most of the decline in labor's share of the economy in Japan can be attributed to the reduction of labor share in service jobs, while in Germany the decline originated in its manufacturing sector. If the Euro did not exist, Germany with its strong national currency would have off-shored its production to a much greater degree. Revenue from investments in Eurozone countries would have suffered from currency volatility—earnings going down every time the Deutsche Mark appreciates.

Figure 6. Changes in Gross and Net Labor Shares in OECD Countries, 1995-2014



Source: Schwellnus et al. 2017.

V. Geo-Political Implications of Too Much Surplus

Germany's trade surplus affected the geopolitical relationship between the EU and the United States. Geopolitically, both Germany and Japan are similar. Partly for historical reasons, they both underspend on their own defense budgets and rely on others—the US or the NATO—to provide security. Germany benefitted greatly from the EU, which not only foreclosed any possibility of bi-lateral trade negotiations between a member state and a non-EU country, but made it difficult to link trade and security issues. This meant that Germany could continue to amass trade surplus against the US, but the US could not raise issues about Germany's meager defense budget. The situation in Japan was very different.

Throughout the 1980s and the 1990s, Japan's large trade surpluses with the United States led to multiple rounds of bi-lateral negotiations between the two countries (Schoppa 1997). The Plaza Accord must be seen as the US's reaction against Japan's trade surplus. In the US-Japan bi-lateral negotiations, security and trade issues were linked, and the negotiations prompted Japan to agree to various concessions. Japan "self-imposed" an unofficial export quota to the US; built factories in the US; paid for the cost of the US military bases in Japan; coordinated its monetary policy with the US; and procured overpriced military weapons from the US. Furthermore, the US demanded that Japan adopt expansionary monetary and fiscal policies to boost its own domestic demand (and to buy more US goods); and Japan obliged by means of a low interest rate policy and greater public investments. The monetary expansion right after the

Plaza Accord led to the rise of a speculative bubble in Japan, which fed the Bubble Economy of the 1980s. Unconstrained by anything like the Maastricht Treaty and helped by its abundant domestic savings, the Japanese government continued its fiscal expansion.

Figure 7. Growth Accounting

YEARLY GROWTH RATE				
	Total output	Capital stock	Labor input	Total factor productivity
Japan				
1970-1990	4.45	2.35	0.73	1.37
1990-2007	1.24	0.85	–0.06	0.44
2007-2011	–0.79	0.13	–1.24	0.33

Source: Sánchez and Yurdagul (2017)

The US Government has been complaining about Germany's excessive reliance on foreign demand (i.e. exports). However, as Merkel explained to Trump, no bi-lateral negotiations are possible, because foreign trade is an EU competence. The inability of the largest European economy to work out bi-lateral solutions has now led the Trump Administration to raise the specter of tariffs against the whole of the EU. One could argue that the whole of the EU is now paying the price for German trade surpluses. Furthermore, the inability of the US to link security and trade issues in dealing with the EU trade partners seems to be eroding the very foundation of the NATO. Again, the history of the Japan-US trade conflicts and the negotiations can tell us what counterfactually would have happened to Germany in the absence of the EU and the Euro. Like Japan, Germany probably would have had to build more factories in the US as a way of cultivating political capital in the US (Japanese big manufactures cleverly invested in "swing states" for Presidential elections) and to buy more "made in US" military weaponry.

Conclusion

When domestic demand starts to contract due to demographic aging, it is very difficult for the government to fins a quick solution. It can either export more or boost domestic demand. This short paper has argued that Germany enjoyed special advantages. In the absence of the EU and the monetary union, Germany would have suffered the long stagnation of Japan. Baccaro and Pontusson (2016) argue that it was the political coalition in Germany that led Germany to rely heavily on foreign demand in lieu of any attempt to boost domestic demand. They contrast Germany to the UK and Sweden as examples of countries that have adopted more lax consumer loans and mortgage lending to boost domestic demand for different reasons. Although it is not mentioned in their piece, it is important to note that these were both countries outside the monetary union and hence could not enjoy the benefits Germany enjoyed. The Netherlands, which is a smaller country, which thrived within the monetary union, exports a lot and does not resort to financial policies to boost domestic demand. Given its small population size, they are the third largest exporter of agricultural goods in the world. Unlike the Netherlands, Denmark, another member state that stayed out of the currency union, also relies on domestic demand stimulation by extremely accommodating mortgage policies. Japan, too, shifted to expansive monetary policy in the 1980s in its attempt to stimulate domestic demand. Once the speculative bubble burst in Japan, the prolonged banking crisis in the 1990s that continued into the early 2000s, prevented Japanese banks from doing the same. In the absence of the past banking crisis, Japan most likely would have pursued a similar policy to stimulate domestic demand.

References

Aoki, Masahiko. 1983. *The Economic Analysis of the Japanese Firm*. Elsevier Science Ltd.

Baccaro, Lucio and Jonas Pontusson. 2016. "Rethinking Comparative Political Economy: The Growth Model Perspective." *Politics and Society*. 44(2): 175-207.

Blome, Agnes. 2016. *The Politics of Work-family Policy Reforms in Germany and Italy.* NY: Routledge.

Blyth, Mark. 2012. *Austerity: A History of a Dangerous Idea.* New York: Oxford University Press.

Cole, Robert. 1971. *Japanese Blue-Collar: The Changing Tradition*. Berkeley, CA: University of California Press.

Cole, Robert. 1989. *Strategies for Learning: Small Group Activities in American, Japanese, and Swedish Industry*. Berkeley, CA: University of California Press.

Constant, Amelie F., and Tien, Bienvenue N. 2011. "Germany's Immigration Policy and Labor Shortages" IZA Research Report No.41. October 2011.

Cusack, Thomas R. Torben Iversen and David Soskice. 2007. "Economic Interests and the Origins of Electoral Systems." *The American Political Science Review.* 101(3):373-391.

Daly, Mary. 2011. "What Adult Worker Model? A Critical Look at Recent Social Policy Reform in Europe from a Gender and Family Perspective." *Social Politics* 18(1): 1-23.

Dore, Ronald. 1973. *British Factory, Japanese Factory*. Berkeley, CA: University of California Press.

Eurostat. 2018. "A new Eurostat publication A statistical portrait of the European Union compared with G20 countries The EU in the world – 2018 edition" Eurostat Newsrelease 116/2018. https://ec.europa.eu/eurostat/documents/2995521/9077665/1-11072018-AP-EN.pdf/4446ce4e-d45c-4b31-9108-23ebb026ea20

Estévez-Abe, Margarita. 2008. *Welfare Capitalism in Postwar Japan*. Cambridge University P ress.

Estévez-Abe, Margarita. 2006. "Gendering the Varieties of Capitalism: A Study of Occupational Segregation by Sex in Advanced Industrial Societies," *World Politics* (October, 2006): 142-175.

Estévez-Abe, Margarita. 2005. "Gender Bias in Skills and Social Policies: The Varieties of Capitalism Perspective on Sex Segregation," *Social Politics* vol.12, no. 2 (Summer 2005): 180-215.

Estévez-Abe, Margarita. "Reinterpretation of the Welfare State. " with Torben Iversen and David Soskice in Peter Hall and David Soskice eds. *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*. London: Oxford University Press.

Hall, Peter A. (2012) The Economics and Politics of the Eurozone Crisis." *German Politics* 21(4): 355-371.

Hien, Josef (2013) "Unsecular Politics in a Secular Environment: The Case of Germany's Christian Democratic Union Family Policy." *German Politics.* 22(4): 441-460

Leitner, Sigrid. 2003. "Varieties of Familialism: The Caring Function of the Family in Comparative Perspective." *European Societies* 5(4): 353-375

Lister, R. 1994. "She has other duties' Women, Citizenship and Social Security. In S Baldwin and J. Falkingham eds. Social Security and Social Change: New Challenges to the Beveridge's Model.

Morgan, Kimberly J. 2013. "Path Shifting of the Welfare State: Electoral Competition and the Expansion of Work-Family Policies in Western Europe." *World Politics* 65(1): 73-115

Patrick, Hugh. ed. 1976. *Industrialization and Its Consequences for Japan*. Berkeley, CA: University of California Press, 1976.

Piore, Michael. 2016. “Varieties of Capitalism Theory: Its Considerable Limits.” *Politics and Society*. 44(2): 237-241.

Sainsbury, Diana. Ed. 1994. *Gendering the Welfare States*. London. Sage Publications.

Schoppa, Leonard. 1997. *Bargaining with Japan*. NYC: Columbia University Press.

Streeck, Wolfgang. 2015. “Why the Euro divides Europe.” *New Left Review* 95 (September/October2015): 5–26.

Streeck, Wolfgang, and Kozo Yamamura eds. 2005. *The Origins of Non-Liberal Capitalism: Germany and Japan in Comparison*. Ithaca, NY: Cornell University Press.

Streeck, Wolfgang. 1992. Social Institutions and Economic Performance: Studies of Industrial Relations and Advanced Capitalist Economies. Sage Publications.

Streeck, Wolfgang. 1984. *Industrial Relations in Germany: A Case Study of the Car Industry*. Heinemann Educational Books.

Varouvakis, Yannis. 2017. *Adults in the Room: My Struggle with Europe's Deep Establishment.* London: Bodley Head.

Wiliarty, Sarah E. 2010. *The CDU and the Politics of Gender in Germany: Bringing Women to the Party*. Cambridge: Cambridge University Press.

IDEATIONAL DIFFERENCES BETWEEN ITALIAN AND GERMAN GOVERNMENTS DURING THE CRISIS

Federico Bruno
University of Milan

1. Introduction

In this contribution, based upon secondary literature, I will review the ideational approaches to the Euro crisis of the Italian and of the German governments. In Section 2, I will show how ideational factors contributed to the making of the Eurozone. In Sections 3 and 4, I account for the role of ideas during the Euro crisis respectively in Italy and Germany. In Section 5, I conclude by comparing the role, the content and the function of these ideas in the two countries.

2. Ideational factors in the making of the Euro

The roots of the Euro crisis are to be sought in the asymmetrical design that has characterised the Economic and Monetary Union (EMU) since its inception (Hall 2012, 2014)where do the roots of the crisis lie, how can the response to the crisis be explained, and what are its implications for European integration? It explores how prevailing economic doctrines con-ditioned the institutional shape of the single currency and locates the roots of the crisis in an institutional asymmetry grounded in national varieties of capit-alism, which saw political economies organised to operate export-led growth models joined to others accustomed to demand-led growth. The response to the crisis is reviewed and explained in terms of limitations in European insti-tutions, divergent economic doctrines and the boundaries of European solidarity. Proposed solutions to the crisis based on deflation or reflation are assessed from a varieties of capitalism perspective and the implications for European integration reviewed. For the past three years, Europe has been mesmerised by the Euro crisis, namely the struggle to resolve the debt problems facing Greece, Ireland, Italy, Portugal and Spain (the GIIPS. In its early stage, economists were already warning that the Eurozone did not constitute an "optimal currency area" and that it would have been subject to asymmetric supply and demand shocks. However, other kinds of evaluations prevailed. The Euro arose as a Franco-German political project: Germany accepted to give up its monetary sovereignty in exchange for a French agreement on its re-unification, whereas France aimed to tame the power of the *Bundesbank* by establishing a European central bank (Hall 2012, 356). The other Member States had interests in joining the monetary union, too. The Northern countries could benefit from the fixed internal exchange rate – which prevented their Southern competitors from competitive devaluation – and from a low external exchange rate. The Southern countries, in turn, would have enjoyed lowered interest rates to finance their public spending, and the possibility of imposing some wage discipline; however, in exchange for this, they had to give up the instrument of competitive devaluations, which represented one of the pillars of their growth model (Ibid., pp. 358-60).

Political and immediate economic interests, however, under-determine the reasons why the single currency was made possible. In order to grasp them fully, we should also account for ideational factors. At the European level, the rise of the monetarist paradigm in the 1980s, caused by the unsuitability of Keynesian policies to deal with stagflation, played a key role (McNamara 1999). Monetarist views shaped the institutions of the EMU: a rule-based monetary-policy targeted on inflation in the hands of an independent central bank, and a fiscal policy in the hands of the Member States. Furthermore, monetarist ideas entailed that supply-side and structural reforms would constitute the one-size-fits-all formula to secure competitiveness in the whole Eurozone (Hall 2012, 356-57).

Ideas played a crucial role in the making of the Euro even at national level. In Italy, the position of the Italian government during the integration process was shaped by the interplay of economic ideas and foreign policy beliefs. Economic and foreign policy ideas were, on occasion, consonant in fostering the integration process, as in the case of the negotiation of the Maastricht Treaty in 1990-1992; other times, the policy imperative of remaining at the heart of European integration prevailed over more sceptical economic considerations, as in the last phase of the EMU in 1999 (Quaglia 2004).

In Germany, the position of the government on the EMU was characterised by a tension between ordoliberalism, represented by Hans Tietmeyer and by the *Bundesbank*, and Europeanism, embodied by Chancellor Helmut Kohl and by his vision of a "community of stability" (Dyson 1998, 39). To be sure, Kohl's vision was not antagonistic to ordoliberalism; on the contrary, being "based on strict fiscal discipline and economic convergence" (Ibid., p. 40), it overlapped it. The ordoliberal features of Kohl's vision stemmed both from his convictions and from the need to secure the support of the *Bundesbank* and of the finance ministry. However, Kohl's position was also motivated by his intimate Europeanism and by his commitment for a Western and European Germany (Ibid., p. 39). During the negotiations, Kohl's Europeanism offered historical and political legitimation to the EMU (Ibid., p. 61), whereas the ordoliberal ideas represented powerful ideational resources. First, they offered the theoretical basis from which the German proposals were derived; second, they limited the win-set of acceptable outcomes for the German government, therefore strengthening its position in the negotiations.

It is worth noting that, outside of the core executive, the ordoliberal camp was split into two, respectively against and in favour of the EMU. The manifesto entitled *Die währungspolitischen Beschlüsse von Maastricht: Eine Gefahrfür Europa* ("The Monetary Policy Decision of Maastricht: A Threat for Europe"), signed in June 1992 by 62 economists (including the distinguished ordoliberal economist Herbert Giersch) and published on the *Frankfurter Allgemeine Zeitung*, concisely represented the former faction: it claimed that the political economies of the European states were still too different for the establishment of a common currency. In turn, the *Ordnungspolitisches Plädoyer* by Olaf Sievert (1993), Giersch's student, represented the pro-EMU faction of the ordoliberal camp. In his article, published in September 1992 in the same newspaper, Sievert claimed that the monetary discipline of the EMU would have secured the ordoliberal principles of stability of monetary policy, and of responsibility. This division within the ordoliberal camp was to re-emerge during the Euro crisis.

For the first years, the EMU seemed to work smoothly: the Northern countries were institutionally well-equipped for the architecture of the monetary union, and started developing huge surpluses. In the meanwhile, the Southern economies, despite having lost the possibility of competitive devaluation, benefited from low interest rates and from the flows of money deriving from their Northern partners' surpluses (Hall 2012, 360). But, as always happens, the honeymoon was destined to end: the Euro crisis made the structural flaws of the Eurozone evident, and called for its reform.

3. Italy: From Berlusconi's Opportunism to Monti's Pragmatic Europeanism

When the crisis broke out in autumn 2008, Italy was not immediately hit: this allowed Prime Minister Silvio Berlusconi to downplay the impact of the crisis, and focus on domestic issues (Jones 2017, 2). At this stage, he claimed that the crisis was a problem of other European states, not Italy's. The situation worsened in Summer 2011, as difficulties in the negotiation of the second Greek bailout programme and a second round of the stress test of the European Banking Association raised concerns about the stability of the Eurozone: investors started losing confidence in the Italian bond market, and the early counter-measures adopted by Berlusconi during the summer did not calm the markets. Since the difficulties in re-financing the Italian debt threatened the stability of the whole Eurozone, the ECB started to buy Italian bonds and urged the government, in exchange, to adopt measures (such as a reform of the pension system) to secure debt sustainability on the long term.

Berlusconi's leadership proved to be inadequate to deal with the crisis. His parliamentary majority was divided, as the *Lega Nord* refused to accept any measure involving pensions, and he came into conflict with his powerful Minister of Finance, Giulio Tremonti. The internal divisions both within the executive and its parliamentary majority led to ineffective and tardy measures. Berlusconi lost credibility in Europe (as testified by Angela Merkel's and Nicolas Sarkozy's chuckles after a question about Berlusconi during a press conference) and in the markets (rating agency Standard & Poor's lowered the rank of Italian bonds from A+ to A). Eventually, he decided to resign, and President Giorgio Napolitano appointed Mario Monti as the new Prime Minister in November 2011 (see Schmidt and Gualmini 2013).

The case of the Fiscal Compact (FC), accurately described by Moschella (2017), shows the role of ideational factors in Monti's government. From a mere economic perspective, the decision of the government to adhere to the FC was puzzling, as it clearly penalised Italy, and offered no guarantees of success (pp. 208-10). Furthermore, despite being popularly remembered as a zealot of austerity, Monti and his ministers constantly asserted that fiscal discipline did not represent the best way to address Italy's long-term problems, and that they would have prioritised growth-oriented measures, instead. Instead, the government abided to the austerity rules because it feared adverse market reactions: the perception of Italy's vulnerability "nurtured a 'there is no alternative' mind-set that dominated the policy-makers' thinking and led them not to even conceive of the possibility of looking for alternative courses of action" (p. 217).

Along with the fear of punishment, three other mechanisms determined the stance of the government: institutional constraints, a pro-European attitude, and a large domestic win-set. The institutional constraints worked in two ways. On the one hand, the incomplete architecture of the EMU did not provide any automatic insurance for countries hit by the crisis, thus amplifying the influence of market pressures: the government felt obliged to adhere to the FC, if it wanted to obtain a European insurance against the crisis. On the other, the FC was in line with the framework set by previous fiscal rules (for instance, the Stability and Growth Pact), and opposing the FC would have not put/called into question the overall framework. The pro-European attitude of the government led it not only to defend the national interest, but also to safeguard the European integration process: the signature of the FC was a demonstration of the Italian commitment to the European project. Finally, the parties in the Parliament broadly supported the FC, in line with their Europeanist attitude – even if in a reactive, rather than proactive, way. This prevented the government from evaluating the opportunity of not signing the Treaty (pp. 218-21).

4. Germany: between pragmatic Europeanism and ordoliberalism

Unlike Italy, the crisis hit Germany from the beginning. As mentioned above, the EMU architecture enabled Northern economies to pile up important surpluses. In investing this money, the German banking sector let down its conservative, risk-averse reputation and became embroiled in the financial bubble (Dyson 2010, p. 400): important commercial banks (the most famous case was the *IKB*) and the state-owned *Landesbanken* needed to be bailed-out by the government. However, when the financial crisis turned into the sovereign-debt crisis that menaced the Eurozone, Germany was out of danger, and, unlike the Southern economies, did not face an immediate threat. Its immediate interests were, on the one hand, to secure the Eurozone (not least because of the exposure of its banks in the Southern countries), and, on the other, to shift away the costs of rescuing the Eurozone. The fact that the immediate consequences of the crisis were much heavier for the Southern countries than for their Northern counterparts increased Germany's power during the negotiations (see Schimmelfennig 2015).

There has been a huge debate on the impact of ideas on Germany's behaviour during the Euro crisis. Some claim that the German government strictly adhered to the principles of the ordoliberal ideology, whereas, according to others, it was driven by self-interest and pragmatism (Hien and Joerges 2017, collected several contributions on this topic). Ordoliberalism and pragmatism should not be considered as being mutually excluding: within the German government, we could find both more pragmatist (such as Chancellor Merkel) and more ordoliberal (such as the director of *Bundesbank*, Jens Weidmann, or Finance Minister, Wolfgang Schäuble) leaders. The German position seems therefore to have been shaped by a tension between ordoliberalism and pragmatism. The ordoliberalism of the German executive, however, was not a strict version of the theory, but a more superficial, crude adaptation of it (see Hien and Joerges 2018; and Wyplosz 2017).

The German political discourse during the crisis was dominated by ordoliberal concepts: stability, responsibility, and competitiveness. The more ordoliberal leaders stressed the *Haftungsprinzip* (principle of responsibility): the rescue of the Eurozone should not have entailed a mutualisation of the sovereign debt, and the Member States should have remained responsible for their own public finances. In turn, the more pragmatic leaders justified, upon the basis of the stability principle, those policies that diverged from the ordoliberal orthodoxy, such as the bail-out packages for indebted countries, or the establishment of the European Stability Mechanism (ESM).

Ordoliberal ideas played, therefore, a double role. On the one hand, together with the immediate interests derived from its status of Northern, export-led political economy, they shaped the German strategy for the reform of the Eurozone. The interplay between stability, responsibility and competitiveness resulted in an approach characterised by intergovernmentalism and market discipline. Intergovernmentalism was seen as the best guarantee to prevent any mutualisation of the debt; market discipline, in turn, was seen as the driving force for the reforms, necessary to overcome the lack of competitiveness that afflicted the Southern economies, and this constituted, according to the ordoliberal (and German) account, the real cause of the Euro crisis (see Matthijs and McNamara 2015).

On the other, ordoliberal ideas represented a constraint to the German executive (see Jamet, Mussler, and De Corte 2011, 64). Even the pragmatist leaders had to pay lip-service and to justify their policies through ordoliberal principles: this is what Chancellor Merkel did in 2011 in Freiburg, the birthplace of ordoliberalism, when she defended her European strategy, and what Klaus Regling, the chief of the ESM, did in 2017 in the same city, when he claimed the consistency of the ESM with the principles of *Ordnungspolitik*. Moreover, beyond the German executive, the remarks of many influential ordoliberal economists (such as Hans-Werner Sinn), highly critical towards the European strategy of Merkel's governments, posed a further constraint on the government. Eventually, some of these economists took part in the foundation of the Euro-sceptic party *Alternative für Deutschland*. Once again, the ordoliberal camp was split into two(see, also, Jacoby 2014).

5. Conclusions

During the Euro crisis, in both Italy and Germany, we could witness the resurfacing of the ideational dynamics that had characterised the previous stage of the monetary integration. In Italy, the committed Europeanism of the Monti government led Italy to accept the German-inspired reforms of the Eurozone, although they penalised it as a demand-led political economy. In Germany, the tension between a pragmatist Europeanism and ordoliberalism – that already characterised Kohl's chancellorship – shaped the European strategy of the government. In the aftermath of the crisis, however, these ideas showed their weaknesses. On the one hand, the last elections in Italy (2018) are the perfect representation of the end of the so-called "permissive consensus": by now, it has become very hard – if not impossible – for a government to justify its choice only relying on Europeanism. On the other, the fact that the Eurozone is still considered to be in danger despite the reforms undertaken during the crisis shows all the limits of the German approach.

Italian and German ideas during the crisis were substantively different. Italian Europeanism translated into a preference for a supranational approach, while the stress on the need to foster growth (that characterised even the Monti government, despite its commitment to fiscal discipline) reflected a preference on market-correcting policies. In turn, the German commitment to ordoliberal principles translated into an intergovernmental, market-discipline-oriented approach, suited to secure responsibility and competitiveness. It is worth noting that the German approach is consistent with the monetarist founding of the EMU and with a certain national egoism, whereas the Italian one requires a high solidarity among European countries, which, to date, does not exist. In this sense, borrowing the Varieties-of-Capitalism jargon, we could speak of a "comparative advantage" of German ideas over the Italian ones.

Finally, the ideational attitudes of the governments had different effects in Italy and in Germany. In Italy, Berlusconi's opportunistic leadership prevented the government from setting up an effective and timely strategy against the crisis. The Europeanist attitude of the Italian parliament during Monti's government, in turn, widened the win-set of acceptable reforms: while this secured the participation of the Italian government in the reform process, it also diminished its negotiating power in the bargaining (on the relation between bargaining power and size of the win-set, see Putnam 1988, p. 440). In Germany, quite the opposite happened: not only did ordoliberal ideas provide a set of principles to articulate the reform of the Eurozone, but they also dramatically restricted the win-set, thus improving the government's bargaining power.

Bibliography

Dyson, Kenneth. 1998. "Chancellor Kohl as Strategic Leader: The Case of Economic and Monetary Union." *German Politics* 7(1): 37-63.

———. 2010. "In the Shifting Shadows of Crisis: Pivot Points, Crisis Attribution, and Macro-Economic Policies under Grand Coalition." *German Politics* 19(3-4): 393-415.

Hall, Peter A. 2012. "The Economics and Politics of the Euro Crisis." *German Politics* 21(4): 355-71.

———. 2014. "Varieties of Capitalism and the Euro Crisis." *West European Politics* 37(6): 1223-43.

Hien, Josef, and Christian Joerges, eds. 2017. *Ordoliberalism, Law and the Rule of Economics*. Oxford-Portland OR: Hart Publishing.

———. 2018. "Dead Man Walking? Current European Interest in the Ordoliberal Tradition." *European Law Journal*.

Jacoby, Wade. 2014. "The Politics of the Eurozone Crisis: Two Puzzles behind the German Consensus." *German Politics and Society* 32(2): 70-85.

Jamet, Jean-François, Werner Mussler, and Stefaan De Corte. 2011. "Eu Economic Governance: The French and German Views." *European View* 10(2): 259-60.

Jones, Erik. 2017. "Relations with Europe." *Italian Politics* 32(1).

Matthijs, Matthias, and Kathleen McNamara. 2015. "The Euro Crisis' Theory Effect: Northern Saints, Southern Sinners, and the Demise of the Eurobond." *Journal of European Integration* 37(2): 229-45.

McNamara, Kathleen. 1999. *The Currency of Ideas*. Ithaca NY: Cornell University Press.

Moschella, Manuela. 2017. "Italy and the Fiscal Compact: Why Does a Country Commit to Permanent Austerity?", *Rivista Italiana di Scienza Politica* 47(2): 205-25.

Putnam, Robert D. 1988. "Diplomacy and Domestic Politics: The Logic of Two-Level Games." *International Organization* 42(03): 427.

Quaglia, Lucia. 2004. "Italy's Policy towards European Monetary Integration: Bringing Ideas Back In?" *Journal of European Public Policy* 11(6): 1096-1111.

Schimmelfennig, Frank. 2015. "Liberal Intergovernmentalism and the Euro Area Crisis." *Journal of European Public Policy* 22(2): 177-95.

Schmidt, Vivien, and Elisabetta Gualmini. 2013. "The Political Sources of Italy's Economic Problems: Between Opportunistic Political Leadership and Pragmatic, Technocratic Leadership." *Comparative European Politics* 11(3): 360-82.

Sievert, Olaf. 1993. "Geld, Das Man Nicht Selbst Herstellen Kann - Ein Ordnungspolitisches Plädoyer Für Die Europäische Währungsunion." In *Währungsunion Oder Währungschaos*, eds. Peter Bofinger, Stefan Collignon, and Ernst-Moritz Lipp. Gabler.

Wyplosz, Charles. 2017. "The Euro and Ordoliberalism." In *Ordoliberalism: A German Oddity?*, eds. Thorsten Beck and Hans-Helmut Kotz. CEPR Press.

A CULTURAL POLITICAL ECONOMY APPROACH TO THE EUROPEAN CRISIS

Josef Hien
University of Milan

Introduction

In 2011, a Greek minister wrote in a newspaper about the *Troika* that "we are dealing here with idiots and Protestants, hence there is no solution" (cited in Makrides, 2015, p. 373). Looking at the split between the crisis and non-crisis countries, it seems, at first glance, that the crisis countries are all Catholic or Orthodox, while the non-crisis countries overwhelmingly share a Protestant background. The cultural and ethical rooting of German ordoliberalism and the reliance of German politicians on the concept helps German politicians to approach the crisis as a morality tale of Northern saints and Southern sinners (Hien 2017). Do we witness a new Thirty Years' War in Europe? Not quite; the ideational and cultural split between Catholic/Orthodox and Protestant countries also overlaps with the material interest-based fault lines between creditor- and debtor-countries or the institutional differences between those countries that generate economic demand primarily through exports or those that do so through internal demand. So far, the European crisis has been analysed through the lenses of the Variety of Capitalism concept, the growth model framework, or ideational accounts. These three accounts have generally been applied in isolation from one another. There has been little room for cross-fertilisation, arguably, due to the different points of epistemological departure that emphasise either institutional rational efficiency, the material driving forces, or the constructivist motives for the political economies during the crisis. This paper adopts the concept of cultural political economy, modifies it, and applies it to the North-South conflict.

Cultural political economy integrates institutional, material and ideational viewpoints, and adopts a decisive neo-Weberian historical evolutionary perspective to show how they have co-evolved and re-enforced one another since the 1950s, creating the discrepancies and irritations that we witness today between the Northern and Southern Member States. The contribution exemplifies the cultural political economy approach to the crisis with the German-Italian discrepancies that have been growing slowly since the 1950s, but have accelerated during the past 30 years. While in the 1950s and 1960s both economies started from similar premises, they are worlds apart today.

While cultural political economy has been promoted for a decade and a half, this approach, to date, has not come centre-stage in the European discussion on the crisis. The paper argues that this is due to the fact that, while, in essence, these approaches are on the right track towards a more encompassing post-disciplinary understanding, they have not left their foundational basis in rational-efficiency-centred institutionalism or in material Marxism. The paper proposes a new starting-point for cultural political economy anchored in a Weberian framework that is ontological and epistemological better suited to integrate institutional, material and ideational explanations and set them in an evolutionary context over time.

After an introduction to the concept of cultural political economy (Section 1), the paper lays out the socio-economic points of divergence between the Catholic and the Protestant thought as they developed from the 1930s onwards in Germany and Italy (Section 2). It also explores how much of this socio-economic thought found its way into the institutional reform of both countries in the 1950s and 1960s, and traces the evolution of the two doctrines and the institutions which they informed to the present day (Section 3).

1. The Dominant Approaches within Political Economy to the Crisis

The "Varieties of Capitalism" approach has dominated comparative political economy for almost 20 years (Hall and Soskice 2001). Putting the firm, business networks, and their interaction with the (welfare) state at the centre of the analysis, "Varieties of Capitalism" scholars argue that market economies cluster into co-ordinated and liberal market economies. Co-ordinated market economies rely on diversified quality production. They orient their production towards market niches where quality and customisation are important. A state-run vocational-training system ensures the supply of skilled labour, and high employment protection creates incentives to invest in specific skills. The system is co-ordinated through strong employer and employee organisations. In the original account of the Varieties of Capitalism and in most of the follow-up literature, Italy and Germany are classified as co-ordinated market economies.

During the 2000s, the Varieties of Capitalism approach reigned supreme. The introductory chapter of Hall and Soskice's Varieties of Capitalism book has been cited according to *google scholar* 11,522 times. Chapters such as Estevez-Abe et al. (2001) on social protection and the formation of skills have led to paradigmatic changes in entire sub-fields of political-economy (e.g., welfare state studies). However, the theory has been seriously challenged through the shockwaves that the financial crisis sent through the European co-ordinated market economies (Hall 2014; Johnston and Regan 2015). The crisis drastically showcased a strong "variety within the variety" of European co-ordinated market economies between North, South, and Central and Eastern Europe (Höppner and Lutter 2017; Armingeon, Guthmann and Weisstanner 2015; Perez and Matsaganis 2018). Accounts started to re-classify countries, and Italy is now presented as a "mixed-model". The euro is the *bête noire* for researchers who emphasise the "within variety" of European political economies. The political economies of the countries that have adopted the euro are simply too heterogeneous to be subsumed under a single currency.

Authors such as Wolfgang Streeck, Lucio Baccaro, Johannes Lindvall and Stefan Svallfors had already criticised the "Varieties of Capitalism" scholarship before the crisis for not accounting for the far-reaching processes of neo-liberalisation that all of these national economies have undergone since the 1990s. The decline in union density and corporatist arrangements, as well as wage dispersion and the dualisation of the labour markets, eroded the equilibrium that the co-ordinated market economies had found before the 1980s (Streeck 2009; Baccaro and Howell 2011; Lindvall and Rothstein 2006; Lindvall 2006; Svallfors 2016; Svallfors and Tyllström 2018). The different ways in which these liberalisations were executed contributed to significant shifts in the configuration of GDP growth in both Germany and Italy. This is the gist of the growth model perspective. It emphasises that, in the 1990s, Germany turned from a growth model that was equilibrated between domestic demand and exports, to an export-led economy. The share of exports in German GDP growth doubled in the 1990s and 2000s (Baccaro and Pontusson 2016, 189). To support the export competitiveness of the price-sensitive German manufacturing goods, domestic demand (household consumption) was suppressed through wage depression. Unions in the manufacturing sector agreed to wage restraints and the rest of the labour market was de-regulated (Baccaro and Benassi 2017; Hassel 2017).

For the proponents of the Growth model perspective and the scholars of the preceding liberalisation, the German model runs at the expense of the Southern political economies of the Eurozone, which are geared towards demand-led growth. The proposed and enforced solutions of Germany to the Euro-crisis also have to be seen in this light. The interests of the German export coalition are the underlying motives of the austerity policies that the German government made the pre-condition for loans and rescue packages. These austerity measures risk being counter-productive because they stifle domestic demand, which has traditionally been the key driver of growth in Southern European economies. In the literature on the European crisis, this features as a cleavage dividing Northern and Southern Europe between importer *versus* exporter states. The cleavage sometimes also appears as a cleavage between debtor *versus* creditor states (Dyson 2014).

A third explanatory framework for the Eurocrisis is based upon ideas. The ideational turn in comparative political economy has demonstrated the power of economic ideas in politics (Berman 1998, 2006; Blyth 2003; Carstensen and Schmidt 2016). During the euro crisis, idiosyncratic national economic ideologies such as German ordoliberalism and French *dirigisme* experienced an unexpected explosion of public and scholarly interest because they link expert ideas with a common national tradition of how the economy should be run (*Economist* 2015; *Financial Times* 2014; Blyth 2013; Scharpf 2016; Hien and Joerges 2017; 2018; Needergard and Snaith 2015; Amable 2017). In particular, the clash between French economic ideas and their German counterparts has been blamed for the prolonged stalemate between the countries on what is the right crisis policy (Brunnermeier, James and Landau 2016).

The "Varieties of Capitalism", the growth model perspective, and the ideational accounts exist largely independently from one another. The reason for this can be found in the different epistemological points of departure. The "Varieties of Capitalism" model is anchored in a rational-efficiency-oriented institutionalism. The growth model perspective relies ultimately on an interest coalition between segments of capital and labour in the export sector. And the ideational approaches rely on the power of ideologies to serve as blueprints for socio-economic actions and institution-building. A severe downside to all three is that they do not incorporate an explicit historical evolutionary perspective. Moreover, they are largely apolitical, since they leave electoral considerations and the anchoring of different economic strategies in the population by the wayside.

Arguably, a fourth explanatory strand for the euro crisis also exists, one which, to date, has lived in the shadow of the three other approaches. Here, historical evolutionary pathways are at the centre of attention, allowing for a more integrative epistemic perspective than the other three approaches: economic historians have developed a notion that has so far not been picked up much in the mainstream of political economy: the idea of different economic cultures (Abelshauser 2003; Abelshauser, Gilgen and Leutzsch 2013). It brings a historical-evolutionary perspective that tracks the embeddedness of socio-economic actors in national cultures, traditions, and prevalent economic ideas within a nation-state (Dyson 2017). Here, the crucial role of "meaning making" to reduce complexity in the economy is brought out. The concept of cultural political economy or economic cultures highlights the importance and instrumental use of shared imaginaries for contemporary economic actors (Jessop 2010; Jessop and Sum 2017; Best and Paterson 2015; Esch and De Jong 2017). While the economic cultures notion of the Bielefeld historians around Abelshauser is based upon the rational efficiency accounts of Douglass North, the notion of cultural political economy advanced by Ngai-Ling Sum and Bob Jessop is rooted in Marx and Gramsci. Jessop and Sum's cultural political economy promises a "dialectic of discursivity and materiality" (Jessop 2004, 164) but the initial vow to "produce a Marxist-inflected 'cultural political economy'" (Jessop and Sum 2001: 92) makes this difficult. Like the cultural economy concept of the Bielefeld historians, Sum and Jessop want to present an integrative account, but both approaches still emphasise material and institutional conditions over ideational factors. Ideas are regarded as tools to solve collective-action problems in the tradition of North, or as fig leaves to manipulate and veil the true material conditions to establish hegemony in a Gramscian sense (Jessop and Sum 2001: 94-95) making one wonder where the culture in these two cultural political economy approaches actually resides. It is certainly understandable that scholars that have worked within the Marxist paradigm for most of their careers will not give it up even when trying to stretch its boundaries towards a "post-disciplinary" (Jessop and Sum 2001: 89) perspective. But it is fair to ask them why the "anti-cultural" (Smith 2001: 6) theorist *par excellence*, Karl Marx, is chosen as the starting-point for the formulation of this post-disciplinary approach. Might not Max Weber, for whom culture had been the starting-point of any socio-economic analysis, be more fruitful as a point of departure?

Culture, in Weber's work, is the "most fundamental category" (Swedberg and Agevall 2005:56) and "culture is a finite segment on which human beings confer meaning and significance" (Weber 1904: 81). "Weber emphasizes to study capitalism not only as an economic phenomenon but also as a cultural phenomenon" (Swedberg and Agevall 2005: 57). Moreover, for Weber, social science was about "*Verstehen*", about finding out about the "subjective meanings". Social science should not emulate the positivism of the physical sciences but should instead be a "*Geisteswissenschaft*", literally, a "science of the spirit". Therefore, social analysis and, especially, the study of political economy, should be a "science which is concerned with the subjective meaning of action", in which "explanation requires a grasp of the complex of meaning" (Weber 1968: 9). Hence, Weber's sociology is about the analysis of meaning-making and shared imaginaries which speak very much to the core concept of shared imaginaries and meaning-making that not only Sum and Jessop but also the Bielefeld School put centre-stage in their accounts. Insightful in this respect is a quick look at the subtitle of Weber's *opus* "Economy and Society", which reads: "An Outline of Interpretative Sociology". There is also an emerging trend towards neo-weberian approaches to the EU in general (Ferrera 2017, 2018). But these are only perceived as manipulating themes in the existing cultural political economy approaches due to their rooting in Marxist materialism. Hence, it is not surprising that the ideational components of Jessop and Sum's analysis have been heavily criticised for an *ad hoc* evoking of cultural themes when their explanatory toolkit is exhausted (Staricco 2015). Weber would offer a much more solid fundament to arrive at an "organic synthesis" of the "soft" and "hard" (Sum and Jessop 2013: 23; Staricco 2015: 9) parts of cultural political economy without subscribing fully to total constructivism or total materialism.

For the rest of social science, culture as an explanatory variable is (often not without foundation) accused of being a residual category that gets evoked when all other explanations fail (Staricco 2017). However, the strength of a cultural political economy that is based upon Weber, is that it can integrate the trichotomy between material, ideational and institutional accounts that currently divides the study of political economy and the euro crisis. As in Weber's famous switchmen metaphor, it is not interests, ideas or institutions that determine action, but all three together. When they all point into the same direction, they form a self-reinforcing compound, an amalgam, that is very hard to overcome or to break up. This is exactly the case in the Eurozone crisis, and the following will show how ideas, interests and institutions re-inforced themselves in an evolutionary process over time, and came to determine today's position of crisis and non-crisis countries.

2. Catholic and Protestants Reactions in Socio-economic Concepts to the Crisis of 1930.

Language and religion are two major carriers of culture. This paper focuses on religion, and traces how the different socio-economic doctrines of religious institutions left their imprint on post-WWII ideologies and institutions. Our story starts with the world economic crisis of the 1930s, which re-formed the dominant strands of socio-economic thought in Europe. The ordoliberal project as it evolved in Germany from the late 1920s onwards is the reaction of Protestant social thought to the upheavals of Weimar that cumulated in the World Economic Crisis of 1929.

Walter Eucken, the founding father of the Ordoliberal School, had already commented, in the

1930s, that the loosening ties to the churches had facilitated the people turning to secular-isms in the Weimar period and that "religion had increasingly lost the power to provide individuals' lives, and thus also their economic activity, a context of meaning" (Eucken 1932). Numerous "explicitly normative-anthropological deliberations" of the ordoliberals were derived from Protestantism, and "the strong affinity of a liberal ethos [was] largely influenced by Protestantism" (Jähnichen 2010: 11, 13).

The "deep Protestant grammar" (Manow 2001) of ordoliberalism was no accident. All the key figures of the first ordoliberal generation were Protestants. Eucken wrote in a 1942 letter to Alexander Rüstow: "I could neither live nor work if I did not believe that God exists." (Lenel 1991, 12) The ordoliberal project that developed in the late 1930s and early 1940s in the Freiburg circles was therefore a genuinely Protestant attempt to design an economic order. The project was meant as an antidote to the social-Catholic, the Keynesian-welfare-state, and the neoclassical Austrian-Anglo-Saxon approaches. The key figure was the Protestant theologian Dietrich Bonhoeffer/Bonhöffer. Between 1938 and 1944, he brought Protestant theologians (Otto Dibelius, Constantin von Dietze), Protestant economists (Walter Eucken, Leonard Miksch, Adolf Lampe), Protestant jurists (Franz Böhm, Hans Großmann-Doerth), and Protestant historians (Gerhard Ritter) together in the *Bonhoeffer Kreis* and the *Arbeitsgemeinschaft Erwin von Beckerath*, the two most important ordoliberal circles in Freiburg (Goldschmidt 1997).

The *Freiburger Denkschrift*, which originated from these circles and was to be the blueprint for post-war re-construction, laid out the first coherent Protestant economic and social ethics. Its underlying values clearly differentiate ordoliberalism from nineteenth century *laissez faire* liberalism, and the post-Keynesian Anglo-Saxon neoliberalism, which has become the dominant ideational paradigm since the late 1970s. Although self-interest induces people to give their best, it can also bring them to manipulate competition to their own benefit. Just as in Protestantism, ordoliberalism considers people to be "neither angels nor devils" (Dietze 1947, 26), but rather "justified and sinners at the same time; that is why it is decisive to place them within an order that disciplines the *peccator*" (Reuter 2010: 3). In his work, Eucken seeks a compromise between "a Calvinist theocracy with its near identity of church and state and the Lutheran two-kingdoms doctrine with its separation of the spiritual and secular spheres" (Petersen 2008, 23). His concepts mirror Bonhoeffer's "authoritative-paternalistic [...] thinking" that "trusts an order and authority based on law and responsibility more than individual freedom" (Falcke 2011, 382). Ordoliberalism's notion of society is not paternalistic, even though the state's capability to provide order is so important to it. The state is supposed to hold back and limit itself to setting the underlying conditions for the social order. Ordoliberals reject social transfer payments as false incentives. Unconditional transfers for reasons of solidarity would, in the end, result in the "total catastrophe for state and society" and make citizens "slaves of the state" (Röpke 1949, 257). Instead, the state should limit itself to ensuring equal opportunity and creating the conditions for helping people to help themselves. This is what sets ordoliberal ideology apart from the Keynesian and Beveridgean welfare-state concept that aims at equality in society, on the one hand, and social-Catholic welfare concepts that emphasise a male-breadwinner-centred corporatist-transfer-heavy welfare state, on the other.

Eucken saw social policy as something that would, in the long run, kill all individual self-responsibility. He emphasised that it would "foster collectivization, create coercion and dependency that would diminish self-responsibility and endanger the unfolding of the powers which strive in the individual human being for fulfillment" (Eucken 1949, 113). Müller-Armack, who later became State Secretary in the Ministry of the Economy, opined, as early as 1947, that, in any case, "the social policy results […] have been quite poor" (Müller-Armack 1947, 130). Kaufmann notes that, for Ludwig Erhard, later to become Minister of the Economy and the single most prominent Christian Democratic exponent of ordoliberalism, "economic policy was the best social policy". (cited in Kaufmann 2003, 131).

Due to their Protestant religiosity, the ordoliberals searched for a political home in the Christian Democratic Party (not in the Liberal Party). Franz Böhm was Minister in Hessen and became member of the Federal Parliament, Ludwig Erhard was Minister and became later Chancellor and Alfred Müller-Armack State Secretary. However, these Protestant ordoliberals faced a mighty opponent within the Christian Democratic party: the social Catholic faction. At the same time as the ordoliberals, and also as a reaction to the crisis of the late 1920s, the social Catholics had developed socio-economic ideas that ran, in most points, exactly the opposite from the Protestant ordoliberals. Their ideology was based largely upon the social Encyclical *Quadragesimo Anno*, which, like the *Ordo Manifesto* (1936), had been issued as a response to the world economic crisis which began in 1929.The prime target of criticism in *Quadragesimo Anno* is the current "economic dictatorship" (*Quadragesimo Anno*, 109) brought about by a rampant system of free competition which had led to the "virtual degradation of the majesty of the state" (*Quadragesimo Anno*, 109). According to *Quadragesimo Anno*, "the free market has destroyed itself" (*Quadragesimo Anno*, 109).

The Encyclical stresses that its socioeconomic concept is neither neo-liberal nor socialist, but marks a distinct, Catholic third way. In contrast to socialism, private property remains central, but, unlike neo-liberal conceptions, any private property has to be subject to the increase of the common good. *Quadragesimo Anno* is of the view that "the right order of economic life cannot be left to a free competition of forces" (*Quadragesimo Anno*, 87). The judgment is harsh: "free competition […] clearly cannot direct economic life" as "it cannot curb and rule itself" (*Quadragesimo Anno*, 88). Unrestricted free market competition would be directed by the "evil individualistic spirit" (*Quadragesimo Anno*, 88) spread by "the errors of individualist economic teaching" stemming from a "poisoned spring" (*Quadragesimo Anno*, 88). Instead, the papal letter puts forward that economic life must again be "subject to and governed by a true and effective directing principle" (*Quadragesimo Anno*, 88).

Quadragesimo Anno marks a new step in Catholic social thinking. Catholic social thinking is now no longer limited to social welfare institutions (as it still was in *Rerum Novarum*) that engage in repair work after capitalism has brought social dislocation and hardship by destroying the old social order. Instead, its plea for corporatism makes a step towards actively shaping capitalism. This is new and novel thinking, different from the Vogelsangian pleas to go back to a medieval estate-based social order, even though it embodies these ideals to a certain extent. The difference is that it fuses them with a decisive Christian Democratic plea to democratise the capitalist system by arguing for the centrality of associations. The Encyclical promotes a specific type of neo-corporatism in which the state only intervenes as a last resort (Invernizzi-Accetti 2019). Christian Socialism emphasises the importance of collective organisation for the common good (*Quadragesimo Anno*, 85). Employers and employees should be organised in mutual associations depending on the sector of activity. These mutual associations should grant a stable and smooth running of the economy, which would avoid strikes, on the one hand, and wage deprivation, on the other. The Encyclical notes that "both workers and employers with united strength and counsel can overcome the difficulties and obstacles and let a wise provision on the part of the public authority aid them". (*Quadragesimo Anno*, 73). Wages should be negotiated fairly in bi-partite negotiations, and only in cases of stalemate or dissatisfaction should the state intervene. Workers should be protected by ample worker-protection legislation that would regulate maximum work hours as well as women in work and child labour. Co-determination should reduce industrial conflict and give the employed a say in the administration of the firm. In general, “the riches that economic-social developments constantly increase ought to be so distributed among individual persons and classes that the common advantage of all, which Leo XIII had praised, will be safeguarded”. (*Quadragesimo Anno*, 75). The prime aim of the economy is to increase the aggregate wealth, instead of individual riches. This shared wealth should be generated not only through the payment of a “just wage” and the regulation of working hours and conditions, but also through a system of re-distribution. Therefore, “we must strive that at least in the future the abundant fruits of production will accrue equitably to those who are rich and will be distributed in ample sufficiency among the workers”. (*Quadragesimo Anno*, 61). With its emphasis on corporatist organisation of socio-economic relations and the transfer-heavy male-breadwinner model, the Encyclical reads like an anti-manifesto to Protestant ordoliberal claims.

Thus, ordoliberalism distinguished itself clearly from Catholic social ethics, and this is largely due to the different (Hien 2012) conceptions of the human being that Catholics and Protestants loaded into Social Catholicism and ordoliberalism. Catholicism assumes that individuals are not equipped with the same intellectual, moral, and physical capabilities. For this reason, ensuring fair and equal starting-conditions and opportunities (level playing-field), as ordoliberals do, would not suffice for Catholic social ethics; instead, society must also guarantee a certain amount of re-distribution (*Quadragesimo Anno*, 75).

The mutual distrust between both camps was tangible up into the 1960s. In 1963, the leading figures of German Catholic social teaching (von Nell-Breuning, Gundlach) and ordoliberalism (Röpke and Rüstow) met secretly in a hotel in Augsburg to discuss whether the social Catholics could be won over for the term “social market economy” that the ordoliberal Alfred Müller-Armack had coined. One of the participants later commented that this was an extremely delicate meeting (Emunds 2010: 1-2). It had to be kept secret because of widespread scepticism in both camps towards collaboration. The Catholics were later reported to have rejected both the term and the concept of a social market economy, since it contained too much ordoliberal Protestant thinking. Both churches were still very far from their (cautious) ecumenical moves of the 1970s, despite having joined forces in a single party (the CDU) for the first time in German history.

The ordoliberals joined the Christian Democratic party for electoral considerations. With German partition, the denominational balance had shifted to roughly 50 per cent Catholics and 50 per cent Protestants in West-Germany. Since Protestants not only voted Christian Democrat but also Liberal and Social Democrat (but almost all Catholics voted Christian Democrat), they needed the Catholics to form an electoral coalition to get at least some of their points through. However, given the differences in socio-economic ideology, Social Catholics worked in, the early years of the republic, as an effective counterweight to ordoliberal ideas. On the other hand, ordoliberalism also balanced social Catholicism towards a moderate position away from its hardcore corporatist standpoints of the 1930s. Such a moderation effect did not exist in Italy. Here, the mono-confessionalism pampered through the softer version of fascist totalitarianism led to a less clear-cut break with the past and a general easier embracing of corporatist and Social Catholic (even Christian Socialist) ideas (a good example here is Amintore Fanfani).

In contrast to the West-German Christian Democratic CDU, the Italian *Democrazia Cristiana* (DC) was all Catholic. The DC’s founding father Alcide De Gasperi is portrayed by historiography as a pragmatic realist politician (Cau 2009, 431), a governor interested in organising with little or no stake in ideology or doctrine. De Gasperi was partly keen on presenting himself in this way. He said, in preparation of the Christian Democratic Congress in 1949, “He [Giuseppe Dosetti] had been getting ready for this congress for many months … in thoughtful analysis … Unfortunately, I have not had so much time, as I have had to deal with practical tasks and constructive experiences" (cited in Cau 2009, 432). Newer historiographic research shakes this picture, pointing to the early formative experience of De Gasperi and his training as a Catholic sociologist and Catholic militant in Vienna (Pombeni and Nobili Schiera 2009). In his early writings, De Gasperi emphasised the centrality of the Catholic corporatism of the *Quadragesimo Anno* and its connection to the personalist concepts of Emmanuel Mounier and Heinrich Pesch. The independence of organisations was "a natural consequence of personal freedom" since they were "natural organs of civil society" (Cau 2009, 441). While De Gasperi and Konrad Adenauer were similar regarding the compromisability of ideological positions for their political ambitions, the Italian Catholic left was arguably much more to the left than its German counterpart.

To the left of De Gasperi stood the "*professorini*" (young professors) or "*dosseti*ans", who were recruited from a circle of young university researchers around Dossetti – a professor and social philosopher at the Catholic University of Milan. Two other central figures in his faction were Giorgio La Pira, who later became mayor of Florence, and Giuseppe Lazzati, who became rector of the Catholic University of Milan (Masala 2004, 101). Dossetti's social thinking drew heavily on personalism inspired by the French Emmanuel Mounier's or Jacques Maritain's philosophy of Christian Democracy (Müller 86). Like Pesch's and Oswald von Nell-Breuning's personalism in Germany, the emphasis was more on the view that "the human personality unfolds through organic belonging to the successive communities" (La Pira cited in Acanfors 2007, 312). In contrast to De Gasperi's insistence on interclassism and mediation, which bears relics of the conservative Austrian Catholic Vogelsangian thought, it aimed at getting rid of classes all together.

Dossetti's followers had a long-lasting influence on Italian Christian Democracy and Italian postwar institutions. His student Aldo Moro engineered the *compromesso storico*, the first collaboration with the Communist Party in the 1970s, and was subsequently kidnapped and murdered by the *Brigate Rosse*. Amintore Fanfani became prime minister in the 1960s and overhauled the economy in a corporative fashion. Like every strong ideological group, the *Dosseti*ans had a central journal, the *Cronache Sociali*. Its contributions were inspired and impressed by the labour victory in Britain, and by Keynes' and Beveridges' political economic ideas of re-organisation. The first programmatic party manifesto of the DC developed during a series of clandestine meetings that rotated around the homes of several of its founding members during 1942 and the first months of 1943 also bore a strong imprint of the Catholic left. Copies were secretly diffused throughout Italy during the German occupation. The manifesto is signed with one of De Gaspari's pseudonyms, but was the result of extensive collaboration of the wings or factions (*correnti*) of the whole party [the DC] (Masala 2004, 106). The programme incorporated a detailed plan for the future institutional framework of the new Italian state, and also featured prescriptions for industrial relations and a detailed social policy agenda.

The programme tried to walk the typical Christian Democratic line between calls for the nationalisation of key industries and the importance of private entrepreneurship. However, the programme had a strong Christian Socialist leaning inspired through the Encyclical *Quadragnesimo Anno*. Moreover, the existence of the largest communist party outside of the Soviet Union in Italy created a stronger drift of party competition towards left-wing socio-economic issues (Ferrera 1984, 1986). Fighting fire with fire, the Christian Democrats had to propose strong social ideas to curb the influence of the Communist party (PCI). The most remarkable prescription of the programme is for the establishment of two parliamentary chambers, of which one would be elected while the other would serve as a forum for corporatist-interest representation (Manow 2015). This "assembly of the organized interests" (DC 1943, 1) should be "founded foremost on the elected representatives of the organized professions". (DC 1943, 1) This represented an almost word for word incorporation of the provisions of the social encyclical *Quadragesimo Anno* into the Christian Democratic program. The concept was one of a "liberal Christian idea of a free organic collaboration of all means of production" (DC 1943, 2). In line with the provisions of *Quadragesimo Anno*, the State should be confined to a role of "vigilance" (DC 1943, 2) that guarantees the functioning of the neo-corporatist model. Regarding the issue of social security, the program spelled out that "social insurance should be extended, simplified, its organization decentralized and its management put into the hands of the people that it concerned"(DC 1943, 2) reflecting the subsidiarity clauses of *Quadragesimo Anno*. In Germany, such corporatist positions can only be found in the Ahlen programme or manifesto of the CDU, an internal concession to the left-Catholic party wing on the part of Adneauer in the 1940s, which was quickly quashed and replaced by the Protestant liberal conservative *Düsseldorfer Leitsätze* in 1949. Another difference between Italian and German social Catholicism was that the DC could count on the backing of a strong Catholic union movement ("*Gronchi*ans" headed by Giovanni Gronchi, the influential union leader), while, in Germany, the Catholic unions were subsumed under the roof of the *Deutscher Gewerkschaftsbund* and pulled into the orbit of the Social Democrats (Schroeder 1992).

3. The Impact of Catholic and Protestant Doctrines on Politics and Institutional Set-up of both Economies

Under De Gasperi the Catholic left remained contained and the socio-economic policy was dominated by the liberal *linea Einaudi*, but, once De Gasperi resigned, the Christian Socialist Amintore Fanfani became the leading figure of the party. Corporatism started to be re-instated wholesale. Fanfani, a student and follower of Dossetti, was a leftist reformer for whom, in the words of the leader of the Catholic union wing of the party in 1952, "the battle of the DC has to be fought, […], on the territory of social justice, on the recognition of the new rights of the new status of work" (Gronchi cited in Vecchio 1978, 182). Gronchi and his union wing pressed for comprehensive social policy programme and the integration of the lower classes as "resistance to Bolshevism, in doctrine as well as in the social political regime, does not compensate for blocking the working classes in their aspirations for more justice" (Gronchi cited in Vecchio, 181). These thoughts were not mere lip service. Under the leadership of Fanfani, the party's left wing, with its connections to farm leagues and Catholic unions, gained considerable strength within the party. Fanfani wanted to compensate for the organisational agony of the DC under De Gasperi. As a contemporary fellow party member observed, they were convinced that "if the absolute majority had not been reached in the country, it was partly the fault of the DC, due to its organizational insufficiencies, the scarce comprehensive penetration of the various social classes, […], its complicated and tired apparatus" (Boiardi cited in Galli 1978, 161). Fanfani foresaw for the DC a much more active role in the penetration of society than under De Gasperi. Fanfani's view was that the party should not only be a transmission belt and interlocutor between state and society, but that it should also actively influence and model both institutions. Fanfani was convinced that the party had to liberate itself from the Vatican and from *Confindustria* (the Italian employers association). His vision was of a modern mass party firmly anchored on the territory and all-encompassing in its aspirations to the electorate.

Fanfani started with the countryside by ordering Paolo Bononi to build up a dense network of rural savings banks and peasant leagues, the so-called *Coldiretti*. They not only gave out loans to farmers but also became a strong interest group or faction within the DC (Ginsborg 1990, 171). In order to anchor in the urban areas, Fanfani promoted the expansion of a huge network of Christian Democratic *circoli* (social organisations), which usually consisted of a venue with an alcohol licence in the centre of the town or neighbourhood in which Catholic workers could gather. At the end of the 1950s, these ACLI (*Associazioni Cristiane dei Lavoratori Italiani*) *circoli* boasted over one million members. Many of them still exist to this day, even though the DC is long gone. In order to acquire more members, Fanfani initiated large-scale membership subscription campaigns that were held in festival-like atmospheres in which prizes were handed out for inscription. These yearly canvassing campaigns increased the membership of the DC from 1,341,000 in 1955 to 1,377,286 in 1956, and boosted it to 1,400,179 in 1958. This went hand in hand with a shift of the socioeconomic background of the DC members in favour of working-class members. Between 1955 and 1959, the proportion of members coming from the working and lower middle classes increased from 52.2 per cent to 56.7 per cent (Galli 1978, 178). The figures added up in the following way: the presence of workers increased from 19 per cent to 21 per cent, while landless farm labourers accounted for 6.8 per cent, as opposed to 6 per cent. This saw the share of working-class members rise from one quarter to 28 per cent (Galli 1978, 178). Though these figures do not display a substantial increase on their own, they do when one takes the family dimension of Italian society into account. Galli notes that "the DC of Fanfani started to gain control over the electorate independent from the institutions of the bourgeoisie" (Galli 1978, 178).

Fanfani was a fervent exponent of the Catholic left, but, at the same time, he had sympathised with fascism and had held some minor offices during fascism. His interpretation of Catholic Socialism sometimes blurred the lines to fascist corporatist organisation of society. By contrast, German Catholicism was pulled in a liberal direction by the ordoliberals and Protestants after World War Two, and therefore away from stronger corporative thinking. The new corporatist strategy entailed that the DC tightened its grip over the existing state entities and even created new ones. The party also had to simultaneously distance itself from the liberal employer's association, *Confindustria*, in order to increase its financial autonomy (Galli 1978, 72). The prime means for this were the creation of the Ministry of State Holdings (*Ministro delle partecipazioni statali*), which was approved by parliament after prolonged and fierce debate on 22 December 1956. One year later, on 11 January 1957, the law on fossils (*legge idrocarburi*) followed, which gave the state company ENI (*Ente Nazionale Idrocarburi*) a monopoly on research and exploitation in this sector. The strategy to curb the power of business over the party, and society in general, was completed by the withdrawal of all IRI (*Instituto per la Riconstruzione Italiana* – a large state holding) companies from *Confindustria* only a year later on 1 January 1958. Galli notes that, from this point on, "the party that used to be the prince of the industrial complex controlled progressively the means of production, which are the source of true power" (Galli 1978, 180). ENI, a huge oil and gas company founded in 1953, is exemplary of this process. The Christian Democrat Enrico Mattei "a man of few principles and great entrepreneurial skill" (Ginsborg) became its restless president. Starting with the state petrol company AGIP, Mattei built up an industrial empire in the state sector that, within a few years, encompassed business sectors as diverse as petrochemicals, motorway construction, synthetic rubber production, contract engineering, construction and nuclear research (Ginsborg 1990, 164-165). Despite the rampant clientelism and often corrupt practices within ENI, it contributed – together with IRI, the second large state holding – as a key driver of Italy's post-war economic miracle. The flipside of this success was that it tightened the state's, and therefore the party's, grip on society and created a class of politico-economic Christian Democratic barons of whom it became increasingly hard to judge whether their motivations were fuelled by left Catholic ideology or pure rent-seeking for themselves and their party fraction (*corrente*).

Fanfani had intended to build a party with electoral ties that were independent of the Vatican, the allies and *Confindustria*. He wanted to do this with a strong left corporatist program. But, owing to Italy's regional disparities, this played out in different ways in different parts of the country. While the North saw the construction of a strong Christian Democratic subculture based upon a Christian Democratic worldview, the South witnessed the establishing of a gigantic clientelist party machine. The party was Catholic-Christian Democratic in the North and clientelist-corrupt in the South. In the same way, some of the large state holdings became synonymous with the rampant favouritism and clientelism of the DC. The special blend of corporatism that Fanfani had elaborated in his 1948 book *Economia* (Fanfani 1948) was too vulnerable to corruption and clientelism. The transformation of the DC under Fanfani into a corporatist party was, especially in the South, coupled with a drifting towards a clientelist party.

In the Italian case, the initial social Catholic motivations for a specific and distinctive model of corporatist capitalism were, after the 1960s, gradually replaced by vote- and rent-seeking interests. However, ideology and interests re-enforced one another in the Italian model for spoils distribution and contributed both to its stability and to the difficulties to reform it right up to the present day and the Eurocrisis.

In Germany, too, the Christian Democratic left also left its mark on the early set-up of institutions, but, due to the balancing effect between ordoliberal Protestants and social Catholics, the outcome was much less corporatist than in Italy. Social Catholics in Germany also had the upper hand but only as long as their subculture and political connections remained strong. The re-instalment of the German Bismarckian welfare state was a key social Catholic project. The pension reform of 1957 was an enormous popular success. The ordoliberals fought it where they could but were defeated. A public opinion survey from the Allensbach Institute found that Germans ranked it as the "Most popular event in the eight year long history of the Federal Republic". (Conze 2009, 169). The reform contributed immensely to Adenauer's landslide victory in the next election. 1957 was not only the year of Adenauer's big pension reform but was, at the same time, also the "Conceptual final stroke of the social market economy" (Schulz cited in Conze 2009, 169). As a compensation, an "interconfessional compromise" (Manow 2001), the core ordoliberal projects of an independent federal central bank (*Bundesbank*) and the Cartel Law, which led to the formation of an independent Cartel Agency, were finally enacted. 1957 was also the endpoint of another often unnoticed struggle between ordoliberal Protestants and Social Catholics: the introduction of a corporatist interest mediation institution (*Bundeswirtschaftsrat*). It was to guarantee a democratisation of the economy by establishing a second forum for interest representation from capital and labour next to parliament as foreseen in *Quadragesimo Anno*. This idea was pushed by the unions and social Catholics, but was heavily opposed by the ordoliberals. Ludwig Erhard (ordoliberal, Protestant, Minister of the Economy and later Chancellor) could not fully erase the plans, but he managed to postpone and transform them. Seven years later and seven legislative proposals later, the result was the establishing of an expert committee that is still of central importance in German economic affairs today. It is dubbed the Council of the Five Sages of the Economy (*fünf Wirtschaftsweise*) and has - ever since its establishment - been a hotbed of ordoliberal economic expertise that counsels the federal government on matters of political economy. Hence, the re-instalment of German socio-economic institutions in the 1950s and 1960s was heavily influenced by social Catholic ideas but it did not lead to a wholesale influence of Catholic corporatism ideology due to the counterweight of the ordoliberal faction within the CDU. On the other hand, central elements of the German socio-economic system never had any ordoliberal imprint. The anti-ordoliberal huge welfare state and the large amount of co-ordination within Germany's organised capitalism which was further re-inforced during the Keynesian episodes under the Social

Democratic regimes of the 1970s and only came to an end with the stagflation crisis in the late 1970s (Scharpf 1991). However, after the stagflation crisis, Germany slowly began to embark on a reform trajectory inspired by ordoliberal Protestant ideology. This process, which picked up speed but met much resistance from a still strong social Catholic wing within the CDU, was accelerated with German re-unification.

Re-unification brought huge economic problems. During the 1990s, Germany underwent the transformation from being regarded as the strong man to being regarded as the sick one. This was the chance for an ordoliberal comeback. The neoliberal reform agenda, with its emphasis on deep welfare cuts, privatisation, equal starting conditions, the individualisation of social risks and equality of opportunity, came against the backdrop of skyrocketing unemployment, debt, and sluggish economic growth. This made it ever the more politically attractive. Reunification also opened an enormous practical laboratory for neoliberal politics. Approximately 14,600 formerly state-owned companies with 4 million employees together with 2.4 billion hectares of land and a huge public housing stock were to be privatised according to the "principles of the social market economy" (§2 *Treuhandgesetz*). However, these "principles of the social market economy" were now interpreted as being more liberal than ever before. In addition, re-unification altered the electoral map of Germany. With the addition of the Eastern states, 16 million citizens from a Protestant cultural background joined the German electorate and decreased the importance of the Catholic vote for the Christian Democratic Party (Hien 2013).

After German partition, West Germany (FDR) became 45.8 per cent Catholic and 50.6 per cent Protestant. In East Germany (GDR), the 1950 census showed 85 per cent Protestants and 10 percent Catholics. Through a strong policy of de-Christianisation, the GDR brought these figures down to 25 per cent Protestants, 5 per cent Catholics and 70 per cent unaffiliated in 1989 on the eve of re-unification (Pollack and Pickel 2003). West Germany, until re-unification, experienced only a slight drop in church affiliation (though church attendance dropped remarkably). In 1987, 42.9 per cent were Catholic, while Protestants became a minority for the first time with a drop to 41.6 per cent. The number of unaffiliated had risen from 3.6 per cent in 1950 to 11.4 per cent in 1987 (FOWID 2011). Through the strong decrease in church affiliation in the East, re-unification boosted the "non-members of a statuary religious corporation", as the census of 2011 put it, to 33 per cent in the same year. Catholic Church membership sank to 31 per cent of the population and Protestant church membership to 30.8 per cent.

Social Catholicism had already lost much of its political clout in the Christian Democratic Party in the 1980s when the Christian Democratic Employees' Association (Sozialausschüsse) lost both members and influence. Angela Merkel, the East German daughter of a Protestant Priest, became the symbol of the (neo-) Protestantisation of the German Christian Democrats, a party that had, for most of its post-WWII history, been more Catholic than Protestant in its programme, its membership and its electorate. Norbert Blüm, the last prominent "heart-Jesus-Marxist" (Herz-Jesu-Marxist), ended his last term as welfare minister in 1998 and was hissed at the party congress at Leipzig in 2003 for his critique of the new neoliberal party programme (*Zeit* 2003). The Protestant Finance Minister Wolfgang Schäuble became the equivalent of a re-strengthened ordoliberalist. This enabled a series of welfare reforms in the 1990s, and later the famous *Agenda 2010*, which was hammered out by the Red/Green coalition under Chancellor Schröder, but was espoused and passed with the votes of the Christian Democratic Party. Chancellor Merkel stated the following when assuming office in 2005: "I want to thank Chancellor Schröder personally for bravely opening a door with the Agenda 2010" (Merkel, 2005). This was the "homework" that Germany demanded from the crisis countries in exchange for fiscal solidarity. Due to the mono-confessional situation of

Italy, a similar reform process and trajectory never happened, and this is the key to understanding the sharp divergence in the positions of the two economies. Even after the implosion of the DC in the early 1990s under the impact of heavy corruption scandals, the Catholic Church has not ceased to be an influential variable in Italian politics. Some even argue that, without the DC as interlocutor, it has become even stronger. It is very hard to reform the Italian political economy from the outside, as most Northern Protestant countries in the Eurozone demand, because it is anchored so strongly in the cultural background of the country. A cultural background that is composed of ideas, interests and institutions that have, over the past 60 years, formed a very dense amalgam. Social Catholic ideas are loaded with interests since the clientelist ties of vote aggregation in Southern Italy not only survived the dissolution of the DC but were inherited and incorporated by Silvio Berlusconi's "descent" into politics (*discesa in campo*).

4. Conclusion

The Euro crisis has now been dragging on for almost a decade. The fixing and emergency measures have not led to an easing of European relations, but have infuriated the European public, putting Northern populations against Southern ones. A look at the tabloids suffices. The powerful German tabloid *Bild* headlines read: "This is how the Greek Cheated us", "Why do we Pay for Greek Luxury Pensions" and "Go Sell your Islands, you Bankrupt Greeks" (*Bild* 2010c; *Bild* 2010a; *Bild* 2010b). The approach of cultural political economy to the European crisis taken here suggests that there are no "quick fixes" to be expected through structural reforms. Instead, it has shown how political economies like the German and Italian ones evolved over almost a century, and that institutions, ideas and interests interacted in setting their pathways providing a highly durable complex of relations that are hard to break up, especially from the outside.

References

Abelshauser, W. (2003): *Kulturkampf: Der deutsche Weg in die Neue Wirtschaft und die amerikanische Herausforderung*, Berlin: Kadmos.

Abelshauser, W., D. Gilgen and A. Leutzsch (eds) (2013): *Kulturen der Weltwirtschaft*, Göttingen: Vandenhoek und Ruprecht.

Acanfora, Paolo (2007): "Myths and the Political Use of Religion in Christian Democratic Culture", *Journal of Modern Italian Studies*, 12 (3): 307-338.

Bruno A. (2017): "*Dirigisme* and Modernism *vs* Ordoliberalism", in: Josef Hien and Christian Joerges (eds.), *Ordoliberalism, Law and the Rule of Economics*, Oxford: Hart Publishing.

Armingeon, K., and L. Baccaro (2014): "The Crisis and Germany: The Trading State Unleashed", in: B. Eberlein and V. Schneider (eds), *Complex Democracy. Varieties, Crisis, and Transformations*, Wiesbaden: Springer VS, 165-184.

Armingeon, K., K. Guthmann and D. Weisstanner (2015): "How the Euro Divides the Union: The Effect of Economic Adjustment on Support for Democracy in Europe", *Socio-Economic Review*, 14 (1): 1 26.

Baccaro, L., and C. Howell (2011): "A Common Neoliberal Trajectory: The Transformation of Industrial Relations in Advanced Capitalisms", *Politics & Society*, 39 (4): 521-563.

Baccaro, L., and J. Pontusson (2016): Rethinking Comparative Political Economy: The Growth Model Perspective", *Politics & Society*, 44 (2): 175-207.

Baccaro, L., and C. Howell (2017): "Unhinged: Industrial Relations Liberalization and Capitalist Instability", MPIfG Discussion Paper 17/19

Baccaro, L., and C. Benassi (2017): "Throwing out the Ballast: Growth Models and the Liberalization of German Industrial "elations", *Socio-Economic Review*, 15 (1): 85-115. The advancements have now also been acknowledged by the celebrities of the Varities of Capitalism approach.

Baccaro, L., and C. Howell (2017): *Trajectories of Neoliberal Transformation*. Cambridge: Cambridge University Press.

Berman, S. (1998): *The Social Democratic Moment: Ideas and Politics in the Making of Interwar Europe*. Cambridge MA: Harvard University Press.

Berman, S. (2006): *The Primacy of Politics: Social Democracy and the Making of Europe's Twentieth Century*, New York, Cambridge University Press.

Best, J., and M. Paterson (2015): "Towards a Cultural Political Economy – Not a Cultural IPE", *Millenium: Journal of International Studies*, 43(2): 738-740.

Bild (2010a): "Geheimakte Griechenland: Wie Athen Sich Den Euro Erschwindelte", BILD.de./0 Available at: http://www.bild.de/politik/2010/griechenland-krise/geheimakte-wie-die-griechen-in-den-euro-kamen-14462666.bild.html.

Bild (2010b): 'Griechenland-Pleite: Warum Zahlen Wir Ihre Luxus-Renten Mit Milliarden-Hilfe?', BILD.de,/0 27/04/2010. Available at: http://www.bild.de/politik/wirtschaft/wir-zahlen-luxus-rente-mit-milliarden-hilfe-12338430.bild.html.

Bild (2010c): "Griechenland: Verkauft Doch Eure Inseln, Ihr Pleite-Griechen! – Wirtschaft – Bild.de",BILD.de, 27/10/2010./0 Available at: http://www.bild.de/politik/wirtschaft/griechenland-krise/regierungathen-sparen-verkauft-inseln-pleite-akropolis-11692338.bild.html.

Blyth, M. (2003): "Structures do not Come with an Instruction Sheet: Interests, Ideas, and Progress in Political Science", *PS: Political Science and Politics*, 1 (4): 695-706.

Blyth, M. (2013): *Austerity: The History of A Dangerous Idea*, Oxford: Oxford University

Press.

Blyth, M., and M. Matthijs (2018): "Black Swans, Lame Ducks, and the mystery of IPE's Missing Macroeconomy", *Review of Political Economy*, 24 (2): 203-231.

Brunnermeier, M., H. James and J.-P. Landau (2016): *The Euro and the Battle of Ideas*. Princeton NJ: Princeton University Press.

Carstensen, M., and V. Schmidt (2016): "Power through, over and in Ideas: Conceptualizing Ideational Power in Discursive Institutionalism", *Journal of European Public Policy*, 23 (3): 318-337.

Cau, Maurizio (2009): "Alcide De Gasperi: A Political Thinker or a Thinking Politician?", *Modern Italy*, 14 (4): 431-444, at 441.

Conze, E. (2009): *Die Suche nach Sicherheit*, Munich, Siedler Verlag.

DC (1943): *Le Idee Ricostruttive della Democrazia Cristiana*, Rome.

Dyson, K. (2014): *States, Debt and Power*, Oxford: Oxford University Press.

Dyson, K. (2017): "Ordoliberalism as Tradition and as Ideology", in: J. Hien and C. Joerges (eds), *Ordoliberalism, Law and the Rule of Economics*, Oxford: Hart Publishing.

Economist (2015): "German Ordoliberalism has Had a Big Influence on Policy-making during the Euro Crisis", *Economist*, 9 May 2015.

Eucken, W. (1949): *Die Sozialpolitische Frage*, Heidelberg, Weber.

Eucken, W. (1932 [1997]): "Staatliche Strukturwandlungen und die Krisis des Kapitalismus", *ORDO: Jahrbuch für die Ordnung von Wirtschaft und Gesellschaft*, 48: 5-25.

Esch, Femke van, and Eelke de Jong (2017): "National Culture Trumps EU Socialization: The European Central Bankers' Views of the Euro Crisis", *Journal of European Public Policy*, DOI: 10.1080/13501763.2017.1391862

Estevez-Abe, M., T. Iversen and D. Soskice (2001); "Social Protection and the Formation of Skills: A Reinterpretation of the Welfare State", in: P. Hall and D. Soskice (eds), *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*, Cambridge, Cambridge University Press, pp. 145-183.

Falcke, H. (2011): "Welche Ansätze Für Eine Wirtschaftsethik finden wir bei Dietrich Bonhoeffer?", *Evangelische Theologie*, 71: 376-95.

Fanfani, A. (1948): *Economia*, Brescia: Morcelliana.

Ferrera, M. (1984): *Il welfare state in Italia. Sviluppo e crisi in prospettiva comparata*, Bologna: Il Mulino.

Ferrera, M. (1986): "Italy", in: P. Flora (ed), *Growth to Limits: The Western European Welfare States Since World War II, Volume 2, Germany, United Kingdom, Ireland, Italy, Berlin*, Walter de Gruyter.

Ferrera, M. (2017), "The Stein Rokkan Lecture 2016 Mission Impossible? Reconciling Economic and Social Europe after the Eurocrisis and Brexit", *European Journal of Political Research*, 56: 3-22. doi:10.1111/1475-6765.12185

Ferrera, M. (2018): "Mass Democracy, the Welfare State and European Integration: A Neo-Weberian Analysis," *European Journal of Social Theory*, First Published July 3, 2018 https://doi.org/10.1177/1368431018779176

Financial Times (2014): "The Wacky Economics of Germany's Parallel Universe", by Wolfgang Munchau, 16 November 2014.

FOWID: "Religionszugehörigkeit Bevölkerung 1970-2011", available at: https://fowid.de/meldung/entwicklung-religionszugehoerigkeiten-nach-bundeslaendern-1950-2011.

Galli, G. (1978): *Storia Della Democrazia Cristiana*, Bari: Laterza.

Ginsborg, P. (1990): *A History of Contemporary*

Italy, London: Penguin Books.

Goldschmidt, N. (1997): "Die Entstehung der Freiburger Kreise", *Historisch-Politische Mitteilungen: Archiv für Christlich-Demokratische Politik*, 1-17.

Hassel, A. (2017): No way to escape imbalances in the Eurozone? Three Sources for Germany's Export Dependency: Industrial Relations, Social Insurance and Fiscal Federalism", *German Politics*, 26 (3): 260-379.

Hall, P. (2014): "Varieties of Capitalism and the Euro Crisis", *West European Politics*, 37 (6): 1223-1243.

Hien, J. (2012): "Competing Ideas the Religious Foundations of the German and Italian Welfare States", Florence: Cadmus, European University Institute.

Hien, J. (2013): "The Ordoliberalism that Never was", *Contemporary Political Theory*, 12 (4): 349-358.

Hien, J. (2017): "The Religious Roots of the European Crisis", *Journal of Common Market Studies*. Early View http://onlinelibrary.wiley.com/doi/10.1111/jcms.12635/abstract.

Hien, J., and C. Joerges (eds)(2017), *Ordoliberalism, Law and the Rule of Economics*, Oxford and Portland OR: Hart Publishing.

Hien, J., and C. Joerges (2018): "Dead Man Walking? Current European Interest in Germany's Ordoliberal Tradition", *European Law Journal*. Early view https://doi.org/10.1111/eulj.12277.

Höppner, M., and M. Lutter (2017): "The Diversity of Wage Regimes: Why the Eurozone is too Heterogeneous for the Euro", *European Political Science Review*, 10 (1): 71-96.

Invernizzi-Accetti, C. (2019): *What is Christian Democracy? The Forgotten Ideology*, Cambridge; Cambridge University Press.

Jähnichen, T. (2010): "Die Protestantischen Wurzeln der Sozialen Marktwirtschaft", *Ethik und Gesellschaft*, 1: 49-58, at 11, 13.

Jessop, B. (2004): "Critical Semiotic Analysis and Cultural Political Economy", *Critical Discourse Studies*, 1 (2): 159-174.

Jessop, B., and N.-L. Sum (2017): "Putting the Amsterdam School in its Righful Place: A Reply to Juan Ignacio Staricco's Critique of Cultural Political Economy", *New Political Economy*, 22 (3): 342-354.

Lindvall, J. (2006). "The Politics of Purpose: Swedish Economic Policy after the Golden Age", *Comparative Politics*, 38 (3): 253-272.

Johnston, A., and A. Regan (2016): "European Monetary Integration and the Incompatibility of National Varieties of Capitalism", *Journal of Common Market Studies*, 54 (2): 1-19, 318-336.

Johnston, A., and A. Regan (2018): "Introduction: Is the European Union Capable of Intergating Diverse Models oif Capitalism?", *New Political Economy*, 23 (2): 145-159.

Kaufmann, F.-X. (2003): *Sozialpolitisches Denken*. Frankfurt aM: Suhrkamp.

Lenel, H.O. (1991): "Walter Eucken's Briefe an Alexander Rüstow", *ORDO: Jahrbuch für die Ordnung von Wirtschaft und Gesellschaft*, 42: 11-14, at 12.

Masala, C. (2004): "Born for Government: The Democrazia Cristiana in Italy", in: M. Gehler and W. Kaiser (eds), *Christian Democracy in Europe since 1945*, Volume 2, London: Routledge.

Manow, P. (2001): "Ordoliberalismus als ökonomische Ordnungstheologie", *Leviathan*, 29: 179-98.

Manow, Philip, (2015): "Workers, Farmers and Catholicism: A History of Political Class Coalitions and the South-European Welfare State Regime", *Journal of European Social Policy*, 25 (1): 32-49, doi:10.1177/0958928714556969

Müller-Armack, A. (1947): *Wirtschaftslenkung und Marktwirtschaft*, Hamburg: pub house.

Nedergaard, P., and H. Snaith (2015): "'As I Drifted on a River I could not Control': The Unintended Ordoliberal Consequences of the Eurozone Crisis", *Journal of Common Market Studies*, 53: 1094-1109.

Perez, S.A., and M. Matsaganis (2018): "The Political Economy of Austerity in Southern Europe," New Political Economy, (23 (2): 192-207, DOI: 10.1080/13563467.2017.1370445.

Petersen, T. (2008): "Die Sozialethik Emil Brunners und ihre Neoliberale Rezeption", HWWI Research Paper No. 5-6, 1-27.

Pollack, Detlef, and Pickel Gert, (2003): "De-institutionalization of Religion and Religious Individualization in Eastern and Western Germany", *KZfSS Kölner Zeitschrift für Soziologie und Sozialpsychologie*, 55 (3): 447-74.

Pombeni, Paolo, and Giuliana Nobili Schiera (2009): "Alcide De Gasperi: 1881-1954-A Political Life in a Troubled Century", *Modern Italy*, 14 (4): 379-397.

Pontusson, J., and D. Weisstanner (2018): "Macroeconomic Conditions, Inequality Shocks and the Politics of Redistribution, 1990—2013", *Journal of European Public Policy*, 25 (1): 31-58,

Reuter, H.-P. (2010): "Vier Anmerkungen zu Philip Manow, "Die Soziale Marktwirtschaft als interkonfessioneller Kompromiss? Ein Re-Statement", *Ethik und Gesellschaft*, 1: 1-22.

Röpke, W. (1949): *Civitas humana : Grundfragen der Gesellschafts- und Wirtschaftsreform*, 3rd ed., Erlenbach-Zürich: pub house.

Schroeder, W. (1992): *Katholizismus und Einheitsgewerkschaft. Der Streit um den DGB und der Niedergang des Sozialkatholizismus in der Bundesrepublik bis 1960*, Reihe: Politik- und Gesellschaftsgeschichte. Band 30. Bonn: Dietz Verlag.

Smith, Philip (2001): *Cultural Theory: An Introduction*, Malden MA: Blackwell.

Stariccio, J.I. (2017): "Putting Culture in its Place? A Critical Engagement with Cultural Political Economy", *New Political Economy*, 22 (3): 328-341.

Sreeck, W. (2005): "Requirements for a useful Concept of Complementarity", in: C. Crouch, W. Streeck, R. Boyer, B. Amable, P.A. Hall and G. Jackson, "Dialogue on 'Institutional Complementarities and Political Economy'", *Socio Economic Review*, 3 (2): 359-382.

Streeck W. (2009): *Re-Forming Capitalism: Institutional Change in the German Political Economy*, Oxford, Oxford University Press.

Streeck, W. (2013): "The Politics of Public Debt: Neoliberalism, Capitalist Development and the Restructuring of the State", *German Economic Review*, 15 (1): 143-165.

Streeck, W. (2016): "Commentary on Lucio Baccaro and Jonas Pontusson, 'Rethinking Comparative Political Economy: The Growth Model Perspective'", *Politics & Society*, 44 (2): 175-207.

Sum, N.-L., and B. Jessop (2013): "Towards a Cultural Political Economy: Putting Culture in its Place in Political Economy", Cheltenham: Edward Elgar.

Svallfors, S. (2016): "Politics as Organised Combat – New Players and New Rules of the Game in Sweden", *New Political Economy*, 21 (6): 505-519.

Svallfors, S., and A. Tyllström (2018), "Resilient Privatization: The Puzzling Case of For-profit Welfare Providers in Sweden", *Socio Economic Review*, Early View. https://doi.org/10.1093/ser/mwy005.

Swedberg, R., and O. Agevall (2005): *The Max Weber Dictionary*, Stanford CA: Stanford University Press.

Thelen, K. (2015): Producer Coalitions and National Growth Strategies (paper presented at the 22nd International Conference of Europeanists, Paris, 8-10 July 2015).

Quadragesimo Anno, Pius XI, (1931): available at: http://w2.vatican.va/content/pius-xi/en/encyclicals/documents/hf_p-xi_enc_19310515_quadragesimo-anno.html, 75, last accessed 22 August 2017.

Vecchio, G. (1979): *La democrazia Christiana in Europa (1891-1963)*, Milan, Mursia.

Weber, M. (1904) "Die 'Objektivität' sozialwissenschaftlicher und Sozialpolitischer Erkenntnis", *Archiv für Sozialwissenschaften und Sozialpolitik*, 19 (1): 22-87.

Weber, M. (1968): *Economy and Society: An Outline of Interpretive Sociology*, New York: Bedminster Press.

Zeit (2003): "Blüms Erben: Kulturkampf in der CDU", available at: http://www.zeit.de/2003/43/CDA

B SECTORS OF THE POLITICAL ECONOMY OF ITALY AND GERMANY

WORLDS APART: THE DIVERGENCE OF SOUTHERN-EUROPEAN HOUSING-CONSTRUCTION ECONOMIES AND NORTHERN-EUROPEAN EXPORT ECONOMIES

Sebastian Kohl & Alexander Spielau
Max Planck Institute for Studies of Societies

Introduction

In both public debates about the economic heterogeneity of Southern and Northern European economies - and especially the Italian and German ones - as well as in Comparative Political Economy, the construction sector and housing construction in particular are rarely debated topics. This contrasts with their overall economic importance and the important cross-country differences in housing construction. Our contribution argues in favour of taking this "forgotten sector" seriously in Political Economy, in which manufacturing or finance, as of late, have been the predominant focus. However, lessons learned in these sectors have hardly been transferred to construction, with its different sectoral logics.

We therefore show how Germany and Italy - and Southern Europe more generally - have moved along different housing and construction trajectories over the last decades. Italy became a high-homeownership country with initially low mortgage debt, while Germany remained a country of tenants with initially high mortgage-debt levels and a declining trend since then. Germany maintained a large private rental market, whereas stronger historical rent legislation eroded the Italian rental market (Voigtländer 2009). Most notably, the end of the post-war construction cycle led to an a-synchronisation of construction cycles in both countries. Germany was uniquely booming after re-unification just as Italy's construction boom was about to take off, leaving Italy with surplus housing and Germany with housing shortages today.

Just when Germany's mortgage debt started to decline seriously in the year 2000, the Italian one began to rise steeply and similar trends can be observed in house prices. At the same time, German export surpluses began to grow to unprecedented levels, while mortgage- and wage-repressed domestic demand left the housing and construction sector starving. Not surprisingly, we find a negative cross-sectional association between the importance of exports and construction in OECD countries from the 1980s onwards.

As we argue in the discussion, construction- and export-driven economies require systematically different macroeconomic conditions. Construction, for instance, thrives with low interest rates, higher inflation, and relies almost exclusively on wage-driven domestic demand. Conversely, exports require stable inflation and, if possible, undervalued real exchange rates. For Germany, exports became cheaper due to its wage repression. One the one hand, the inclusion of structurally heterogeneous economies in one monetary union could therefore be seen as problematical, as macroeconomic policies cannot address contradictory demands. On the other hand, it could also be an insurance-mechanism, as construction cycle downturns are no longer as correlated between countries as they were previously.

1. Construction: A Neglected Core Component of Advanced Capitalist Economies

In the shadow of economic sectors as predominant as manufacturing, finance, and various services-sector branches, contemporary Political Economy has neglected core components of capitalist economies. Among those sectors left behind, the construction sector stands out not only with regard to its contribution to GDP, but also with regard to its contribution to employment (especially for low- and medium-skilled workers). It, moreover, contributes largely to the formation of the physical capital stock of modern economies, even if its added-value contribution varies significantly across OECD economies.

When we speak of construction, we distinguish it from the debates on housing and especially housing finance which have gained overwhelming attention since the dawn of the global financial crisis in 2007/08 (Schwartz and Seabrooke 2008b). These debates usually discuss aspects of wider financialisation, such as the effects of financial (de-) regulation, product developments in the financial sector for the purpose of insurance, hedging, and speculation, as well as general macroeconomic steering actions to create GDP growth in a globalising economy through capital attraction (Schwartz 2009, Fuller 2018). However, very few studies are actually interested in the real economy output of activities in the housing sector, which should accompany the rise of housing finance (Malpezzi and Maclennan 2001).

We want to stress the fundamental role of construction for any governmental gross fixed capital formation. Since governments in advanced capitalist economies usually do not own factory productions, they spend their investment necessarily not on machine goods,[103] but largely on the production of infrastructure and (social) housing. They are thus the principal clients of the construction sector. The sector refers to all parts of an economy that are concerned with the construction, maintenance, and utilisation of buildings and other structures (*i.e.*, dwellings and infrastructure), and the adjustment and change of building stock through construction activity. The stock of dwellings matters not only with regard to its absolute number, but also with regard to the level and development, that is, the cumulated (building) assets as well as the residential capital stock (Rußig, Deutsch, and Spillner 1996, 12f., Fleming 1988, Gornig and Michelsen 2017).[104]

Yet, compared to other sectors, the construction sector shows certain industry-specific qualities. One of these is that the nature of the (building/dwelling) product demands for mostly individual solutions in the form of made-to-order production. This reduces repeatability, mass-standardisation, and thus continuous productivity increases within the sector. Moreover, the multitude of sites on which firms have to operate as well as the number of trades that are involved both within a firm as well as across construction projects create complex, industry-specific co-ordination problems. Furthermore, due to the close bond between producer and buyer, the mostly regional nature of the construction market, and the necessity to form consortia and small companies which act as suppliers to these trades limit competition and customer diversification severely. Last, high capital requirements and the longevity of production processes create a high sensitivity to changes in the monetary, financial, and regulatory environment.

Consequently, the different sectoral logic also promotes different macroeconomic repercussions. For reasons of space, we will focus only on two macroeconomic policy aspects of construction activity. First, the construction sector serves as a kind of natural buffer to macroeconomic shocks. Due to its dominant role as an investment goods industry in conjunction with a higher general level of volatility in investment compared to general demand, the construction sector faces additional vulnerability to changes in the general economic climate. Thus, the severity that booms and slumps have on construction activity goes hand-in-hand with a higher likelihood of adverse effects on the industry during these business-cycle events.

In contrast to manufacturing, a loss of demand in the construction sector usually represents a severe short-term threat to the regional business models of firms. On the one hand, although production lasts, on average, over a longer period of time, the dependence on long-term finance represents a threat to payment and fulfilment of contractual obligations both on the side of customers as well as on that of the construction firms itself. Hence, construction firms cannot simply "wait and see" during crises, but are under constant threat of insolvency despite full order books. On the other

103 With the noticeable exception of car pools and military equipment.

104 The construction sector resembles not so much a singular industry (in the narrow understanding), but rather a complex sub-system of the economy due to its deep interlinkages with other sectors such as manufacturing for the production of pre-manufactured steel or concrete parts.

hand, a reduction in employment – which is something necessary during times of reduced order numbers – is difficult to accomplish as a construction firm needs to retain various trades and skills in order to maintain its operational capacities. This retention of excess labour capacities in this "populated" sector prevents the immediate severe increase of overall unemployment in an economy.

Only in the case of a lasting recession and further reduced order numbers will small construction and specialised supply-trade firms face bankruptcy and thus ramp up unemployment overall. Hence, the delay of unemployment due to the necessity to retain intra-firm skills makes the sector a buffer for macroeconomic shocks and a bearer of significant adjustment costs of business-cycle downturns in general.

Second, the construction sector is a core playing-field for governments wanting to engage in macroeconomic management, because a government's capacity to steer economic activity through investment depends on its access to the sector. For one, it is the easiest way to increase overall economic activity. An activist government can use the sector (in so far as labour capacity is available economy-wide) to enlarge positive employment and growth. However, a government willing to enforce construction activity has to provide conducive macroeconomic and monetary conditions (e.g., lower capital costs and increased capital availability in the domestic economy to be spent on housing and infrastructure). Yet, in so doing, it faces negative consequences for the overall export competitiveness which profits from quite different conditions such as a comparably lower inflation rate and unit labour cost developments (that result in an effective real exchange-rate under-valuation with regard to trading partners). Hence, construction companies benefit from the opposite monetary conditions than export-oriented manufacturing firms.

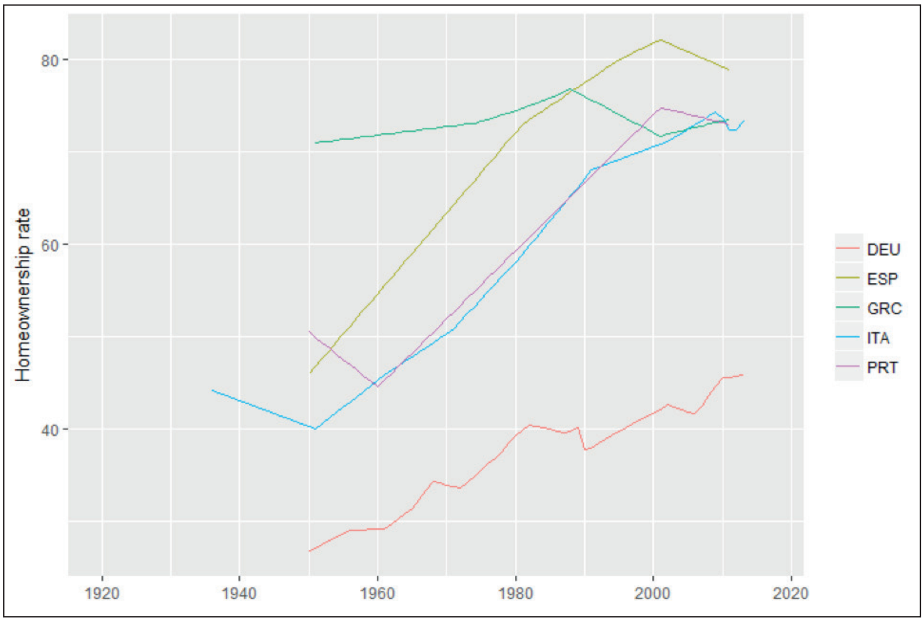
This, in turn, has consequences for the national growth strategies and the development of national housing regimes. If a government wishes to facilitate a national strategy of export-orientation, it has to curtail both the inflationary effects of construction activities as well as the overall size and contribution of the sector itself. On the other hand, due to its role for the active domestic macroeconomic management, one can attribute the promotion of construction activity to the domestic consumption-led growth model (Baccaro and Pontusson 2016). Since national housing and ownership patterns vary significantly across OECD countries for historical reasons (Kohl 2017), a government is unable to change the general role of construction activity in the short term. For instance, a government that encourages property ownership relies on the availability and the provision of new housing stock to make this model work.

Given the difference in the underlying monetary conditions as well as the importance that governments attribute to construction, there is an overall, distinguishable effect on the macroeconomic performance of an economy and, thus, potentially on the development of macroeconomic imbalances. For the discussion about European macroeconomic imbalances, this means that the construction sector is at the core of the origins of the North-South divide.

2. Diverging Housing and Construction Trajectories in Southern Europe and Germany

The differences in housing and construction between Southern and Northern Europe are not of recent origin. Traditionally, Southern European housing and construction regimes have been characterised as distinct from Northern European countries, and, even internationally, have been exceptional along a variety of dimensions (Castles and Ferrera 1996). First of all, all Southern European countries have developed into high-homeownership countries, comparable only to the completely privatised housing regimes of Eastern Europe and largely surpassing even the traditional Anglo-Saxon high-homeownership countries (Stephens, Lux, and Sunega 2015). In the German-Italian comparison, the homeownership gap amounts to 30 plus percentage points, as shown in Figure 1.

Figure 1: Homeownership rates in Germany and Southern Europe



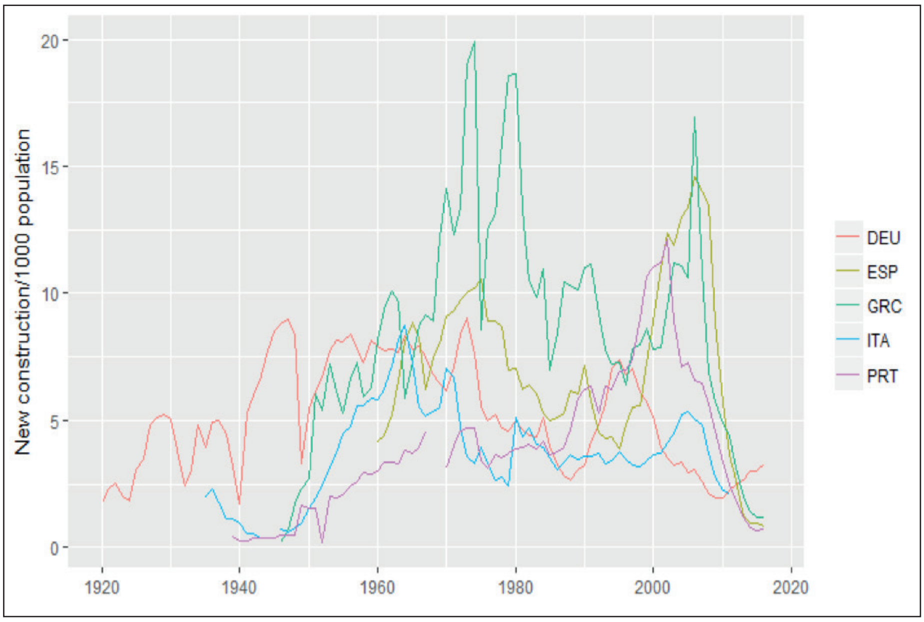
Source: (Kohl 2017)

The flipside of these differences in tenure is, of course, that the rental stock is much larger in Germany than in Southern Europe. One reason behind these diverging developments is that the regulation of private rental relations was historically much more intense in Southern Europe than in the North (Weber 2017, Kholodilin 2018). All countries started rent regulation and tenant protection during the two World Wars. Yet, Southern European countries were both slower in de-regulating after the wars and more likely to re-introduce hard rent freezes when rent inflation risked endangering the social peace. One potential cause for these social policies via consumption price stops was the lack of functioning and effective wage co-ordination in the South (Höpner and Lutter 2018). A direct consequence of strong rent regulation, however, was the increasing conversion of private rental units into owner-occupied ones and a flight of landlords from this market segment. When Italy started its de-regulation of rent prices again in the 1980s, large conversions had already taken place and Italy had become a country of homeowners.

A second dimension is the kind of homeownership which has mostly grown in the form of condominium or apartment ownership in Southern European countries. Legal arrangements of privately owning parts of a building on the same plot of land were absent in German Civil Code between 1901 and 1951. After being legally introduced, owner-occupied flats remained a very exceptional form of tenure until the late 1970s (Kohl 2017, Chapter 4). Even nowadays, flats that are available for purchase under condominium ownership law are still a minority in German cities, albeit a growing one. Much to the contrary, countries following the French Civil Code have either always known a sort of condominium ownership or introduced an updated form of it much earlier in the twentieth century. In Italy in the 1930s, still under Mussolini's policies in favour of an ownership society (Bortolotti 1978), most of the new constructions were apartment buildings with flats in condominium ownership (Di Feliciantonio and Aalbers 2018). This mostly urban phenomenon makes Southern European countries' housing stock appear as an exception among OECD countries (Hoekstra 2005) and creates crucial differences in how the urban fabric works. German major cities, for instance, are populated by majorities of (private) tenants, whereas Italian cities have long since moved to homeowner majorities. Given tenure and house-price related voting patterns (Ansell 2014), this can be a crucial political difference as well.

A third dimension of a South-Northern divergence is in the sector of new constructions. While all countries saw a similar post-war re-construction boom which peaked in the 1970s, the subsequent trajectories were different from each other. Germany had an exceptional construction boom after re-unification, which set it apart from all other countries. Scandinavian countries at that time had just experienced a house price bust and major recession, and Southern European countries were just about to start one of their most extensive construction booms in the mid-1990s. As a result, the building cycles, usually correlated with the general business cycle, became asynchronous among countries that began the European Monetary Union, as Figure 2 shows. Italy's housing boom was still the most conservative one among Southern European countries; hardly going beyond the 5 units built per 1,000 inhabitants. A potential source of distortion here could be that a certain number of informal housing units were not counted in the construction statistics, due to informal housing being part of the belated urbanisation process in Southern Europe (Allen 2004). But in all Southern European countries, the construction sector made up large shares of the GDP and was booming at a time when Germany's was in a deep recession.

Figure 2: Construction cycles[105]



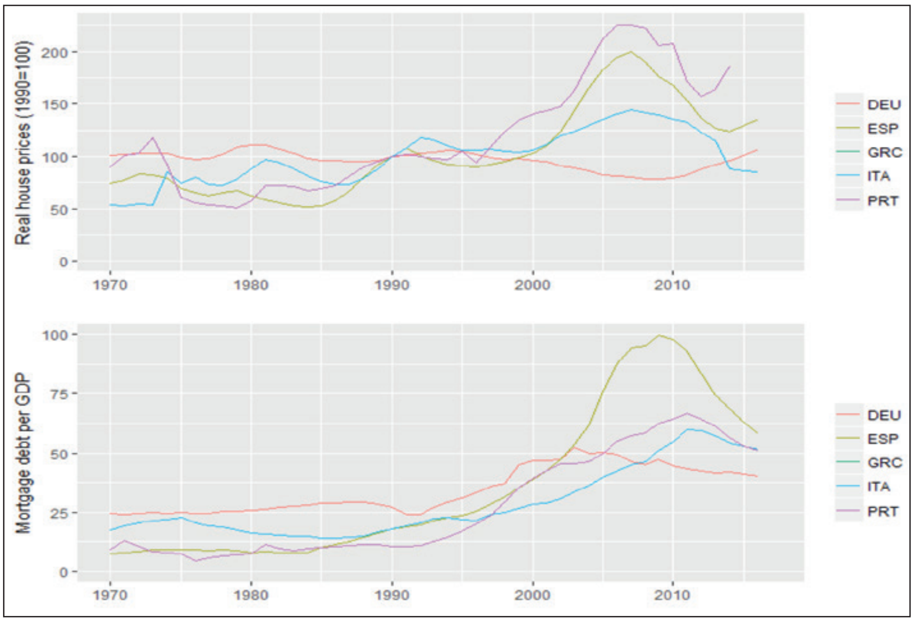
Source: National construction statistics; (Bolt et al. 2018)

A final divergence was in house price and mortgage developments, as presented in Figure 3. While Southern European countries witnessed continuously rising real house prices over the last five decades, Germany's house prices stagnated until the crisis of 2007, only to take off in 2010 when house prices started to decline again in all Southern countries. The German house prices, in relation to 1990, have even overtaken the Italian development again in recent years. House prices are, of course, closely related to mortgage indebtedness. Traditionally, Southern European economies were characterised by family-owned forms of housing finance. Rather than relying on bank credit, *ex-ante* savings and within-family credit were supposed to fill the gap left by a still underdeveloped social system (Schwartz and Seabrooke 2008a, Blackwell and Kohl 2018). Although elements of this system might still persist, the recent mortgage-debt growth in Southern European countries reveals a changing picture, as Figure 3 shows. Germany has had a higher mortgage debt per GDP until the late 1990s. But with the end of the re-unification boom, all Southern European economies overtook Germany in terms of institutionalised mortgage debt. This was driven by house price increases, but also by banks relying more on external (foreign) capital and new securitisation techniques.[106]

105 Numbers use housing completions. If not available, housing starts or permits were deflated by the first lag times 0.95 of permits issued. The displayed deflated Greek permit-based numbers still reflect speculative exaggeration before the crisis 2007 and need to be interpreted accordingly.

106 Spain being a prime case for the latter development (van Gunten and Navot 2016).

Figure 3: House prices and mortgage debt per GDP



Note: House prices (above figure) and mortgage debt per GDP figures (below figure).

Source: (Jordà, Schularick, and Taylor 2017, Knoll, Schularick, and Steger 2015, Amaral 2018).

The only point of convergence in the countries' housing systems has been the decline of social rental housing (Harloe 1995). It amounted traditionally to up to a third of Germany's housing stock, but never more than 10 per cent in the case of Southern European countries. In recent years, this public housing segment has been generally in retrenchment mode, reported to be about 4 per cent in Germany in 2012 (*Bundestag* 2012).[107]

One consequence of these diverging construction trends is that housing markets in the North and South are currently facing very different problems. In Southern Europe, the overcapacity of the construction industry has led to a construction-driven prolonged recession, to an oversupply of housing and high vacancy rates, as well as problems of mortgage delinquency and foreclosures (Cano Fuentes et al. 2013, Gentili and Hoekstra 2018). Given the oversupply of housing, however, prices (and outstanding mortgage debt) remain surprisingly sticky. In Germany, by contrast, the construction sector has been running at full capacity and still not producing sufficient (affordable) urban housing to fill the run-up shortages or to drive down urban prices (Voigtländer et al. 2017).

3. Discussion: What are the implications of different housing/construction regimes for the broader political economy in Europe?

If it was not the construction sector that most employees and domestic credit was allocated to in Germany, where did the factor input go? Germany, much more than other Northern European countries, developed into an export-driven economy (Baccaro and Pontusson 2016). While tendencies of export-orientation or currency under-valuation can be traced back to the post-war period (or even earlier) in the German case (Höpner 2018, Scharpf 2018), it was not until the last three decades that Germany produced persistently high and even growing exports surpluses. This occurred at the same time that its construction sector and mortgage debt declined, while Southern Europe produced a mortgage-driven construction boom. Not surprisingly, OECD countries display a negative cross-sectional association between the importance of their export and their construction sectors in the economy, with Germany and Sout-

107 Even if non-profit housing organisations and co-operatives still make up more than 10 per cent of Germany's private rental sector.

hern Europe choosing alternative strategies along this negative association.

The fact that countries usually do not have both - a thriving export and a booming construction sector - has to do with the different macroeconomic environments that the two sectors require in order to prosper. The construction sector works best in times of higher inflation and lower interest rates. Construction and particularly the purchase of houses requires cheaply available capital, and higher inflation makes the burden of mortgage indebtedness less onerous. It also motivates people to switch from financial to the intangible asset of housing. The mostly manufacturing export sector in the economy, by contrast, requires low inflation through higher interest rates in order to have reliable exchange rates, *i.e.*, expectable prices both of goods imported and of goods sold abroad. Finally, on the demand side, the construction sector almost exclusively relies on domestic demand, whereas the export sector, by definition, is much less in need of domestic demand. Much to the contrary, it emphasises wage restraint to guarantee the competitiveness of goods exported abroad. Therefore, one can understand the worry of the *Bundesbank* in 2017 when discussing the potential negative macroeconomic consequences of an ongoing house-price boom in Germany (*Bundesbank* 2017).

Whatever initiated the divergence along different construction/export trajectories in the 1980s and 1990s, the different functional requirements of dominant sectors in conjunction with social blocs defending their interests acted as reinforcing mechanism to keep countries on the track (Baccaro and Pontusson 2018). A comparative look at party manifestos (Kohl and Spielau 2018), for instance, reveals that OECD countries with a large construction share in the economy, are associated with all manifestos that are more likely to defend infrastructure and housing investments, independently of party cleavages. In countries with large export sectors, by contrast, party manifestos are rather associated with the defence of free trade across party families. Thus, once construction or export-dominated regimes are in place, they tend to produce their own stabilisers.

In international perspective, the two different trajectories of economies can even help stabilise each other, as when export economies simultaneously export their surplus capital to lend it to the domestically consuming construction economies (Fuller 2018). Having countries with asynchronous construction cycles in a monetary union, however, can also be a blessing in disguise, because it could act as a risk-sharing mechanism.[108] When construction is down in one economy, it could be compensated for by an upturn in another one.[109] The risks of a construction-cycle and hence business-cycle downturn could thus become uncorrelated and work as a sort of insurance, with one economy absorbing the capacities and demand of the other. Yet, the extent of the insurance-mechanism might be limited, as the regional character of construction reduces the easy transferability of workers, firms, and building traditions from one country into another.

This rosier insurance mechanism could also be thwarted by the inability to adjust the macroeconomic steering of inflation and interest rates to nationally different construction markets. This meant in particular that the common European interest rate in the early 2000s was too restrictive for the German construction sector, where household debt was decreasing and construction output down (Scharpf 2018). Conversely, Southern European economies faced house-price, construction, as well as mortgage booms, and thus the risk of an overheated economy followed by an even deeper recession. Therefore, the current struggles within the Eurozone can also be interpreted through the lens of structurally different economies: some of them relying on debt-financed domestic demand with large construction sectors, and others relying on wage- and credit-restraint domestic demand in favour of a growing export sector.

108 See Schelkle for a related argument (Schelkle 2017).

109 One can compare this to times when urban construction cycles had not been synchronised in national economies and provided for regional balancing.

References

Allen, Judith. 2004. *Housing and Welfare in Southern Europe*. Oxford: Blackwell.

Amaral, Francisco. 2018. *House Prices in Spain, 1870-2015*. University of Bonn: Master's thesis.

Ansell, Ben W. 2014. "The Political Economy of Ownership: Housing Markets and the Welfare State." *American Political Science Review* 108 (2): 383-402.

Baccaro, Lucio, and Jonas Pontusson. 2016. "Rethinking comparative political economy: the growth model perspective." *Politics & Society* 44 (2): 175-207.

Baccaro, Lucio, and Jonas Pontusson. 2018. "Wirtschaftswachstum nach dem Fordismus: Neue Ansätze in der vergleichenden politischen Ökonomie." *WSI-Mitteilungen* 71 (2): 83-95.

Blackwell, Timothy, and Sebastian Kohl. 2018. "The origins of national housing finance systems: a comparative investigation into historical variations in mortgage finance regimes." *Review of International Political Economy* 25 (1): 49-74.

Bolt, Jutta, Robert Inklaar, Herman de Jong, and Jan Luiten van Zanden. 2018. "Rebasing 'Maddison': New Income Comparisons and the Shape of Long-run Economic Development." *GGDC Research Memorandum* 174.

Bortolotti, Lando. 1978. *Storia della politica edilizia in Italia : proprietà, imprese edili e lavori pubblici dal primo dopoguerra ad oggi (1919-1970)*. Rome: Editori Riuniti.

Bundesbank. 2017. Immobilienmärkte und mikroprudenzielle Aufsicht. Vortrag von Andreas Dombrat beim 39. Symposium des Instituts für Bank- und Finanzgeschichte. https://www.bundesbank.de/Redaktion/DE/Reden/2017/2017_05_04_dombret.html.

Bundestag, Deutscher. 2012. "Schriftliche Fragen." *Drucksache 17/10425, 03.08.2012.*

Cano Fuentes, Gala, Aitziber Etxezarreta Etxarri, Kees Dol and Joris Hoekstra. 2013. "From Housing Bubble to Repossessions: Spain Compared to Other West European Countries." *Housing Studies* 28 (8): 1197-1217.

Castles, F.G., and M. Ferrera. 1996. "Home Ownership and the Welfare State: Is Southern Europe Different?" *European Society and Politics* 1 (2): 163-185.

Di Feliciantonio, Cesare, and Manuel B. Aalbers. 2018. "The Prehistories of Neoliberal Housing Policies in Italy and Spain and Their Reification in Times of Crisis." *Housing Policy Debate* 28 (1): 135-151.

Fleming, Michael. 1988. "Construction." In *The Structure of the British Industry*, edited by Peter Johnson, 213-234. London: Unwin Hyman.

Fuller, Gregory W. 2018. "Exporting Assets: EMU and the Financial Drivers of European Macroeconomic Imbalances." *New Political Economy* 23 (2): 174-191.

Gentili, Martina, and Joris Hoekstra. 2018. "Houses without People and People without Houses: A Cultural and Institutional Exploration of an Italian Paradox." *Housing Studies*:1-23. doi: 10.1080/02673037.2018.1447093.

Gornig, Martin, and Claus Michelsen. 2017. "Construction sector: Full order books, good growth prospects." *DIW Economic Bulletin* 7 (6/7):75-85.

Harloe, Michael. 1995. *The People's Home? Social Rented Housing in Europe and America*. Oxford: Blackwell.

Hoekstra, J. 2005. "Is There a Connection between Welfare State Regime and Dwelling Type? An Exploratory Statistical Analysis." *Housing Studies* 20 (3): 475-495.

Höpner, Martin. 2018. "Strategic Undervaluation: The History of Germany's Export Orientation " *MPIfG Discussion Paper*.

Höpner, Martin, and Mark Lutter. 2018. "The Diversity of Wage Regimes: Why the Eurozone is too Heterogeneous for the Euro." *European Political Science Review* 10 (1): 71-96.

Jordà, Òscar, Moritz Schularick and Alan M Taylor. 2017. "Macrofinancial History and the New Business Cycle Facts." In *NBER Macroeconomics Annual 2016, vol. 31*, edited by Martin Eichenbaum and Jonathan A. Parker. Chicago: Chicago University Press.

Kholodilin, Konstantin A. 2018. "Measuring Stick-Style Housing Policies: a Multi-Country Longitudinal Database of Governmental Regulations." *DIW Discussion Papers* 1727.

Knoll, Katharina, Moritz Schularick and Thomas Steger. 2015. "No Price Like Home: Global House Prices, 1870-2012." *Centre for Economic Policy Research Discussion Paper* 10166.

Kohl, Sebastian. 2017. *Homeownership, Renting and Society: Historical and Comparative Perspectives*. London: Routledge.

Kohl, Sebastian, and Alexander Spielau. 2018. "The Political Economy of Diverging Export and Construction Trajectories since the Demise of the Keynesian Construction State." *Unpublished manuscript*.

Malpezzi, Stephen, and Duncan Maclennan. 2001. "The Long-run Price Elasticity of Supply of New Residential Construction in the United States and the United Kingdom." *Journal of Housing Economics* 10 (3): 278-306.

Rußig, Volker, Susanne Deutsch and Andreas Spillner. 1996. *Branchenbild Bauwirtschaft: Entwicklung und Lage des Baugewerbes sowie Einflußgrößen und Perspektiven der Bautätigkeit in Deutschland*,Berlin: Duncker & Humblot.

Scharpf, Fritz. 2018. "International Monetary Regimes and the German Model." *MPIfG Discussion Paper* 1.

Schelkle, Waltraud. 2017. *The Political Economy of Monetary Solidarity: Understanding the Euro Experiment*: Oxford: Oxford University Press.

Schwartz, H., and L. Seabrooke. 2008a. "Varieties of Residential Capitalism in the International Political Economy: Old Welfare States and the New Politics of Housing." *Comparative European Politics* 6: 237-261.

Schwartz, Herman. 2009. *Subprime Nation. American Power, Global Capital, and the Housing Bubble*. Ithaca NY: Cornell University Press.

Schwartz, Herman M., and Leonard Seabrooke. 2008b. "Varieties of Residential Capitalism in the International Political Economy: Old Welfare States and the New Politics of Housing." *Comparative European Politics* 6 (3): 237-261.

Stephens, Mark, Martin Lux and Petr Sunega. 2015. "Post-Socialist Housing Systems in Europe: Housing Welfare Regimes by Default?" *Housing Studies* 30 (8): 1210-1234. doi: 10.1080/02673037.2015.1013090.

Van Gunten, Tod, and Edo Navot. 2018. "Varieties of Indebtedness: Financialization and Mortgage Market Institutions in Europe." *Social Science Research* 70: 90-106.

Voigtländer, Michael. 2009. "Why Is the German Homeownership Rate so Low?" *Housing Studies* 24 (3): 355–372.

Voigtländer, Michael, Philipp Deschermeier, Ralph Henger and Björn Seipelt. 2017. *Zuwanderung, Wohnungsnachfrage und Baubedarfe in Deutschland*. Edited by Stephan Mitschang, *Erhaltung und Sicherung von Wohnraum*. Baden-Baden: Nomos Verlagsgesellschaft mbH & Co. KG.

Weber, Jan Philip. 2017. *The Regulation of Private Tenancies - A Multi-Country Analysis* Universität Regensburg: Dissertation.

BANKING CRISIS INTERVENTIONS IN GERMANY AND ITALY: THE UNPLEASANT CASE OF THE NEW EUROPEAN BANK RESOLUTION FRAMEWORK

Frederik Traut

Hertie School of Governance

Introduction

The banking crisis of the late 2000s not only had a long-lasting impact on the European Union, its economy, and many of its citizens, it also changed the political discourse to a certain extent. References to the billions mobilised overnight to rescue struggling banks have become defining parts of many political debates surrounding financing welfare spending, rescuing bankrupt firms, and reducing taxes. Why could states raise money for bank rescues but not for pensioners or workers? There is some truth in this argument: confronted with great turmoil on financial markets, liquidity and solvency problems of major parts of the banking sector, in addition to an alarmed public, many European countries intervened in markets and saved a number of struggling banks with taxpayers' money. Governments injected capital into failing banks, they bought non-performing loans (NPLs), facilitated take-overs, or guaranteed banks' assets. This was necessary due to the high importance of banks for the rest of the economy. They were often "too-big-to-fail" (Krugman, 2010), meaning that a single bank was so important for the functioning of an economy that a country could not afford to let it go bankrupt. In other cases, governments feared public panic and the breakdown of their banking sector simply due to a loss of confidence if they let one bank fail – a self-fulfilling prophecy. As soon as banks can no longer fulfil their role as financiers of businesses, an economic crisis is almost inevitable. Hence, most major economies bailed out their banks (and investors) instead of letting them go bankrupt, even though bad investment decisions and unreasonably high exposures to risks had led to such scenarios. States simply had no alternative but to save banks.

Governments vowed never to let their economies be held hostage by struggling banks again. This resulted in increased regulation at international (such as Basel III) as well as at European level, more stringent supervision especially for the most important banks (e.g., the European Single Supervisory Mechanism - SSM), and other common rules for banks across Europe, especially with regard to their resolution in the case of failures. This common approach towards regulation became necessary as the recent crisis had revealed major contagion risks across countries (Fecht, Grüner, & Hartmann, 2012). In Europe, this contagion across national banking sectors was accompanied by interdependencies in a monetary union through public debts that rose as a result of the banking and economic crises. The new rules implemented in Europe in recent years are supposed to avoid banking crises through regulation and supervision as well as through market discipline by making the bankruptcy of a bank a credible threat for investors. This paper focuses on the newly introduced European resolution framework for failing banks that contributes to the latter.

In theory, investors are supposed to bear the full risk of their investment and supervise it accordingly; any prospect of government intervention in times of crisis distorts such incentives. It is a straightforward assumption of economic theory that investors would choose their preferred risk class by maximising their utility in a trade-off between security and returns. Some investors might very well be risk-seeking in return for high premia and allow a firm to behave hazardously, while many others might prefer to contain risks and control the respective firm more stringently. In a perfect world, all actors are aware of these risks and should either be ready to face the consequences or hedge against losses. The prospect of state intervention in times of crisis changes this pattern and, consequentially, may lead to riskier behaviour of firms because their investors do not see the need to control them as stringently; in fact, they may even push them into risky business since they know that there is a certain amount of government insurance that limits their risk. Due to the systemic importance of banks for all major economies, their investors can usually count on bail-outs by the respective government. Eventually, this leads to both potential economic crises through the inefficiently risky behaviour of banks and high costs for taxpayers for direct bank rescues.

To address this problem, the new European resolution regime was put in place once most states had saved their banks. Future investors should face an undistorted risk of loss, leading to lower costs for taxpayers and better market control of banks. However, parts of the EU had not overcome the crisis at this point and the new regime bound their hands to address threats to investors and whole economies that were still formed under the old regime. Italy is a prime example of this. I contrast Italy's long-lasting banking crisis and the effects of introducing new rules during the ongoing crisis with Germany, whose banking crisis ended early after heavy state intervention.

In the following, I will argue that, while both were affected by the same crisis, the cases of Germany and Italy reveal major differences in their banking sectors prior to, during, and in reaction to the crisis. Germany intervened much faster and with much more power than Italy when the crisis hit in the period from 2007 to 2009. Italy's banks were not greatly affected by the international turmoil, partially due to better supervision and more stability-oriented regulators. The Italian crisis unfolded more slowly following the economic downturn and never reached a peak like the German one, but lasted much longer. Timing was key here because the new European resolution regime was introduced after the German crisis had been resolved, but before the Italian banks ran into deep trouble. This bound Italy's hands in addressing its banking problems in the same way in which the Germans had. Italy partially circumvented the rules and used taxpayers' money to save banks through recapitalisation or at least to facilitate their liquidation. This was highly criticised by German politicians, because it probably reduced the credibility of the new resolution regime. I will argue that Italy had little choice but to evade the new rules to some extent since they were implemented prematurely for countries that were at an earlier stage of the crisis than Germany or other northern European countries.

The following section will be dedicated to sketching the new EU approach towards re-structuring struggling banks. Afterwards, I will describe the banking crises in Germany and Italy, the respective government responses, and the effects that the new rules had on the crisis responses. I will conclude with a comparison of the two cases and an argument on how the premature introduction of a strict and stringent resolution regime has damaged the very purpose for which it was intended.

The EU's Pledge to Let Investors Pay First

The EU Bank Recovery and Resolution Directive (BRRD – European Union, 2014a) and the EU Single Resolution Mechanism (SRM –European Union, 2014b) are supposed to rule out state aid for struggling banks and to ensure orderly resolution if they fail. While the BRRD is an EU-wide measure to harmonise regulation and resolution, the SRM is a feature of the banking union that especially includes the countries of the Eurozone and their banks, which are supervised by the ECB. The introduction of such regulation is a political signal for all those who criticised costly government interventions during the Global Financial Crisis of 2007 to 2009 (GFC) and who fear future cross-border bail-outs in the case of bank failures due to contagion risks across closely interlinked economies. But it is also a measure to get incentives for investors straight and reduce excessive risk-taking. Shareholders and bondholders are supposed to be the first ones to bear the losses of a struggling bank through so called bail-in mechanisms that result in financing the bank's resolution or recapitalisation through investor liability before any other stakeholder have to step in.

Key to achieving a change in future investor incentives is the credibility of such a scheme. Investors will adjust their behaviour only to a limited extent if they can expect bail-ins to remain an exception and bail-outs – the standard intervention during the GFC – to prevail as a standard reaction to bank failures. In particular, the SRM was supposed to be a solution that credibly regulates the resolution of a failing bank – including investor liability – complementing the new Single Supervisory Mechanism that was supposed to prevent Europe-wide systemic banking crises in the first place. A potential result of such a credible resolution regime is a virtuous circle in which market forces require banks to act more prudently, which results in fewer banking crises and renders the new resolution regimes almost unnecessary.

In the event of a crisis that threatens a bank's existence, the new resolution mechanism is organised around two pillars: a liability cascade for bank investors (the bail-in mentioned before), diverging from usual insolvency regulation, and a resolution fund for the case that recapitalisation through the bail-in is not enough to cover the costs of a potential failure. These pillars come into effect when a normal insolvency of a financial firm would endanger financial stability. The liability cascade means that, after own funds are used up for recapitalisation measures, junior and even senior bondholders must write off their investments or convert them into shares to recapitalise the firm, following a pre-determined pattern. While seeming like a straightforward consequence of "bad" investments, losses for senior investors have rarely occurred in the past, which probably played a role when investment decisions were made. This corresponds to the too-big-to-fail argument mentioned before. Letting a bank fail based upon normal procedures, even if it is not too-big-to-fail, would probably take much time and destroy trust in the financial system if the state did not step in and smoothen the failure. Pre-determined rule-based recapitalisation can make this process faster and more efficient so that triggering it is a real threat.

The resolution fund is an instrument of last resort that is supposed to cover the costs of bank resolution if the liability cascade is not enough to cover them. Only if investors already covered losses of at least 8 per cent of the bank's balance-sheet total, does a bank qualify for aid from the resolution fund, which serves as a backstop against state intervention that would have to pay for resolution costs not covered by investor liability (European Union, 2014b). It is financed through contributions from banks themselves so that, in theory, taxpayers do not have to bear any of the costs.

Even though credibility and coherence are key for changing the incentives for investors, the new resolution framework entails exceptions and loopholes. Not only do the usual exceptions for German savings banks and similar small financial firms tend to make the new framework incoherent, but also the definitions on when a bank must be resolved or when it can be saved using state aid in order to avoid significant negative consequences for the rest of the economy remain unclear. An important loophole in this regard is *precautionary recapitalisation* (see Article 16 SRM Regulation/ Article 32 BRRD), which has already been used in Italy to circumvent resolution rules. In the case of precautionary recapitalisation, a government can provide state aid to a struggling bank if it is solvent and systemically important for a country's economy (see Hellwig, 2017) for a detailed analysis of precautionary recapitalisation). These rules were meant for extraordinary cases, but they were already used on the first serious occasion when Italian banks ran into trouble.

Given that the new mechanisms had already been circumvented when they were tested for the first time, it seems questionable whether they can gain enough credibility to change the incentives for investors as described above. If BRRD and SRM are regarded as sham standards, they will not have much impact. It seems questionable whether governments would be able to resist demands to use exceptions from the new rules when banks in their countries fail.

I will come back to this problem after outlining the banking crisis developments in Germany and Italy, which have led to state aid in recent years and how they differ.

The German Response to the Crisis: Quick, Costly, Successful

The German federal government and several state governments as well as government agencies heavily intervened in the banking markets in the period of turmoil between 2007 and 2009. Both private banks and state banks (especially *Landesbanken*, state-level banks that were mostly owned by the respective federal state and the semi-public *Sparkassen*) ran into major trouble during the financial crisis in the US – partially because of their investments in risky assets, and partially because of a loss in confidence in the banking market following the failure of major international banks. The crisis responses included the outright nationalisation of banks, relief from bad loans through special asset management corporations (bad banks), state-guarantees, and the facilitation of take-overs or liquidation. Some examples might be helpful to illustrate the mismanagement of German banks prior to the crisis and how much the German government intervened:

IKB, a bank specialised in lending to medium-size enterprises, was the first German bank that faced great difficulties in the GFC and had to be saved by public entities in the 2007–2008 period. It suffered dangerous losses from large investments in the infamous US asset-backed securities market [1]that brought the bank to the brink of failure, which it was feared would initiate a chain reaction of failures that would bring the German economy to its knees. The state-owned bank *KfW* (which already held a share of the bank prior to the crisis) and the federal government intervened and bailed out *IKB* with direct capital injections and guarantees for outstanding debts. Eventually, the government helped the bank both directly and indirectly with more than 7bn € (Handelsblatt, 2008).

State banks also faced tremendous losses from unreasonably high exposure to failing US markets; other state banks, states, and the federal government stepped in and bailed them out. For example, *WestLB*, the state bank of North Rhine-Westphalia, was recapitalised through guarantees covering risks of about 5bn € based on the book values of assets whose fair values were obviously much lower; this was regarded as illegal direct state aid by the EU Commission, which nevertheless subsequently proceeded to allow it (German Ministry of Finance, 2013). Later, a bad bank took over most toxic loans and the remaining parts of *WestLB* were liquidated. For many other state banks, it is evident that they behaved hazardously when investing in American asset-backed securities, often encouraged and poorly supervised by politicians who represented the respective states on the banks' boards Hallerberg and Markgraf (2018) provide an examination of political influence on German state banks before the crisis which resulted in bad supervision and risky behaviour; Traut (2017) examines the way in which three state banks (Sachsen LB, HSH Nordbank, and BayernLB) came to be in crisis and finds major shortcomings in risk management and reactions to warnings as well as outright moral hazard. This hints at highly distorted incentives prior to the crisis and insufficient supervision from German government entities that resulted in great interventions and high costs for taxpayers.

The list could be extended much further: names like *Hypo Real Estate or Commerzbank* are still strongly associated with the crisis, and obligations from bank rescues have not yet disappeared yet. This becomes clearer when looking at indicators for the aggregated involvement of government entities in supporting the financial sector through several agencies and state-owned firms. Figures 1.1-1.3 show how much Germany invested into saving its banks by becoming a shareholder of banks or their asset management companies (bad banks), taking over debt from struggling banks

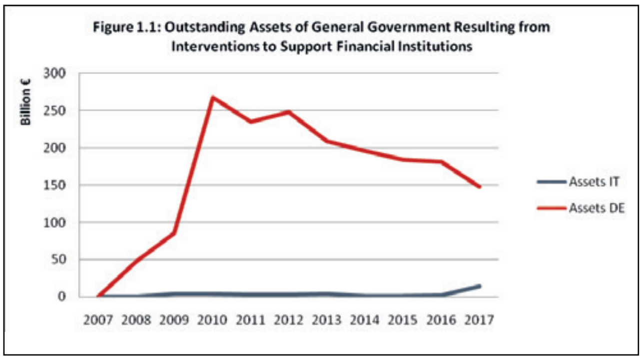
1 US mortgages to dubious borrowers were bundled and sold all over the world under the assumption that losses from some mortgages would be outweighed by profits from others – they were not.

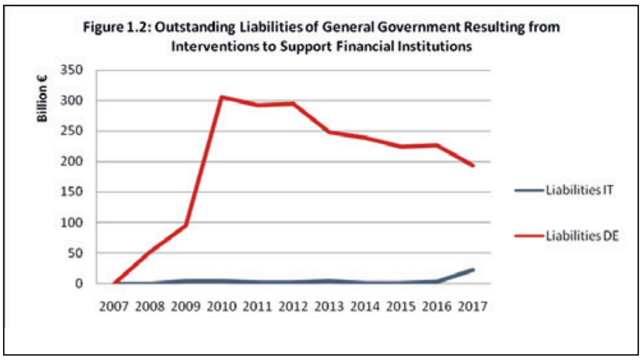
(often correlated with becoming a shareholder, which explains the similar curves in Figures 1.1 and 1.2), or giving out guarantees for bank debts, which are contingent liabilities (Figure 1.3). German involvement in rescue operations started quickly in 2007 and stopped growing in 2009 when the international financial markets were stabilised. Since then, new state intervention has not been required.

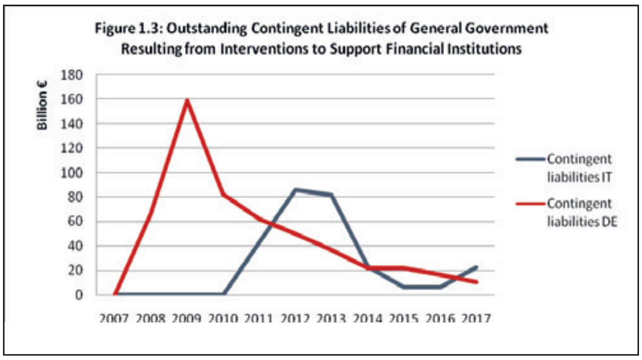
The sheer size of the rescue packages needed during the GFC reveals the immense problems in the German banking sector. These problems certainly required a reaction by regulators and changes in the regulatory framework. Especially in the cases of the failures of banks with potential systemic importance such as *Commerzbank or Hypo Real Estate*, state aid was unavoidable, which included compensation for the shareholders and the non-participation of the bondholders in the rescue operations. This was mostly due to lack of rules that facilitated investor liability. Those who made giant profits from risky bank investments in the past were bailed out and only suffered minor losses (Reiermann & Reuter, 2009). Simply to avoid future hazardous behaviour on the part of banks, it was important to set up a framework in which every bank can fail and which makes actual holders of stocks and bonds responsible for controlling the bank's activities and bearing the consequences if they fail to do so.

A credible bank resolution framework was probably among the most important consequences of the crisis. As soon as banks can be treated almost like normal firms that can go bankrupt if they make bad investments, more disciplined behaviour and more supervision by investors will follow. Furthermore, the quick crisis resolution in Germany and the following economic boom as well as the general structure of German investors (usually, normal citizens do not invest substantial amounts of their life savings into bank bonds or shares) resulted in a truly fresh start for investment in banks, as investors could adjust their expectations and investment behaviour to the new environment. A new framework could be introduced in which supervision might work better and risk and return are actually connected (European Commission, 2014). Given the German experience and the state of its economy, a new resolution regime seems like an adequate measure to foster financial stability.

Figure 1: Assets (e.g., equity in banks), liabilities, and contingent liabilities (e.g., guarantees) resulting from supporting financial institutions in Germany and Italy (Eurostat, 2018).







Italy: a Hidden Banking Crisis

The Italian crisis experience was quite different from the German one. As already indicated by the numbers on government involvement in the financial sector in Figure 1, Italy did not intervene heavily in the markets early on. While the displayed numbers show almost no support for banks, it is important to recognise that the government did indeed give out a guarantee for insured deposits to avoid a bank run in case the depositors lost trust. Furthermore, guarantees for some types of bank liabilities were announced and banks were partially shielded from losses from non-financial sector lending. The Italian government had also prepared instruments to recapitalise struggling banks (OECD, 2009). However, these measures were much less specific than the German ones, since German banks actually failed in the period 2007 to 2009 due to high exposure to toxic assets, while Italian banks were much less exposed to turmoil on international markets. As the OECD stated, "[t]he Italian financial system managed to cope with the 'first round' of the crisis better than most of its European peers […]" (OECD, 2009, p. 37) and mostly suffered due to spill-over effects that reduced confidence in banks and increased funding costs. The measures taken by the Italian government mostly aimed at reducing such burdens for Italian banks.

The Italian banking sector was apparently kept in rather good shape by regulators prior to the GFC. Two examples illustrate this: first, the general regulatory attitude towards the risk-taking of banks was relatively strict in Italy (Laeven & Levine, 2009). Especially regarding the factors that were among the determinants of the GFC, Italian regulators were exceptionally prudent. Regulators for different types of financial firms collaborated and closed loopholes that banks could have used to avoid regulation. [2] Shifting loans outside a bank's balance sheet – a measure to reduce capital requirements – was much harder in Italy than, for example, in Germany. Italian regulators were also well-informed about potential risks to bank assets, because they collected much more data than international standards would have required (OECD, 2009). Regulators basically prevented Italian banks from holding assets that later turned out to be toxic. Second, Hallerberg and Markgraf (2018) show that especially (semi-) state banks in Italy were relatively well-managed and were efficiently supervised before the GFC. This stands in stark contrast to the management and supervision of, for example, German state banks.

The problems for Italian banks came later, when many other countries had already consolidated their financial sectors or were in the process of doing so. As we can also see in Figure 1, Italy eventually intervened to support its banks when the economic crisis – the second phase of the GFC in Europe – became an unbearable burden for some banks. This economic crisis was partially caused by funding and liquidity problems for banks, which resulted in tightened credit conditions for firms which relied on financing from banks (OECD, 2009); however, as a trade-dependent economy, Italy was also highly affected by the world-wide economic downturn. Furthermore, larger Italian banks suffered from exposure to Eastern European markets, which suffered great economic turmoil as international credit conditions tightened (Di Quirico, 2010). Support for domestic banks became necessary in the course of this economic crisis whenever more bank loans to local businesses became non-performing and the credit-crunch – the unavailability of credit for businesses – worsened.

It is important to stress again that the Italian crisis was fundamentally different to that of other countries: while banks and bursting bubbles brought the world economy to the brink of chaos, Italian bank troubles were rather the result of these worldwide problems. The Italian economic downturn and its banking crisis went hand in hand, while the GFC preceded the worldwide economic problems. Italian banks had to reduce credit as a

2 Such efficient collaboration between regulators was an exception in major economies. See Barth, Caprio & Levine (2012) for a detailed discussion on how regulators in industrial countries had the powers and resources to efficiently supervise banks prior to the GFC, but did not use them and failed to cooperate efficiently.

result of financial market turmoil and a lack of liquidity in the period 2007 to 2009. The highly leveraged Italian corporate sector could not cope with the resulting credit-crunch and the general economic downturn. [3] As a result, it now accounts for 80 per cent of Italian banks' non-performing loans (NPLs), reflecting a long-lasting recession as well as a reluctance on the part of banks to write off NPLs (Jassaud & Kang, 2015).

The economic crisis in Italy eventually lasted much longer than the recessions in other Euro countries, with the resulting NPL problems producing a slow-motion banking crisis. Shortly after the SRM regulation took effect in January 2016, Italian banks ran into trouble when their funding and liquidity positions eroded in the course of the ongoing NPL crisis. The smaller banks *Banca Popolare di Vincenza* and *Veneto Banca* tried to prevent liquidation through loopholes in the banking resolution directive, but their limited size prevented this. They were eventually sold in 2017 under Italian insolvency law, including substantial state guarantees on the liquidation mass (European Commission, 2017a). The common resolution regime was not used in this case; an important feature of the liquidation of the two Italian banks was that senior bonds were protected from losses as well as small savers' junior bonds – partially financed by the Italian state (Humblot, 2017). Hence, the promise that taxpayers would not pay for bank failures was not kept. The liquidation of a failing bank using state guarantees and other instruments of state aid to facilitate liquidation very much recalls the German reaction to the failure of *SachsenLB* – a German state bank that failed in the early days of the GFC in 2007 due to unreasonably high exposure to risky US assets.

Much more important, however, is probably the case of *Monte dei Paschi di Siena* (MPS), [4] which enjoyed precautionary recapitalisation. MPS had failed to collect enough money from private investors to meet the requirements of the EU-wide bank stress test, which is supposed to ensure adequate capitalisation of major banks. The bank, just like the two smaller banks, requested precautionary recapitalisation to solve this problem. In mid-2017, it was found that MPS as the country's fourth-largest bank was important enough and at the same time generally solvent so that recapitalisation was feasible under the loopholes in the new resolution rules. After shareholders and junior bondholders contributed 4.3bn € to its rescue, the Italian state contributed more than 5bn € to the bank's capital in exchange for shares (European Commission, 2017b). Again, senior bondholders did not participate in the bail-in prior to the government bail-out. It is not very far-fetched to say that this state intervention again recalls German reactions to its own banking crisis; this time, it looks quite similar to the rescues of *IKB* or *Commerzbank*.

Estimates show that the two Italian regions mostly affected by the bank turmoil, the Veneto and Tuscany, saw a substantial decline in business lending of 6 per cent and 3 per cent respectively in 2016, while similar regions do not show such patterns (Zingales, 2017). Rome could only choose between great turmoil on financial markets as a result of non-interventionist resolution of struggling banks (leading to a credit-crunch which already induced the economic crisis that had caused these troubles) or finding loopholes to intervene in the banking crisis to resolve the problem smoothly. Discretionary intervention would have been a viable choice in 2007, but now the Italian government faced a different regulatory environment.

3 Germany strongly supported its industry in replacing international demand by domestic public spending. While these efforts were successful, they were also classic Keynesian measures and had little to do with Germany's celebrated model of *Ordnungspolitik*– a concept that relies on rules and rejects discretionary intervention in markets. Perhaps, one could say that Italy behaved in a more "German" way than Germany during the crisis.

4 MPS had also faced major difficulties before and had already been a burden for financial stability for years. For example, it managed to circumvent regulators in some cases and lost hundreds of millions in the GFC due to risky transactions. It also had to be supported by the state in 2012 when it failed to raise enough capital to meet stricter European capital requirements (Thompson, 2013).

The ownership structure of bonds and the potential losers of non-intervention eventually made this a non-choice. Italian households are traditionally among the most important buyers of bank bonds for investment purposes, exposing the most vulnerable economic players to great economic pain in the event of resolution. This is partially due to an under-developed pension fund sector (which would then pool savers' money) and tax incentives that favour bonds over deposits (Grasso, Linciano, Pierantoni & Siciliano, 2010). Banks obviously had an interest in selling bonds that secured their own funding and Italians were willing to buy them. Italian households' bond ownership was 200 million € in 2017 – four times higher than that of German households (Barbera, 2017). Letting senior bondholders participate in recapitalisations would have meant expropriating citizens who had invested into allegedly safe assets. Their long-running investments were supposed to pay for their pensions or other big plans and could not simply be sold to investors at a low price to get out of the business after the rules were changed externally. Hence, Rome basically had no choice but to circumvent the new rules.

Despite its own interventions in similar cases, the German government heavily opposed any state aid by the Italian government under the new resolution framework. German politicians and government officials condemned all government efforts to cushion the Italian banking crisis and to protect senior bondholders. It was argued that the new resolution framework was circumvented on the first occasion and that the European authorities should not have allowed state guarantees to facilitate the liquidation of the two smaller banks, nor the precautionary recapitalisation for *MPS*. A conservative German MEP was quoted in the *Financial Times* a few days prior to the eventual MPS decision with the statement: "the promise that the taxpayer will not stand in to rescue failing banks any more is broken for good" (Brundsen, 2017). The same article spoke of "outrage among German politicians" that rules introduced after the GFC had been undermined.

The future of the Italian banking system remains uncertain. Italy's quantity of NPLs is still the highest in Europe in absolute numbers (*The Economist*, 2017). The government in Rome seems to lack the power and resources to solve the NPL problem in due time; the new all-populist government will probably make it even more difficult to convince investors to relieve banks of NPLs at reasonable prices. For the foreseeable future, European regulation and political constraints (including the reluctance of northern countries to enter risk-sharing schemes) make it unlikely that the NPL crisis can be resolved without harming Italy's economy or investors – among them, many normal citizens saving for their retirement.

Bail-in, Bail-out, and How Double-Standards Hurt Everyone

Both data and anecdotal evidence on government intervention during recent banking crises as well as on banking supervision show major differences between Germany and Italy. Italy did relatively well in terms of banking supervision and regulation prior to the crisis. Nevertheless, a long-lasting economic downturn brought its banks into serious trouble. This economic downturn was a result of the global financial crisis of the period 2007 to 2009 and resulted in huge amounts of non-performing loans on bank books. In contrast, Germany's banks were much more exposed to the initial financial crisis and partially caused it. This required early and severe government intervention by government entities. Figures 1.1-1.3 show that the magnitude of these interventions exceeded Italian state aid for its banks by far. When Italy's banks needed state aid, the German crisis had already been resolved and its government had started working on preventing such events in the future.

A consequence of Germany's early intervention was that its banks' balance sheets were relatively clean when the financial crisis turned into a European economic crisis. This stands in contrast to the Italian experience where bank balance sheets turned sour over the years, resulting in a slow-motion banking crisis. This Italian banking crisis overlaps with the introduction of EU rules to address the reasons for the last financial crisis, including a new resolution regime that was supposed to prevent government interventions with taxpayer money to save banks. In Germany, these rules were introduced in a more or less stable environment and it seems reasonable to assume that market participants could change their behaviour accordingly. This would be in line with the goals of introducing the new resolution regime: reducing incentives for moral hazard by banks and their investors, and making them liable for their mistakes.

Thus, the outrage of German politicians about state aid for Italian banks in 2017 is understandable from their point of view: it hurts the credibility of the newly introduced resolution regime that was supposed to prevent interventions like the one conducted by Germany in the GFC. As argued before, credibility is key to change the future behaviour of banks and investors as well as to make resolution feasible at all. It is perfectly reasonable for a German government that just cleaned up its banking sector to want to change the rules as long as no new problems have emerged that might require new intervention.

It is problematical, however, to impose such rules on Italy for the same reason. As argued before, the Italian banking crisis evolved from an economic crisis and hit much later. In contrast to Germany in the period 2007 to 2009, Rome's hands to resolve its own crisis on the banking market from 2016 onwards were bound by the new regulatory regime introduced in 2014-16. The Italian government could not react to a crisis of its banks as Berlin had done. Yet, the Italian economic crisis had been caused by the worldwide economic downturn and resultant market turmoil from the GFC; one can very well say that these crises belong together and cannot be regarded separately.

The timing aspect is key to understand the flaws of the new system and the need to circumvent them. One cannot change incentives retrospectively. The new rules can only work when they are introduced in a relatively stable environment in which new investment patterns can emerge; Germany was apparently at such a stage after heavily intervening in the markets. Italy did not intervene in its markets so much, and suffered a slowly evolving crisis based upon an economic crisis. Consequently, Italy was not ready for the new rules when they were introduced, and investors could not react appropriately.

One could very well accuse the Italian governments of recent years of doing too little against the economic crisis that then resulted in the Italian banking crisis; they certainly also failed to work on the NPL problem (Zingales, 2017). Especially during the major downturn of the world-economy in the period 2008-10, Berlusconi's right-wing government reacted much more timidly compared to Britain's centre-left government or Germany's centrist grand coalition. Italy rather stuck to the general European rules of non-intervention, while its peers conducted classic Keynesianism. Neoliberal Britain, as well as Germany with its tradition of Ordnungspolitik, faced great trouble during the GFC and did not stick to their principles. In contrast, traditionally interventionist Italy acted in a restrained way and adhered more to the principles of prudence and order, at least with regard to banking supervision, and did not have to intervene. The Italian government clearly did not conduct "rogue policies" or moral hazard that led to failing banks prior to the crisis, nor did financial firms in general. Instead, it was the economic environment that caused problems on the Italian banking market.

It is not without irony that Italy adhered to northern European principles for too long. This does not mean that it was intelligent to do so, nor does it mean that the Italian economy was in exceptionally good shape prior to the crisis, of course.

The introduction of the European resolution regime had two purposes: the economic one was to change the future incentives of banks and their investors in order to reduce the risk of banking crises; the political one was to show voters that no more tax money would be used for bank rescues. Premature implementation prior to all the affected banking markets being cleaned up probably mainly served the political purpose, but this happened at the cost of the economic one. Since current regulation cannot change past incentives, solutions had to be found to deal with the impact of the new rules on old investors. This corrupted the credibility of the system, thereby certainly harming the economic purpose of these rules for the foreseeable future as well as probably harming the political signal in general.

Bibliography

Barbera, A. (2017, July 19). "We warned Italy in 2014 about risks for banks." La Stampa. Turin. Retrieved from http://www.lastampa.it/2017/07/19/esteri/lastampa-in-english/enria-eba-we-warned-italy-in-about-risks-for-banks-ZqtCBNa7Yp1dPEtxY5CHWI/pagina.html.

Barth, J. R., Caprio, G., & Levine, R. (2012). Guardians of Finance : Making Regulators Work for us. Boston MA: The MIT Press.

Brundsen, J. (2017, June 26). "Berlin leads backlash against Italian bank rescue." The Financial Times. London. Retrieved from https://www.ft.com/content/71ece778-5a53-11e7-9bc8-8055f264aa8b.

Di Quirico, R. (2010). Italy and the Global Economic Crisis. Bulletin of Italian Politics, 2(2), 3-19. Retrieved from https://www.gla.ac.uk/media/media_191024_en.pdf.

European Commission. (2014). Umfassende Reaktion der EU auf die Finanzkrise: Wichtige Schritte in Richtung solider Rahmenbestimmungen für den Finanzsektor in Europa und einer Bankenunion für den Euroraum. Retrieved 10 June 2018, from http://europa.eu/rapid/press-release_MEMO-14-244_de.htm.

European Commission. (2017a). Staatliche Beihilfen: Kommission genehmigt Beihilfe für den Marktaustritt der Banca Popolare di Vicenza und der Veneto Banca gemäß dem italienischen Insolvenzrecht, einschließlich des Verkaufs einiger Teile von Intesa Sanpaolo. Retrieved 6 June 2018, from http://europa.eu/rapid/press-release_IP-17-1791_de.htm.

European Commission. (2017b). Staatliche Beihilfen: Kommission genehmigt vorsorgliche Rekapitalisierung der italienischen Bank Monte dei Paschi di Siena (MPS). Retrieved 6 June 2018, from http://europa.eu/rapid/press-release_IP-17-1905_de.htm.

European Union. RICHTLINIE 2014/59/EU DES EUROPÄISCHEN PARLAMENTS UND DES RATES vom 15. Mai 2014 zur Festlegung eines Rahmens für die Sanierung und Abwicklung von Kreditinstituten und Wertpapierfirmen (2014). Brussels: European Parliament & Council of the European Union. Retrieved from https://eur-lex.europa.eu/legal-content/DE/TXT/PDF/?uri=CELEX:32014L0059&from=DE.

European Union. VERORDNUNG (EU) Nr. 806/2014 DES EUROPÄISCHEN PARLAMENTS UND DES RATES vom 15. Juli 2014 zur Festlegung einheitlicher Vorschriften und eines einheitlichen Verfahrens für die Abwicklung von Kreditinstituten und bestimmten Wertpapierfirmen im Rahmen eines e (2014). Brussels: European Parliament & Council of the European Union. Retrieved from https://eur-lex.europa.eu/legal-content/DE/TXT/PDF/?uri=CELEX:32014R0806&from=DE.

Eurostat. (2018). Ergänzende Tabellen zu öffentlichen Interventionen zur Unterstützung von Finanzinstitutionen - Eurostat. Retrieved 29 May 2018, from http://ec.europa.eu/eurostat/de/web/government-finance-statistics/excessive-deficit/supplemtary-tables-financial-crisis.

Fecht, F., Grüner, H. P., & Hartmann, P. (2012). "Financial integration, specialization, and systemic risk." Journal of International Economics, 88 (1), 150-161. Available at: https://doi.org/10.1016/j.jinteco.2012.01.012.

German Ministry of Finance. (2013). Bundesfinanzministerium - Fünf Jahre Finanzmarktstabilisierungsfonds unter dem Dach der Bundesanstalt für Finanzmarktstabilisierung. Retrieved 29 May 2018, from https://www.bundesfinanzministerium.de/Content/DE/Monatsberichte/2013/12/Inhalte/Kapitel-3-Analysen/3-6-fuenf-jahre-finanzmarktstabilisierungsfonds.html.

Grasso, R., Linciano, N., Pierantoni, L., & Siciliano, G. (2010). Bonds Issued by Italian Banks: Risk and Return Characteristics (Working Papers No. 67). Rome. Retrieved from http://www.consob.it/documents/46180/46181/qdf67en.pdf/e22656a7-738a-4205-8912-3cb0e6254057.

Hallerberg, M., & Markgraf, J. (2018). "The Corporate Governance of Public Banks Before and After the Global Financial Crisis." Global Policy, 9, 43-53. https://doi.org/10.1111/1758-5899.12562.

Handelsblatt. (2008). Fehlspekulationen: Koalitionsspitzen billigen Rettungspaket für IKB. Retrieved 29 May 2018, from www.handelsblatt.com/politik/deutschland/fehlspekulationen-koalitionsspitzen-billigen-rettungspaket-fuer-ikb/2927418.html?ticket=ST-2721244-TXkdeP70FwJwZKoexppn-ap1.

Hellwig, M. (2017). Precautionary Recapitalisations: Time for a Review. Brussels. Retrieved from http://www.europarl.europa.eu/RegData/etudes/IDAN/2017/602089/IPOL_IDA(2017)602089_EN.pdf.

Humblot, T. (2017). Italy: liquidation of Veneto Banca and Banca Popolare di Vicenza. Paris. Retrieved from http://economic-research.bnpparibas.com/Views/DisplayPublication.aspx?type=document&IdPdf=30109.

Jassaud, N., & Kang, K. (2015). A Strategy for Developing a Market for Nonperforming Loans in Italy A Strategy for Developing a Market for Nonperforming Loans in Italy Authorized for distribution (IMF Working Paper No. WP/15/24). Washington. Retrieved from https://www.imf.org/external/pubs/ft/wp/2015/wp1524.pdf.

Krugman, P. (2010, April 1). "Financial Reform 101." The New York Times. New York. Retrieved from https://www.nytimes.com/2010/04/02/opinion/02krugman.html.

Laeven, L., & Levine, R. (2009). "Bank Governance, Regulation and Risk Taking." Journal of Financial Economics, 93 (2), 259-275. https://doi.org/10.1016/j.jfineco.2008.09.003.

OECD. (2009). OECD Economic Surveys: Italy 2009 (OECD Economic Surveys: Italy). Paris: OECD Publishing. https://doi.org/10.1787/eco_surveys-ita-2009-en.

Reiermann, C., & Reuter, W. (2009, February 2). "The State's Silent Takeover: Germany's Big Banking Bailout." Der Spiegel. Hamburg. Retrieved from http://www.spiegel.de/international/business/the-state-s-silent-takeover-germany-s-big-banking-bailout-a-605044.html.

The Economist. (2017). "Going South." The Economist, 68.

Thompson, M. (2013, January 29). "Scandal at world's oldest bank." CNN Money. London. Retrieved from http://money.cnn.com/2013/01/29/news/economy/italy-banking-scandal/index.html.

Traut, F. (2017). The Failures of German Landesbanken in the Financial Crisis: Micro-Reasons and Internal Dynamics. Hertie School of Governance. Retrieved from https://sites.google.com/site/frederiktraut/research.

Zingales, L. (2017). "Italy's non-existent bank rescue strategy." Retrieved 10 June 2018, from http://www.italy24.ilsole24ore.com/art/business-and-economy/2017-02-24/italy-s-non-existent-bank-rescue-strategy--165915.php?uuid=AE3n0xc.

COMPARING THE GERMAN AND ITALIAN APPROACHES TO BANKING UNION

Lucia Quaglia
University of Bologna

1. Introduction

The establishment of a Banking Union represented a major development in European economic governance and European integration history more generally. The Banking Union was the main response of the European Union (EU) - to be precise, the euro area - to the sovereign crisis in the euro area periphery and the ensuing fragmentation of the financial markets in the euro area (Donnelly 2014; De Rynck 2015; Epstein and Rhodes 2016; Glöcker et al. 2016; Howarth and Quaglia 2016a,b; Nielsen and Smeets 2017; Schaeffer 2016; Schimmelfennig 2016; Skuodis 2017). The Banking Union, as initially proposed by the so-called "Four Presidents' Report" (Van Rompuy 2012), was supposed to break the "vicious circle" between ailing banks and fiscally-weak sovereigns, elevating the "responsibility for supervision to the European level", and providing for "common mechanisms to resolve banks and guarantee customer deposits". Moreover, the European Stability Mechanism (ESM) was to "act as the fiscal backstop to the resolution and deposit guarantee authority". Hence, the Banking Union was to be based upon four pillars: single banking supervision, single banking resolution, common deposit guarantee scheme, and common fiscal backstop.

This paper compares the approaches of Germany and Italy to the Banking Union by focusing on their preferences concerning each of the four main components of the Banking Union. It is argued that German and Italian policy-makers had different views concerning the construction of the Banking Union, its purposes and its institutional design. These dissimilar visions for the Banking Union had partly to do with different underlying sets of interests in the two countries, but it can also be ascribed to different economic cultures (or ideas) concerning macroeconomic governance in the euro area and the completion of Economic and Monetary Union. It is, however, important to point out that both Germany and Italy were internally divided (*i.e.*, had different domestic preferences) on some of the issues at stake.

2. The Negotiations on the Construction of the Banking Union

The main purpose of the Banking Union was to break the dangerous link (the so-called "doom loop") between the high and rising sovereign debt in the euro area peripheral Member States and domestic banks, which had come to hold an increasing amount of this debt (Veron 2012). At the same time, the Banking Union was an attempt to address the increasing fragmentation of financial markets in the EU, which was a consequence of the crisis. Banks reduced their cross-border activities, and the cost of money (e.g., the interest rate paid on bank loans) also varied considerably across the Member States of the euro area. In turn, this disrupted the conduct of the single monetary policy of the European Central Bank (ECB) (Howarth and Quaglia 2016).

In June 2012, the President of the European Council, the President of the Eurogroup, the President of the Commission, and the President of the ECB, prepared an interim report entitled "Towards a Genuine Economic and Monetary Union" (Van Rompuy 2012), the above-cited "Four Presidents' Report" or Van Rompuy Report. The report, which was discussed at the European Council and Eurogroup meetings in late June, proposed what later became known as the Banking Union. However, the most pressing issues discussed at the Council meetings concerned the possibility of using the ESM directly to re-capitalise ailing Spanish banks, rather than doing so indirectly, that is to say, *via* a loan to the Spanish government, which would have weakened the already fragile fiscal position of Spain. Spanish and Italian policy-makers were the main supporters of direct re-capitalisation by the ESM (*Financial Times,* 29 June 2012). Reluctantly, German policy-makers agreed to it, but posed, as a condition, the supranationalisation of banking supervision by transferring it to the ECB (*The Economist*, 29 June 2012). Consequently, the Member States asked the Commission to put forward legislative proposals for the establishment of the Single Supervisory Mechanism (SSM) (Euro summit 2012). Subsequently, German policy-makers reneged on their commitment to allow the ESM directly to recapitalise banks (*Financial Times*, 18 October 2012).

Two legislative proposals concerning the establishment of the SSM were prepared by the Commission in close collaboration with the ECB (Nielsen and Smeets 2017; Glocker et al. 2016) and were officially put forward in September 2012. During the negotiations on the SSM, the most controversial issues concerned the distribution of supervisory power between the ECB and the competent national authorities. The Commission's proposal, which was also supported by France, Italy and Spain, envisaged the direct supervision of all euro area banks in the SSM by the ECB. The ECB (2012) issued an opinion, supporting the proposal and calling for a Single Resolution Mechanism (SRM) to complement the SSM. However, German policy-makers opposed the transfer of supervisory competences for the country's regional public savings banks and co-operatives to the ECB (*Financial Times*, 12 December 2012). The institutional design of the SSM eventually agreed by the Member States in the European Council (2012) involved a compromise that took the German preferences into account. Thus, the ECB was to be "responsible for the overall effective functioning of the SSM" and the "oversight of the euro area banks". This supervision, however, was to be "differentiated" and the ECB would carry it out in "close co-operation with national supervisory authorities". Direct ECB supervision was to cover only the so-called "significant banks", while thousands of smaller, so-called "less significant" banks would continue to be under the direct supervision of the national competent authorities, albeit according to increasingly harmonised rules and practices. Moreover, the ECB was permitted to step in, by taking direct supervisory responsibilities, if and when necessary (Howarth and Quaglia 2016b).

The regulation on the SRM was proposed by the Commission in July 2013. Most of the negotiations concerned the scope of the SRM, the decision-making process in the Single Resolution Board (SRB), and the establishment of the Single Resolution Fund (SRF). The Commission, supported by French, Spanish and Italian policy-makers, proposed that the SRM should cover all euro area banks and that the Commission should be given the final power to decide whether to place a bank in resolution and determine the application of resolution tools (*Financial Times*, 10 July 2013). These policy-makers were also in favour of a timely setting up of a large SFR. For example, Treasury Minister Fabrizio Saccomanni (2013) sent a letter to the other EU finance ministers stressing that, in order "to break the nexus" and "reduce the risk of contagion", the system had to rely on "common financial resources". By contrast, German policy-makers argued that the SRB should be given the power to decide on resolution, and insisted on the setting up of a small SRF through an intergovernmental agreement (*Financial Times*, 8 November 2013). The ECB, the Commission and the European Parliament (EP), mainly challenged the German position. The ECB (2013) issued a 32-page opinion that the SRB should be, from the very start, a single "strong and independent" body. In order to move the negotiations forward, the Eurogroup and Ecofin (2013) issued a statement that made it clear that the SRM should be "fiscally neutral over the medium term so that taxpayers will be protected".

In March 2014, an agreement was reached in the Council of Ministers on the establishment of the SRM. As advocated by German policy-makers, the Commission's proposal was modified: the SRB would be responsible for the planning and resolution of cross-border banks and those directly supervised by the ECB, while national resolution authorities would be responsible for all other banks, except if or when a bank required access to the SRF. However, it would be possible for the SRB to decide to exercise its powers directly with regard to other banks. Under German insistence, the SRF, financed by bank levies raised at national level, was to be set up through an intergovernmental agreement (Schild 2017). It would initially consist of national compartments that would be gradually merged over a period of eight years. German policy-makers - joined by the Austrian, Dutch and Finns - insisted that the funds of the ESM - as a backstop of the SRF - could not be used to cover legacy problems, which was to be revealed by a comprehensive assessment of euro area banks by the ECB (Howarth and Quaglia 2016a), as elaborated below. The SRM regulation was adopted in conjunction with the Bank Recovery and Resolution Directive (BRRD), which harmonised resolution instruments and powers in the EU. The BRRD and the SRM regulation introduced a new instrument in bank resolution, the bail-in, which substantially reduced the need for public funding to bail out banks (Nielsen and Smeets 2017). The German-led coalition insisted on an earlier entry into force of the bail-in than the originally envisaged date in 2018. Other policy-makers, especially from Italy (Visco 2016), resisted this, but to no avail. The start date for the entry into force of the bail in was eventually moved forward to 2016 (*The Economist*, 14 December 2013).

The other missing pillar of the Banking Union, beside the common backstop, was what later came to be known as the European Deposit Insurance Scheme (EDIS) (see Gros and Schoenmaker 2014). In June 2012, the interim Van Rompuy (2012) report mentioned the need to set it up. Subsequently, the Commission prepared a draft proposing a new agency, the European Deposit Insurance and Resolution Authority (EDIRA), which would oversee a new European Deposit Guarantee and Resolution Fund (*Financial Times*, 13 September 2012). However, due to German opposition, the proposal for the EDIRA was removed from the final Commission document "A Roadmap Towards Banking Union" (2012). German policy-makers and German banks feared that they would probably become net contributors to an EDIS - bailing out depositors in other euro area Member States (Donnelly 2014; Howarth and Quaglia 2016a; Schimmelfennig 2016; Schild 2017). German banking associations and individual banks also feared that an EDIS would impinge upon their sectoral institutional protection schemes (*Handelsblatt*, 7 November 2012). By contrast, policy-makers in France and in the euro area periphery regarded the EDIS as the final pillar of the Banking Union, necessary to sever the "doom loop" between banks and sovereigns (*Reuters*, 11 September 2015).

The issue came back on the policy agenda in June 2015, when the "Five Presidents' Report" on the future of the euro called for an EDIS (Juncker 2015). In the autumn of 2015, the Commission proposed the EDIS as "the third pillar of the Banking Union" (Commission 2015). The Commission proposal would, as a first step, involve the establishment of a mandatory "reinsurance"' scheme that would "contribute under certain conditions when national deposit guarantee schemes are called upon", and thus, in effect, act as a backstop to national deposit guarantee schemes. The proposal was supported by French, Italian and Spanish policy-makers. By contrast, the German finance minister, Wolfgang Schäuble strongly criticised the proposal: his concern was that "German taxpayers" would have to "foot the bill" (*Financial Times*, 10 September 2015). In order to make progress on the EDIS and overcome German opposition, the Commission proposed that savings and co-operative banks be exempted from having to contribute to the EDIS (*Reuters*, 2 November 2015).

In June 2017, the Governor of the Bank of Italy, Ignazio Visco, and Treasury Minister Pier Carlo Padoan renewed their calls for a common deposit guarantee scheme (*Bloomberg*, 23 June 2017). Nonetheless, given the *impasse* reached in the negotiations on the EDIS, due to strong opposition from Germany, the Commission discarded its earlier proposals for fully-fledged EDIS in the autumn of 2017 (Howarth and Quaglia 2018). Trying to establish some common ground between the positions of the two coalitions, the President of the ECB Mario Draghi argued before the EP that the "EDIS remains a fundamental pillar of Banking Union", although "risk reduction and risk sharing should go in parallel", thus "there cannot be an EDIS if the level of unpaid bank loans [mostly in the euro area periphery] is not reduced" (*Reuters*, 20 November 2017).

Overall, the Banking Union was established in timely fashion between 2012 and 2014. However, it was incomplete and hence asymmetric in three main respects. First, a rather "complex" compromise was reached concerning the resolution process in the SRB, and Member State governments retained an important say on the use of the resolution funds in the SRM. Second, a common deposit guarantee scheme was not set up. Third, no common fiscal backstop was established. Most of the intergovernmental negotiations basically boiled down to distributional conflicts on two dimensions: the centralisation of decision-making, and the allocation of costs via risk-sharing (Schild 2017). The discussions pitted the countries expected to make net contributions to common rescue funds - either from taxpayers or from banks - against those that expected to be the principal recipients. Thus, compromises were sought during the negotiations. The institutional design eventually agreed for the Banking Union was closer to the preferences of the German led-coalition as far as risk-sharing was concerned, whereas Germany had to make concessions concerning the transfer of decision-making to the EU/euro-area level (Skuodis 2017). The result was an incomplete and asymmetric Banking Union, which was rather different from the one initially envisaged: out of the four pillars initially proposed, only one and a half were set in place (supervision and resolution, respectively).

3. Economic Interests and Ideas Concerning Banking Union in Germany and Italy

The construction of the Banking Union was characterised by the need to reconcile different national sets of interests and ideas concerning macroeconomic governance. At the risk of over-simplifying, the main line of division was between the Northern (German-led) coalition and the Southern coalition, with France in-between, but overall closer to the Southern coalition.

Germany policy-makers, like the policy-makers from Austria, Finland and The Netherlands, shared similar interests: they had sound fiscal positions; they had mostly healthy banks; and they were likely to be net contributors to any mechanism for financial support in the Banking Union. However, the German approach was also shaped by the ordo-liberal economic paradigm. The German authorities were particularly concerned about "moral hazard" - that is to say, not to provide incentives for any "risky" behaviour of sovereigns and banks – or for "legacies problems" derived from past "supervisory forbearance" (Schild 2017; Schaeffer 2016).

The argument of moral hazard featured prominently in the German debate (2014). Even though the term, as such, was not regularly used by most German policy-makers, Finance Minister Wolfgang Schäuble used it both to justify the transfer of supervisory power over banks receiving aid from the ESM (*New York Times*, 18 November 2011) and to oppose the creation of the Common (DGS) (*Financial Times*, 8 December 2015). More generally, the fear of moral hazard was implicit in talk of fiscal transfers. Moral hazard was of great concern for policy-makers in some countries, notably Germany, that were less likely to need financial support in the Banking Union because their banking systems were in sufficiently rude health and/or because these governments had a sufficiently strong fiscal position that would enable them to withstand real and potential bank losses.

There were several moral hazards that preoccupied the German government: for bank shareholders, bondholders, and depositors; for the banks themselves; and for governments. Thus, policy-makers in Germany sought to establish clear limits to their financial assistance to ailing banks and governments in countries hit by the sovereign debt crisis. They were also keen to minimise the elements of the Banking Union that could result in fiscal transfers from fiscally and financially stable Member States to ailing Member States. Thus, Germany was keen to supra-nationalise banking supervision for systemic banks – an important qualification for Germany, given the three-pillared configuration of its national banking system - but opposed mechanisms for financial support to ailing banks and their sovereigns (Howarth and Quaglia 2016b). German concerns about moral hazard help to account for the limited scope of the SRM agreed upon, the delay to an agreement on a Common DGS, and the limited amount of ESM funds made available and the strict conditionality attached to their use. A core element of the German political discourse on the Banking Union was that (German) taxpayers should be protected against all future public bail-outs of banks (Schild 2015).

Germany was the largest economy in the euro area, and had a sizeable current account surplus and a sound fiscal position. Consequently, Germany had a strong bargaining position resulting from asymmetric interdependence (Schild 2017). It was the pivotal country, the "win set" of which determined what was acceptable (or not) in the negotiations on the Banking Union. This explains why the compromise solutions were generally within the win-set of Germany on several (but not all) issues, and why the institutional design of the Banking Union had a German "imprint". German policy-makers enjoyed a "constrained veto power" in the construction of Banking Union (Bulmer 2016; Bulmer and Patterson 2013) because German and French banks were heavily exposed (*i.e.*, they had invested substantially) in the EU/euro periphery. Moreover, Germany had a stake in the survival of the euro area, which was at risk of losing Member States and even falling apart following the sovereign debt crisis. Indeed, the prospect of a euro area collapse was worrisome for all its members, Germany included. Hence, German policy-makers were willing to proceed - albeit with some reluctance - with the Banking Union.

Yet, countries were not "unitary actors" in the negotiations on the Banking Union because they often had different (even competing) domestic political economy preferences that had to be reconciled (Moravcsik 1993: 30-1). In other words, different domestic economic interest groups were likely to be affected in different ways by the Banking Union; they therefore lobbied domestically as well as at the EU level in order to pursue their preferences. This was particularly the case in Germany, where the national position was pulled in different directions by the representative associations of each of the three pillars of the German banking system. The big commercial banks wanted the Banking Union and wanted it to apply both to all banks in Germany and the euro area, while the domestically-focused co-operative and savings banks did not want Banking Union to apply to them. Domestic divisions weakened German reluctance to Banking Union, contributing to Germany's negotiating position as a "constrained veto player".

Italian policy-makers, like policy-makers from Spain and other countries in the euro area periphery, shared similar interests concerning the Banking Union: they had weak fiscal positions; they had several ailing banks; and they were at risk of contagion from the crisis (Howarth and Quaglia 2016a). Moreover, domestic banks in these countries held considerable amounts of national government bonds, creating a "doom loop" bank-sovereigns (Veron 2012). Policy-makers in Italy were keen to secure financial support mechanisms for ailing banks and sovereigns. In return, they were willing to accept the supra-nationalisation of banking supervision. Moral hazard was less of a concern for policy-makers in countries such as Italy, that would be more likely to need access to external financial support in the Banking Union because their banking system was in poorer health and/or their domestic fiscal position was weaker.

For Italian policy-makers, the over-riding importance of EU-level support mechanisms was to bolster international financial confidence in the Italian banking system. They also advocated the mutualisation of risks. Thus, the SRF and the common fiscal backstop of the ESM were a priority for the Italian government. In the final stage of the negotiations in December 2013, the Italian finance minister, Saccomanni (2013), called for a "common backstop" to "provide contribution to the cost of resolution without conditionality".

In the negotiations on the Banking Union, the Member States had an asymmetric distribution of bargaining power determined by the size of the national economy and the banking system, the relative stability of the national banking system and the state of the public finances. Italy and other euro area periphery countries were mostly *demandeurs*: they were directly hit by the crisis and needed German political and financial support for the Banking Union to go ahead. Hence, they had relatively limited bargaining power. Countries that were not directly hit by the sovereign debt crisis and were relatively less exposed to it - first and foremost, Germany, which was also - by a significant margin - the largest economy in the EU with the second largest banking sector after the UK - were better positioned to resist the requests of the "*demandeurs*" and impose their design for the Banking Union. The asymmetric distribution of bargaining power during the Banking Union negotiations, which were skewed in favour of Germany, accounts for the prioritisation of some components of the Banking Union rather than others.

4. Banking Union and the Completion of EMU

The Banking Union was presented as contributing to the completion of EMU. Indeed, the institutional design of EMU agreed by the Maastricht Treaty and eventually set up from 1999 onwards was incomplete and asymmetric, whereby full monetary union was not coupled with full economic union (Dyson, 2000; Hodson 2009; Verdun, 1996). Fiscal Union was notably missing and had deliberately been left out, principally (but not exclusively), because of the opposition of German policy-makers, and despite the half-hearted calls of French and Italian policy-makers for a *gouvernemente economique* in the euro area (Dyson and Featherstone 1999). Moreover, there was some debate as to whether the ECB should be responsible (or not) for banking supervision in the euro area. Partly (but not exclusively) due to opposition of German policy-makers, the supervision of banks was left at national level (Dyson and Featherstone, 1999). Thus, the Banking Union can be seen as a crisis-driven attempt to address several important issues that were sidestepped or papered over during the EMU negotiations which led to the Maastricht Treaty.

After the (partial) establishment of the Banking Union, the debate on the completion/reform of EMU re-gained momentum. In October 2015, the President of the European Commission, in close co-operation with the President of the Council, the President of the Eurogroup, the President of the European Central Bank, and the President of the European Parliament, produced what became known as the "Five Presidents' Report" on "Completing Europe's Economic and Monetary Union". This report built on "Towards a Genuine Economic and Monetary Union" (the so-called "Four Presidents' Report") of June/December 2012, the Commission's "Blueprint for a Deep and Genuine EMU" of November 2012, and the Analytical Note "Preparing for Next Steps on Better Economic Governance in the Euro Area" of February 2015. The Five Presidents' report stated the objectives of a "genuine Economic Union", a "Financial Union", a "Fiscal Union", and a "Political Union", arguing that these four Unions depended on each other and should therefore be developed in parallel and with the participation of all euro area Member States.

In December 2017, the European Commission presented a package of initiatives that included, amongst others: a proposal to bring the European Stability Mechanism (ESM) into the EU legal framework, transforming it into a European Monetary Fund; and a Communication on establishing a European Minister of Economy and Finance minister. Negotiations on these reform proposals have barely started and are expected to last for some time. However, we can expect that the different interests and ideas that characterised the German and Italian approaches to the Banking Union and to EMU more generally will play out in the negotiations of these pieces of legislation as well. The additional complication is that the recently elected Italian government is likely to adopt a more Eurosceptic stance compared to that of previous Italian governments.

Acknowledgements: Parts of this paper were informed by my joint research with David Howarth (University of Luxembourg). I wish to thank the participants to the conference at Villa Vigoni for their perceptive comments.

References

Bulmer, S. 2014. "Germany and the Eurozone Crisis: Between Hegemony and Domestic Politics". *West European Politics* 37 (6): 1244-1263.

Commission. 2012. Communication: A Roadmap towards a Banking Union. 28 November, Brussels.

De Rynck, S. 2015. "Banking on a Union: The Politics of Changing Eurozone Banking Supervision". *Journal of European Public Policy* 23 (1): 119-135.

Donnelly S. 2014. "Power Politics and the Undersupply of Financial Stability in Europe". *Review of International Political Economy* 21 (4): 980-1005.

Draghi, M. 2014. *Speech at the conference for the 20th anniversary of the establishment of the European Monetary Institute*. 12 February 2014, Brussels.

Dyson, K. (2014), *States, Debt, and Power,* Oxford: Oxford University Press.

Dyson K. (2000). *The Politics of the Eurozone*. Oxford: Oxford University Press.

Dyson, K. and K. Featherstone (1999). The Road to Maastricht. Oxford: Oxford University Press.

Epstein, R. and M. Rhodes. 2016. "The Political Dynamics behind Europe's New Banking Union". *West European Politics* 39 (30): 415-37.

Eurogroup and Ecofin Council. 2013. *Statement on the SRM Backstop*. 18 December.

Euro Summit. 2012. *Statement of the Euro Area Heads of State or Government*. 29 June.

European Central Bank. 2013. *Opinion on a Proposal for a Single Resolution Mechanism*. 6 November, Frankfurt.

European Central Bank. 2012. *Opinion on a Proposal for a Single Supervisory Mechanism*. 1 February, Frankfurt.

European Commission. 2015. *Proposal for an EDIS*. 24 November, Brussels.

European Council. 2012a. *Council Agrees Position on Single Supervisory Mechanism*. December, Brussels.

Glöckler, G., J. Lindner & M. Salines. 2016. "Explaining the Sudden Creation of a Banking Supervisor for the Euro Area". *Journal of European Public Policy* 24 (8): 1135-1153.

Gros, D., and D. Schoenmaker. 2014. "European Deposit Insurance and Resolution in the Banking Union". *Journal of Common Market Studies* 52(3): 529-546.

Hodson, D. (2011), *Governing the Euro Area in Good Times and Bad*. Oxford: Oxford University Press.

Howarth, D., Quaglia, L., (2018), 'The Difficult Construction of a European Deposit Insurance Scheme: A step too far in Banking Union?', *Journal of Economic Policy Reform*, http://www.tandfonline.com/doi/full/10.1080/17487870.2017.1402682.

Howarth, D., and L. Quaglia. 2016a. *The Political Economy of Banking Union*. Oxford: Oxford University Press.

Howarth, D., and L. Quaglia. 2016b. "Internationalized Banking and National Preferences on European Central Bank Supervision". *West European Politics* 39 (3): 438-461.

Juncker, J.-C. 2015. *Completing Europe's Economic and Monetary Union*. Brussels [Five Presidents' Report]

Nielsen, B., and S. Smeets. 2017. "The Role of the EU Institutions in Establishing the Banking Union. Collaborative Leadership in the EMU Reform Process". *Journal of European Public Policy*, http://dx.doi.org/10.1080/13501763.2017.1285342.

Saccomanni, F. 2013. *Letter to the Other Finance Ministers*. 13 December, Rome.

Schaffer, D. 2016. "A Banking Union of Ideas? The Impact of Ordoliberalism and the Vicious

Circle on the EU Banking Union". *Journal of Common Market Studies* 54 (4): 961-980.

Schild, J. 2017. "Germany and France at Cross Purposes: the Case of Banking Union". *Journal of Economic Policy Reform*, doi.org/10.1080/17487870.2017.1396900.

Schimmelfennig, F. 2016. "A Differentiated Leap forward: Spillover, Path-dependency, and Graded Membership in European Banking Regulation". *West European Politics* 39 (30): 483-502.

Skuodis, M. 2017. "Playing the Creation of the European Banking Union: What Union for Which Member States". *Journal of European Integration*, doi.org/10.1080/07036337.2017.1404056.

Van Rompuy, H. 2012. *Towards a Genuine Economic and Monetary Union*, [Four Presidents' Report]. Brussels.

Verdun, A. 1996. "An 'Asymmetrical' Economic and Monetary Union in the EU: Perceptions of Monetary Authorities and Social Partners?". *Journal of European Integration* 20 (1): 59-81.

Veron, N. 2012. *Europe's Single Supervisory Mechanism and the Long Journey Towards Banking Union*. Bruegel, October, Brussels.

Visco, I. 2016. *Speech: The State of the Union*. 5 May, Florence.

MATERNAL EMPLOYMENT, ATTITUDES TOWARD GENDER EQUALITY AND WORK-FAMILY POLICIES. GERMAN-ITALIAN DISCREPANCIES?

Agnes Blome

Introduction

Germany and Italy were long known for their familialist and male-breadwinner-oriented models of welfare capitalism. Social security and labour markets developed based on traditional gendered divisions of labor, where men are expected to become breadwinners and women are expected to become unpaid carers. Work-family reconciliation policies such as care services were absent, or, if they existed, reinforced traditional gender roles by supporting long leaves and part-time work for mothers. As a consequence, women's and mothers' employment rates have been low in both countries. Yet, in recent years the labour market participation of mothers increasingly shows diverging trends. While maternal employment rates in Germany jumped to 70 percent in 2014, only 56 percent of Italian mothers participated in the labour market in the same year.

This piece draws on institutional and cultural factors to describe and explain recent trends in maternal employment in Germany and Italy. While a large body of research focuses on the impact of public policies and labour market characteristics, more recent research takes into account cultural factors such as ideas and norms about mothers' employment and childcare. In countries where "ideals of care" emphasize the importance of maternal care for small children, maternal employment rates may be lower because mothers' labour market participation may be perceived as in conflict with the ideal of "good motherhood" (Kremer 2007, Boeckmann et al. 2015). Since the traditional male-breadwinner model shaped both public policies and people's attitudes in Germany and Italy for a long time, these recent changes in German mothers' employment are surprising. What happened to the care ideals in both countries and what impact do they still have on public policies and on maternal employment?

Based on this research I argue that childcare norms and attitudes towards gender equality not only shape maternal employment, but are also related to changes of public work-family policies. Thus, where attitudes and the cultural context changes, mothers' employment-friendly policies become more likely and this will be reflected in increasing maternal employment rates. I use attitudinal data from the European Values Study (EVS) to examine country-level differences in cultural norms regarding the gender division of work and beliefs that children and family life suffer when a mother works for pay. To analyze policies, I examine maternity and parental leaves as well as publicly funded childcare for 0-3 years old children.

Maternal employment, work-family policies and cultural norms

Due to their unequal access to positions and economic resources, men and women are affected differently by the economic context. Several studies on gender inequalities in the labour market show that women in general spend less hours in paid work and are less likely to have highly remunerated positions than men (Mandel and Semyonov 2005, Pettit and Hook 2009, Dieckhoff et al. 2015). This is especially the case when women have children. Childless women and men, but also fathers, have higher employment rates and work longer hours than mothers (Boeckmann et al. 2015). Yet, cross-country differences in maternal employment rates point to the importance of country-specific contextual factors that shape women's decisions about employment as well as employers' understanding and treatment of mothers in the workforce. For instance, the Varieties of Capitalism literature claims that the way the market economy works influences the degree of sex segregation in a country. A country's production system emphasizes either specific or general skills. Since general skills are more easily portable on the labour market than specific skills, countries with an emphasis on specific skills (Coordinated Market Economies, CME) provide more generous employment security provisions and social protection to safeguard people who lose a job during e.g. a recession (Hall and Soskice). Moreover, because employers have invested in worker training they are interested in committing employees to their workplaces. By anticipating women's discontinuous work and lower working hours due to care responsibilities, employers often practice statistical discrimination. As a consequence, women are often excluded from many sectors of employment in these economies (Estevez-Abé 2006, Mandel and Shalev 2009). Social protection schemes designed to protect the male model of full-time continuous employment reinforce the effect ("institutional complementarities"). In addition, generous family policies may exacerbate employer's reluctance to invest in women's specific skills' training and to hire them. Long maternity and parental leaves, in particular, worsen women's chances, because firms would have to find a replacement for someone with specific skills (Estevez-Abé 2005, 2006).

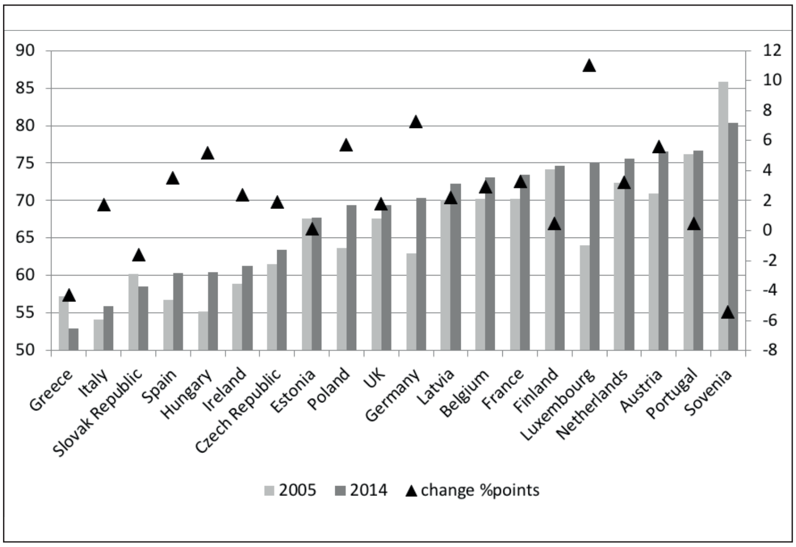
The comparative feminist welfare state scholarship has long pointed to the extent of a male-breadwinner orientation of social policies, where a strong male breadwinner welfare state undermines women's and mothers' employment (Lewis 1992, Sainsbury 1996). While some focused on the role of classic social policies such as unemployment protection and pension schemes for fostering the male full-time continuous breadwinner model, a prominent body of research claims that maternal employment is shaped by work-family reconciliation policies designed to alleviate gender-based labor market inequalities. All in all, this literature is inconsistent in their conclusions (Brady et al. 2018). Some argue that generous work-family policies encourage female and maternal employment and reduce motherhood penalties (Müller and Wrohlich 2018, Budig et al. 2012, Korpi et al. 2013, Nieuwenhuis 2014). Others claim that certain aspects of work-family policies such as lengthy parental leaves and part-time employment have adverse labour market consequences for women (e.g. Mandel and Semyonov 2005, 2006; Pettit and Hook 2009). This literature has provided evidence of large cross-national variation in the design of work-family policies – not only between Anglo-Saxon, Scandinavian and Conservative welfare states, but also within these groups. For example, the Conservative welfare states Germany, France and Italy strongly differ in their family policy approaches. While the French model of comprehensive childcare support comes close to the Nordic welfare states, Italy is characterized by very low public support of working mothers. Germany only recently reformed some of the work-family reconciliation policies, but is at the same time characterized by regulations such as the income splitting that continue to support the male breadwinner model.

International comparisons have also highlighted the role of normative beliefs in shaping maternal employment. In fact, some argue that the decisions of mothers do not simply respond to the policy context, implying that other factors than economic gains play a role for a mother's decision to take up employment and to what extent (Pfau-Effinger 2004, Kremer 2007). Rather, the cultural support of mothers' employment is also decisive. In a mothers' employment supportive cultural setting, maternal employment is more likely to increase than in a context with a lack of support for working mothers (Budig et al. 2012).

Normative beliefs towards childcare and maternal employment not only shape mothers' employment decision-making processes, but are also mirrored in policy design. For example, generous work-family policies that enable mothers to take a long leave from the labour market reflect conservative understandings of the gender division of work (Budig et al. 2012). At the same time, work-family policies may change people's attitudes towards maternal employment in the long run (Ziefle and

Gangl 2015). To understand change it is therefore essential to analyze developments of normative beliefs and public policies over time. In recent decades, many rich democracies have reformed work-family reconciliation policies, yet maternal employment continues to differ across countries. Differences in the (changes to the) cultural context may explain the discrepancies. When policy-makers consider work-family policy reforms they take into account the electorate's normative beliefs. When their beliefs change, policy change becomes more likely (Blome 2017). Together with changed cultural expectations regarding maternal employment, these reformed policies may then shape mothers' decisions about employment as well as employers' treatment of mothers in the workforce.

Graph 1: Employment of mothers aged 25-54 years in European welfare states, 2005 and 2014



Note: Mothers with at least one child under 14 years old. Source: OECD Family Database

Mothers' employment rates: Large differences in Europe, sharp increase in Germany, continuing low levels in Italy

Maternal employment is on the rise throughout Europe. At the same time, the employment level differs considerably between European welfare states (Graph 1). In 2014, more mothers are in employment than in 2005 in all countries except for Greece, Slovenia and the Slovak Republic. Still, the average growth is moderate (about 4 percentage points). Germany stands out for a considerable increase of maternal employment from 63 percent to 70,3 percent, while in Italy only 56 percent of mothers are in employment in 2014 compared to 54 percent in 2005.

One of the main differences between working mothers in Germany and Italy is related to the number of hours worked. Part-time work in Germany is widespread, and mothers, in particular of very small children, usually work few hours (Statistisches Bundesamt 2017). In contrast, (quality) part-time work is often not available to Italian mothers. Therefore, the barriers to take up employment while children are small are high. It should be noted, though, that the recent increase of maternal employment rates in Germany is related to a rise in (near) full-time employment.[1] Compared to 23 percent in the mid-2000s, more than 30 percent of German mothers worked full-time in 2013 (OECD Family Database). At the same time, the share of German mothers who worked part-time remained at about 40 percent during the years. In Italy, the relationship between motherhood status and working hours is inverse: more mothers work full-time (35 percent) than part-time (21 percent) and this has not changed over time.

1 The OECD defines full-time/part-time work as more/less than 30 hours per week.

During the economic crisis, women in both Germany and Italy had been protected by the persistence of sectoral and occupational segregation by gender in their countries. Most employment losses happened in the manufacturing and construction sectors as well as in selected financial branches which are dominated by men (European Commission 2012). At the same time, employment growth in the services sector – which is where many women work – is often accompanied by a rise in temporary work and related to more precarious employment conditions (reference). In Italy, most of the increase in women's employment took place in lower ranked job positions, and lower educated women experienced less job losses than highly educated women (Gálvez-Muñoz et al. 2014). Furthermore, older workers (49 years and older) appear to have been able to keep jobs at the expense of younger women (and men). As women tend to have children once their labour market prospects are more secure, they are older when they become mothers. Since older workers are more likely to keep their jobs, this might partly explain the stability in maternal employment rates in Italy and the rise in Germany.

As shown, part-time work is one of the maternal employment facilitating factors in Germany. It is related to other institutional differences between Germany and Italy. The following section concentrates on the – arguably – two most important public work-family reconciliation policies: maternity and parental leave regulations and the public provision of childcare.

Public work-family reconciliation policies: Expansion in Germany, stagnation in Italy

At the beginning of the 1990s, Germany and Italy stood paradigmatically for welfare states in which the lack of day care and other policies supporting mothers' employment led to a strong gender division of labor. The support of the male-breadwinner model was more comprehensive in Germany: For example, the joint taxation splitting system and the free co-insurance of non-employed spouses incentivizes mothers to opt out of the labor market or to reduce labor market participation. While Germany made substantial changes in the work-family policies between 2000 and 2008, policy developments in Italy have been discontinuous and fragmentary (Blome 2017). The following paragraphs describe (1) the developments in maternity and parental leave schemes and (2) childcare provision for children under three years of age.

In Germany, mothers are entitled to paid maternity leave 6 weeks before and 8 weeks after birth. After maternity leave, parents may be on parental leave. After its first adoption in 1986 parental leave regulation changed several times in Germany. Since 1992 parents have a right to return to their previous employer until the child is 3 years old. The last substantial reform took place in 2006, when the maximum duration of paid parental leave for all parents was increased to 14 months including two "use-it-or-lose-it" fathers' months and the previously flat-rate sum changed to an income-related measure of 67% of previous net income with a cap of €1,800. A further reform in 2011 abolished the entitlement of social assistance beneficiaries to the flat-rate basic parental leave allowance of €300 and reduced the replacement rate to maximum 65% for parents who earn more than €1,200. In 2015, parental leave was flexibilized by giving parents the possibility to share more months (up to 32 paid leave months). It can be classified as a generous parental leave scheme that offers some incentives for fathers to participate in care work and thus enable couples a more gender equal division of work.

In Italy, mothers are entitled to a comparatively long maternity leave of five months at 80% of previous earnings. Paid parental leave was created in 1994 and offered up to six months per parent at 30% of earnings for a child under six. The 2000 parental leave reform gave fathers the right to claim the benefit independently of the mother. Parents are entitled to a total of 10 paid parental leave months, but each of them may only claim 6 months at most. If one parent (usually the mother) uses 6 months and the other (often the father) uses at least 4 months, the leave period may be extended by one month. In addition, fathers are entitled to two days paternity leave. The low replacement rate and the short overall duration of parental leave makes the Italian parental leave scheme parsimonious with little incentives for a more gender equal division of work.

Children older than three are well covered by public provision of childcare in both Germany and Italy. However, parents of children aged between 0 and 3 years faced care supply shortages. There is a gap between the end of paid parental leave and the start of ample childcare. In the beginning of the 1990s, only 3 percent of children of that age group had a publicly subsidized childcare place in Western Germany (40 percent in Eastern Germany) (Statistisches Bundesamt 2004). Furthermore, opening hours in Germany were only short. Often, children did not stay until lunchtime. Only 6 percent of 0-3 years old children had access to publicly provided childcare in Italy in 1994 (Centro nazionale di documentazione e analisi per l'infanzia e l'adolescenza 2002). Thus, in both countries mothers were the primary caretaker for the very young children.

In 2004 and 2008 two reforms pushed the provision of childcare places for children younger than three years in Germany. The 2004 reform required municipalities to provide enough places for children below three to meet demand, or as a minimum to make places available for children with parents in employment/training. The 2008 reform introduced the right to a childcare place for children over one year of age. Since 2013, every child between the age of one and six has had the legal right to a place in a daycare centre or with a qualified childminder. The ratio of the number of places available per 100 children of that age group rose from 14 percent in 2006 to 33 percent in 2017 (Statistisches Bundesamt 2017). In Italy, by contrast, medium-range reforms and much fewer financial resources led to only marginal increases in coverage rates (Naldini and Jurado 2013, Naldini and Saraceno 2008). During the crisis years the small expansion came to a halt in 2008 (13 percent).

In sum, the German family policy model became much more supportive of the dual-earner model, while in Italy, maternal employment is not supported by public policies and childcare remains the responsibility of mothers. The most important reforms happened after the Millennium in Germany.

Attitudes towards gender equality, maternal employment and childcare

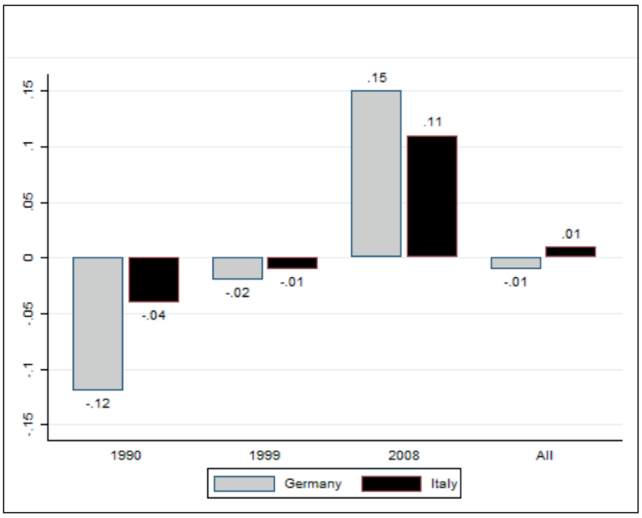
More recent research on the determining factors of maternal employment argues to take into account the cultural context of maternal employment. Attitudes toward gender equality and toward proper childcare shape both individuals' decisions to return to or to look for employment and employers' willingness to employ mothers. At the same time, the population's beliefs are reflected in work-family policy design and their reforms. The following paragraphs will assess the normative beliefs of Italians and Germans towards gender equality, childcare and maternal employment. Budig et al. (2012) argue that motherhood-based employment differences are less likely in countries where gender ideologies support both men's and women's contribution to the household income, while dominant ideals of care that emphasize mothers' care for children may be associated with higher employment differences.

The following analyses are based on three waves of the European Values Study. A battery of questions is asked to assess people's attitudes towards gender equality, the gender division of work and childcare. By way of factor analysis two indicators were identified that represent (1) attitudes towards gender equality and (2) attitudes towards childcare and maternal employment. The graphs show the deviations from the mean over all years.

The higher the value the more progressive are attitudes towards gender equality and towards childcare and maternal employment.

Italians have had more progressive attitudes towards gender equality than Germans (Graph 2). Yet, the change in Germany between 1990 and 2008 is remarkable. In 2008, the likelihood to support gender equality is higher in Germany than in Italy.

Graph 2: Attitudes towards gender equality

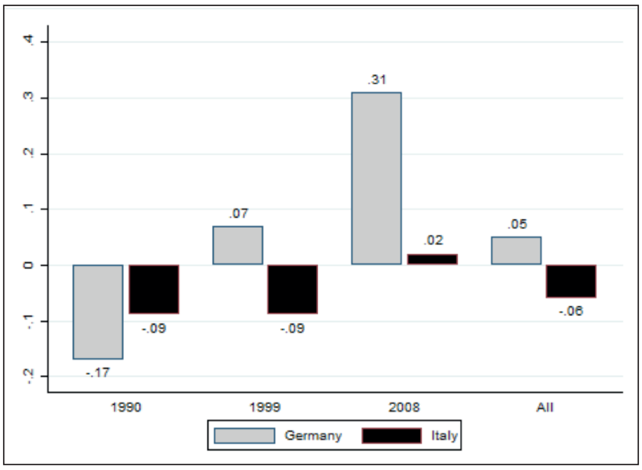


Note: Values are based on a factor analysis. The factor loads on the following questions: (1) Both the husband and wife should contribute to household income, (2) Having a job is the best way for a woman to be an independent person, (3) Being a housewife is just as fulfilling as working for pay, (4) A working mother can establish just as warm and secure a relationship with her children as a mother who does not work.

Source: European Values Study 1990, 1999, 2008.

A significant change in Germany is also noted for attitudes toward childcare. In 2008, more Germans were positive toward maternal employment than in 1999 and even more compared to 1990. Italians, by contrast, continued to be opposed to maternal employment despite a small change between 1999 and 2008 (Graph 3).

Graph 3: Attitudes towards childcare

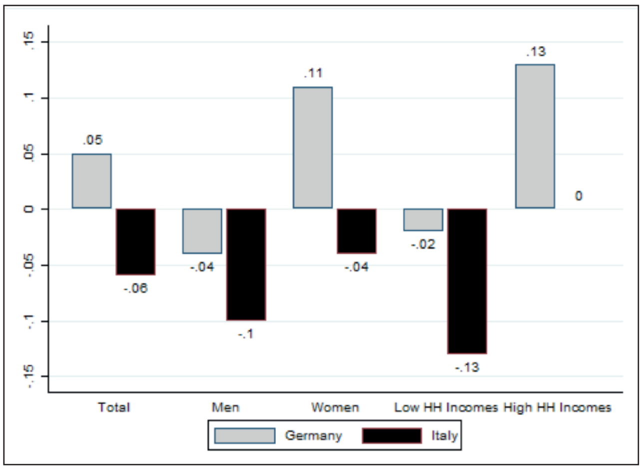


Note: Values are based on a factor analysis. The factor loads on the following questions: (1) A working mother can establish just as warm and secure a relationship with her children as a mother who does not work, (2) A pre-school child is likely to suffer if his or her mother works, (3) A job is alright but what most women really want is a home and children.

Source: European Values Study 1990, 1999, 2008.

The picture also holds when we look at specific groups in society (Graph 5). In both countries, women have more progressive attitudes towards childcare and maternal employment than men. Yet, Italian women are much less supportive of maternal employment than German women. In addition, people with low incomes have more traditional attitudes in both countries – again with a big difference between Germany and Italy. People with a high income have more progressive views in Germany, while they are not different to the mean in Italy.

Graph 5: Attitudes towards childcare by social groups



Note: Values are based on a factor analysis. The factor loads on the following questions: (1) A working mother can establish just as warm and secure a relationship with her children as a mother who does not work, (2) A pre-school child is likely to suffer if his or her mother works, (3) A job is alright but what most women really want is a home and children.

Source: European Values Study 1990, 1999, 2008.

The comparison of Germany and Italy shows increasing cultural differences. While Germans have had traditional attitudes towards gender equality and maternal employment for a long time, this changed around the Millennium. Even though Italians had slightly more progressive attitudes toward gender equality than Germans in the beginning of the 1990s, this reversed in the 2000s. Especially regarding opinions on childcare and maternal employment, Italians seem to continue to favor a more male-breadwinner-oriented family model (see Lomazzi 2017). The fact that attitudes in Germany changed before the turn of the millennium while policy reforms happened after implies that policy-makers reacted to the changed cultural context and re-designed policies. In Italy, by contrast, attitudes hardly changed, and policy-makers might not have deemed it necessary to reform policies (see Blome 2017 for a more detailed account of the policy reforms). Both the cultural context and the respective (adapted) policies likely build the context for the low maternal employment rates in Italy and the increase in mothers' labour force participation in Germany. Despite the overall developments, the data also show some degree of polarization in attitudes in both countries. Certain groups of the electorate (e.g. women, people with high incomes) drive the change of attitudes towards more progressive attitudes in Germany while others (e.g. men, people with low incomes) tend to support the traditional male-breadwinner model. The situation is similar in Italy, even though attitudes polarize the population to a lesser extent.

Conclusion

Maternal employment increasingly differs between Germany and Italy. This article aimed at showing how institutional and cultural developments build a context for maternal employment. More precisely, it shows how policy effects are influenced and conditioned by cultural contexts. By examining the evolution of attitudes towards gender roles, maternal employment and childcare I show how the cultural context changed in Germany and enabled a series of work-family policy reforms. Both factors then contributed to the increase of maternal employment. At the same time, attitudes did not change to a similar extent in Italy. As a result, only small-scale changes happened to work-family policies. This likely contributed to the persistent low maternal employment rates.

Several questions are left for further research. In this paper I have looked at the relationship between maternal employment, cultural factors and public policies on the macro level. Analyses on the individual level may explore further the role attitudes and policies play for an individual's or couple's decision (when) to return to employment after a baby was born. A pertinent question is why attitudes changed so dramatically in Germany, but less so in Italy. Religion, secularization and unification arguably play a role, but given the diverging attitudes of societal groups obviously these factors are not the whole story. Last, future research should attend to the question of unequal policy responsiveness, i.e. whether and under which political conditions policy-makers respond to certain groups of the electorate – e.g. women and the highly educated in the case of work-family policies – more than to others.

References

Blome, Agnes. 2017. *The Politics of Work-family Policies in Germany and Italy.* Abingdon/New York: Routledge.

Blome, Agnes. 2018. „Von Kinder, Küche, Kirche zu Kinder, Karriere, KiTa? Geschlechterrollen, Familienpolitik und Religion im Wandel der Zeit", *Sozialer Fortschritt* 67, special issue „Ökonomisierung und Konfession. Was bleibt?", edited by Josef Hien and Wolfgang Schroeder, pp. 453-475.

Boeckmann, Irene, Joya Misra, and Michelle J. Budig. 2015. "Cultural and Institutional Factors Shaping Mothers' Employment and Working Hours in Postindustrial Countries." *Social Forces* 93: 1301-1333.

Budig, Michelle J., Joya Misra, and Irene Boeckmann. 2012. "The Motherhood Penalty in Cross-National Perspective: The Importance of Work-Family Policies and Cultural Attitudes." *Social Politics* 19: 163-193.

Centro nazionale di documentazione e analisi per l'infanzia e l'adolescenza. 2002. I servizi educativi per la prima infanzia. In *Quaderni no. 21*. Firenze: Istituto degli Innocenti.

Dieckhoff, Martina, Vanessa Gash and Nadia Steiber. 2015. "Measuring the Effect of Institutional Change on Gender Inequality in the Labour Market." *Research in Social Stratification and Mobility* 39: 59-75.

European Commission. 2012. *The Impact of the Economic Crisis on the Situation of Women and Men and on Gender Equality Policies*. Luxembourg: Publications Office of the European Union.

Estevez-Abe, Margarita. 2005. "Gender Bias in Skills and Social Policies: The Varieties of Capitalism Perspective on Sex Segregation." *Social Politics* 12(2): 180–215.

Estevez-Abe, Margarita. 2006. "Gendering the Varieties of Capitalism – a Study of Occupational Segregation by Sex in Advanced Industrial Societies." *World Politics* 59(1): 142–75.

Gálvez-Muñoz, Lina, Paula Rodríguez-Modroño, and Tindara Addabbo. 2014. The impact of austerity on women's work in Italy and Spain. Available at: www.aiel.it

Hall, Peter A, and David W. Soskice 2001. *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*. Oxford: Oxford University Press.

ISTAT. 2013. Rapporto Annuale: La Situazione del Paese, Rome, Istat. Available at: www.istat.it.

Korpi, Walter, Tommy Ferrarini and Stefan Englund. 2013. "Women's Opportunities Under Different Family Policy Constellations: Gender, Class, and Inequality Tradeoffs in Western Countries Re-Examined." *Social Politics* 20: 1-40.

Kremer, Monique. 2007. *How Welfare States Care.* Amsterdam: Amsterdam University Press.

Lomazzi, Vera. 2017. "Gender role attitudes in Italy: 1988–2008. A path-dependency story of traditionalism." *European Societies* 19(4): 370-395.

Mandel, Hadas and Moshe Semyonov. 2005. "Family Policies, Wage Structures, and Gender Gaps: Sources of Earnings Inequality in 20 Countries." *American Sociological Review* 70: 949-967.

Mandel, Hadas and Moshe Semyonov. 2006. "A Welfare State Paradox: State Interventions and Women's Employment Opportunities in 22 Countries." *American Journal of Sociology* 111: 1910-1949.

Müller, Kai-Uwe and Katharina Wrohlich. 2018. Does Subsidized Care for Toddlers Increase Maternal Labor Supply?: Evidence from a Large-Scale Expansion of Early Childcare. DIW Discussion Paper No. 1747. https://www.diw.de/sixcms/detail.php?id=diw_01.c.596085.de

Naldini, Manuela and Chiara Saraceno. 2008. “Not totally frozen, but far from structural reforms.” *Social Policy & Administration* 42(7): 733-748.

Naldini, Manuela and Teresa Jurado. 2013. “Family and welfare state reorientation in Spain and inertia in Italy from a European perspective” Population Review 52(1): 43–61.

Nieuwenhuis, Rense. 2014. *Family policy outcomes: Combining institutional and demographic explanations of women's employment and earnings inequality in OECD countries, 1975-2005* (SSRN Scholarly Paper No. ID 2438617). Social Science Research Network, Rochester, NY.

Statistisches Bundesamt. 2004. Kindertagesbetreuung in Deutschland. Einrichtungen, Plätze, Personal und Kosten 1990 bis 2002. Wiesbaden

Statistisches Bundesamt. 2017. Statistiken der Kinder- und Jugendhilfe. Kinder und tätige Personen in Tageseinrichtungen am 01.03. eines Jahres. Wiesbaden.

Ziefle, Andrea and Markus Gangl. 2015. “Do Women Respond to Changes in Family Policy? A Quasi-Experimental Study of the Duration of Mothers' Employment Interruptions in Germany.” *European Sociological Review* 30: 562-581.

C GERMAN AND ITALIAN PERCEPTIONS, DIFFERENCES AND MISGIVINGS

ITALY AND GERMANY DURING THE CRISIS: SUPPORT FOR THE EU AND RECIPROCAL VIEWS[110]

Alessandro Pellegata
Università degli Studi di Milano, Department of Social and Political Sciences

Mutual trust among citizens of different EU Member States is a cornerstone for the establishment of a sense of European identity and the strengthening of the EU integration process (Hooghe and Verhaegen 2017). However, the current multifaceted crisis that the EU is experiencing and some side effects of the integration process have not only exacerbated public opposition to the EU, but are also eroding the stock of mutual trust among the citizens of the different Member States that was accumulated after the end of the Second World War. In particular, the recent Eurozone crisis has increased the tension between core countries of Northern Europe, with strong macro-economic performances, and countries of the Southern periphery, struggling with excessive deficits and increasing public debt. Two competing narratives about who is to blame for the crisis are at play. The core countries' narrative is about feckless Greeks and Italians and the inability of their national institutions to adopt structural reforms to keep their public debt under control and thereby render the Euro sustainable. The narrative running in peripheral Member States blame the Northern countries, Germany *in primis*, for their austerity measures and their lack of solidarity towards countries facing severe economic and financial difficulties. As Grabbe (2012) pointed out, the sovereign debt crisis is more than the breakdown of both a currency and a political project, as it is also causing a loss of trust between EU Member States.

By taking Germany and Italy as illustrative examples of this "Core-Periphery" divide, this article aims to investigate the evolution of public support for the EU in these two countries, both before and after the Euro crisis, and its relation with the mutual perceptions of both countries as expressed by public opinion and the political élites. We postulate that, given the leading role played by Germany within the EU institution and the different narratives fuelled in the core and peripheral Member States, Italian citizens and representatives tend to blame Germany both for the Euro crisis and for the bad Italian economic situation. Therefore, we expect to find a significant association between the orientations of Italians towards the EU and their view of Germany. Empirical analyses have been conducted using cross-sectional survey data at both the mass and élite levels taken from multiple sources. The findings obtained confirm our expectations.

Political Commonalities but Long-lasting Stereotypes

Germany and Italy share numerous historical commonalities, such as a late nation-building process which occurred only in the second half of the nineteenth century, and the experience of authoritarian regimes during the two world wars. Germany and Italy are both founding members of the EU and, since the end of WWII have been characterised by a pronounced Europeanism by both their political élites and citizens. Moreover, both countries have undergone major political changes after the end of the Cold War: the re-unification of West and East Germany following the tearing down of the Berlin Wall in 1989, and the collapse of the traditional party system in Italy, following the *Mani Pulite* corruption scandal(s)

110 This article has been presented at the workshop "Responses of European Economic Cultures to Europe's Crisis Politics: The Example of German-Italian Discrepancies" held in Villa Vigoni, Menaggio (IT) on 25 – 27 June 2018. The present contribution is mostly taken by Olmastroni, Francesco and Alessandro Pellegata (2018) "Members Apart: A Mass-Elite Comparison of Mutual Perceptions and Support for the European Union in Germany and Italy", *Contemporary Italian Politics* 10 (1): 56-75. This study received the financial support of the project "Reconciling Economic and Social Europe: The Role of Values, Ideas and Politics (REScEU)", funded by an Advanced Grant of the European Research Council (Grant no. 340534, P.I: Maurizio Ferrera).

in the 1990s. Italian-German relations are intense and co-operative at the cultural, economic and societal level, as well as in daily political life. In 2015, Italy ranked third among EU countries for the total value of German imports, and Germany is the biggest source of Italian imports and the first destination for Italian exports (Diedrichs 2010; Dinger 2013).

However, Germany and Italy have been also characterised by longstanding stereotypes and prejudices. Germans express a high self-esteem and consideration of their leading role in Europe, and, while they admire Italy for its lifestyle, they consider its institutions to be inefficient and corrupt. On the other hand, Italians appreciate German efficiency and the hardworking ethic of its people but, at the same time, criticise their excessive rigour and their harsh and uncompassionate nature. (Pew Research Center 2012, 2013; Friedrich Ebert Stiftung 2016). Gian Enrico Rusconi (2008), one of the most important scholars of Italian-German relations, argues that, since the end of the Cold War, several political events have represented sources of tension in Italian-German bilateral relations and have contributed to exacerbating the divergent views that the two countries have of each other.

Core versus Periphery: Germany-Italy Relations in Times of Crisis

With the outbreak of the Euro crisis, the EU and the integration process, which, for many years, had represented the common denominator of German-Italian bilateral relationships, have become the most challenging source of tension between these two countries. A new sharp dividing line over the issue of fiscal stability and, ultimately, cross-national solidarity has polarised German and Italian publics, their media and their political élites. Thus, two opposing narratives about who is to blame for the crisis and the initiatives that should be taken to manage its detrimental consequences are in play.

In Germany, the debate over the Euro crisis has been framed as a conflict between "Northern saints" and "Southern sinners" (Matthijs and McNamara 2015). Hard work, prudent savings, moderate consumption, wage restraint, and fiscal stability – primarily in Germany, but also in Austria, Finland and The Netherlands – were seen as northern virtues and were juxtaposed to the southern vices of low competitiveness, meagre savings, disproportionate consumption, inflated wages, and fiscal profligacy which characterised the offensive acronym of "PIIGS" (the countries of Portugal, Ireland, Italy, Greece and Spain). Therefore, Germany supports a markedly "disciplinarian" approach, deeply rooted in the ordoliberal doctrine (Bulmer 2014; Meiers 2015), according to which the burdens of fiscal adjustment should fall exclusively on national governments and taxpayers.

In contrast, a large part of the Italian media and of the political élite, even among mainstream political parties, blame the excessive rigour and lack of solidarity of the EU institutions and northern governments, Germany *in primis*, and advance the notion of debt pooling in the form of Eurobonds or fiscal equalisation schemes. They oppose the conditionality regime and austerity measures, and call for more flexibility in the application of rules, the mobilisation of EU resources for investment and growth, and, most importantly, the "mutualisation" of risks (Ferrera 2017). The REScEU (Reconciling Economic and Social Europe: Values, Ideas and Politics) Mass Survey provides evidence in support of the difference between the Germans' and the Italians' approval of financial bailouts, and their views about who is to blame for the recent Eurozone crisis (Ferrera and Pellegata 2017).

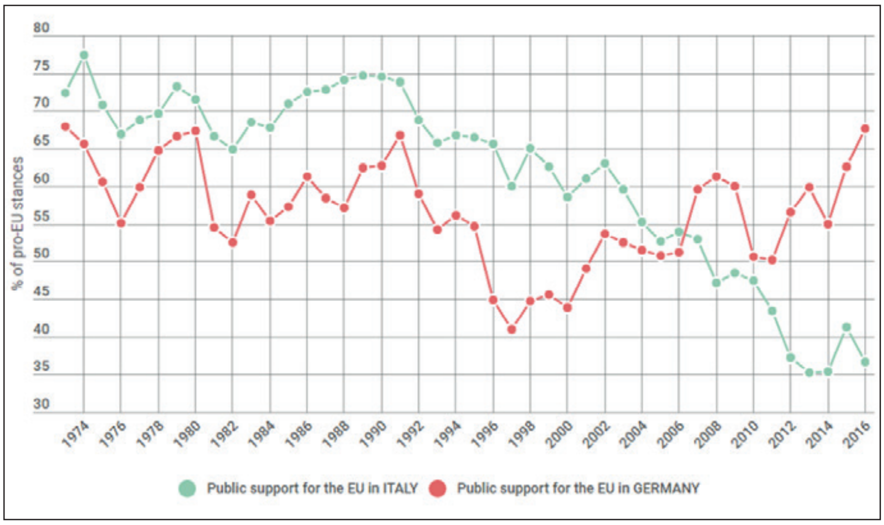
Previous research has shown a positive relation between support for the EU and macroeconomic performance (Anderson 1998; Anderson and Kaltenhaler 1996). Considering that the economic crisis, fiscal austerity measures and the conditionality regime have produced clear and tangible losses in the Euro periphery, we expect to find a sharper decrease in public support for the EU in

Italy than in Germany caused by the onset of the Eurozone crisis. However, we push our expectations a step forward by postulating an association between support for the EU and the Italians' view of Germany. The narratives of both the media and the Italian political élite scapegoat EU institutions and their policy initiatives for the stagnant Italian economy and its excessive public debt. Given the strong relations that have occurred historically between Germany and Italy, and the leadership that the former plays within the EU institutions (Paterson 2011; Kundnani 2015), Italian citizens and its political élite tend to identify the EU behaviour with that of the role of Germany. Thus, we expect to find evidence in support of a decline in the level of trust of Italians *vis-à-vis* Germans relating to their decreasing support for the EU.

Assessing the Relation between Support for the EU and Mutual Feeling

A vast amount of the literature has argued that, from the early 1990s, the EU and the integration process started to be politicised in domestic politics, and became increasingly disputed after the onset of the financial crisis (Hooghe and Marks 2009; Hutter, Grande and Kriesi 2016). In order to estimate the preferences of the Germans and the Italians for the EU, we have built a measure of public mood based upon several EU-related issues. This measure stems from the concept of policy mood developed by Stimson (1999), which is an aggregate and longitudinal estimation of the opinions of citizens on one or more controversial policy issues. More precisely, we have aggregated the frequency distributions of responses to survey questions related to general attitudes towards the EU gathered from Eurobarometer series conducted between 1973 and 2016.

Figure 1. Public Mood towards the EU in Germany and Italy



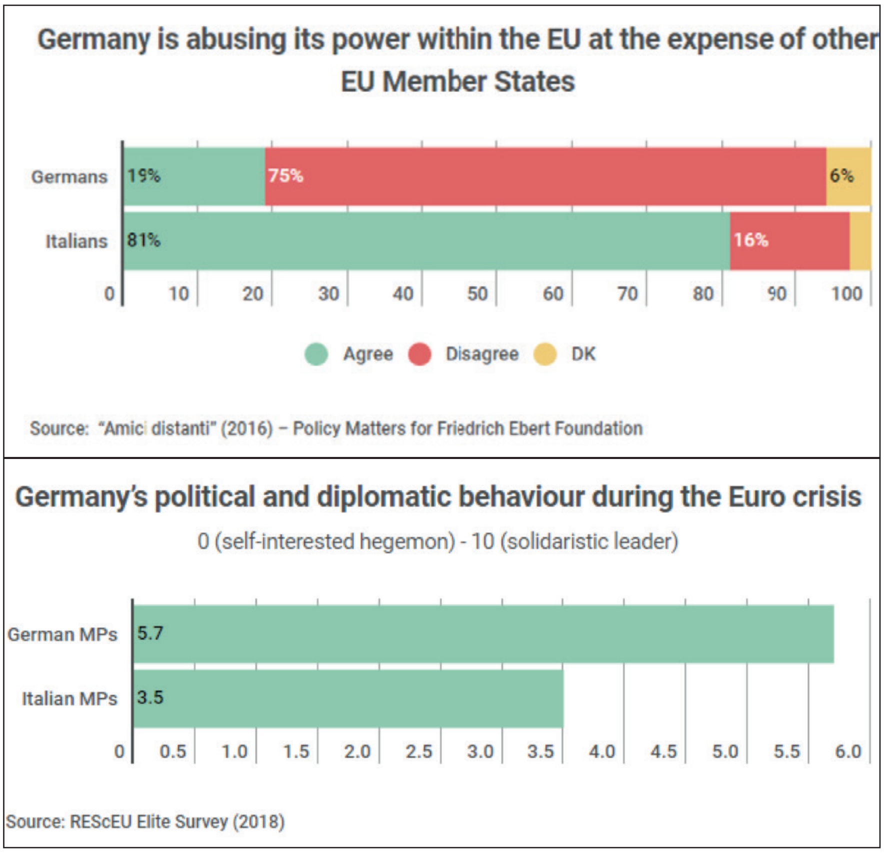
Notes: Mood in the two countries has been estimated through the dyad ratio algorithm (WCalc software, Stimson 1999).

Source: Eurobarometer 1973-2016.

The green line in the graph plotted in Figure 1 represents our estimate of the public mood of Italians towards the EU, while the red line indicates that of the Germans towards the EU. This indicator should be interpreted as the annual share of citizens who express "pro-EU" stances. The average level of public mood towards the EU is quite high in both Germany (65.7%) and Italy (70.0%), confirming the marked Europeanism that has characterised the two countries from the beginning of the EU project. However, the two countries show different patterns of variation over time. The public mood of the Germans towards the EU remained high and fairly constant during the 1970s and the 1980s. It decreased during the 1990s, after the re-unification process and the decision to abandon the *Deutschmark*, but subsequently increased again to remain high even in recent years. As expected, the Italian mood, in contrast, relentlessly decreased from 1993, following the adoption of the Maastricht Treaty, and fell below the threshold of 50 per cent after the onset of the sovereign debt crisis. While, in 2016, two Germans out of three expressed positive orientations towards the EU, only 37 per cent of Italians supported the integration process.

Unfortunately, we could not rely on a yearly estimate of the reciprocal views of the Germans and the Italians to allow us to make a longitudinal description of their evolution. However, a number of recent surveys provide us with data that depict alarming signals regarding the mutual feelings of the Germans and Italians. The Friedrich Ebert Foundation (2016) shows important differences in the opinions of the Germans and the Italians regarding the role of Germany within EU institutions. While 68 per cent of the Italian respondents agreed with the statement that Germany should contribute more to the EU budget since it receives more advantages than other Member States, 66 per cent of Germans took the opposite position. Furthermore, while an impressive 81 per cent of Italian respondents believe that Germany is abusing its power within the EU at the expense of other EU Member States, only 19 per cent of their German counterparts agree on this position (see Figure 2). Few available data at the élite level confirm this discrepancy. A recent élite survey conducted by REScEU between 2017 and 2018 among the national representatives of seven EU Member States, including Germany and Italy, asked the respondents to evaluate Germany's political and diplomatic behaviour during the Euro crisis on a scale ranging from 0 (a self-interested hegemon) to 10 (a solidaristic leader). As the lower panel of Figure 2 indicates, the average value of German MPs is 5.7, while the average score among Italian MPs is 3.5.

Figure 2. Germany-Italy mutual feelings. Mass (upper panel) and elite (lower panel) level



Then, to test our conjecture that the orientations of Italians towards the EU and their views about Germany are related, we have investigated empirically which individual-level factors are associated with the view of Germany expressed by Italian citizens and their political representatives. Unfortunately, as already observed, data on the reciprocal views of Germans and Italians do not systematically cover a long period. As a result, we have selected two partially different questions in order to operationalise Italian views of Germany in the last ten years taken from the Transatlantic Trends Survey and the LAPS-PRIN PEI survey.[111] The first survey question asked respondents to evaluate their feelings towards Germany, its institutions, and people using either a 100-point or 10-point

111 For Transatlantic Trends Survey, see http://www.gmfus.org/initiatives/transatlantic-trends-%E2%80%93-public-opinion, and for LAPS PRIN_PEI data, see the Special issue "Italian Foreign Policy: To Take Arms against a Sea of Troubles?" of the *Italian Political Science Review*.

"thermometer" scale, with 100 (or 10) meaning a very warm, favourable feeling, 0 meaning a very cold, unfavourable feeling, and 50 (or 5) meaning not particularly warm nor cold. For the sake of consistency, we re-scaled the original values in order to obtain a 10-point scale. This survey item was available in 2006, 2008 and 2016. In 2012, we selected an item which presented a different wording. This item asked respondents whether they had a favourable or unfavourable opinion of Germany. We have recoded the original Likert scale, which included four response categories into a dummy variable: "tend not to favour" (0) and "tend to favour" (1). The main explanatory variables included in the regression models refer to individual perceptions of the economic and migration crises, the role of Germany and its leadership during and after the crisis, and their opinion of the EU and their country's membership of the Eurozone.[112] The results are controlled for the inclusion the ideological orientations, gender, age, and education of the respondents.[113] Table 1 summarises the main findings obtained in regression analyses.[114]

As expected, the lower the level of support for the EU expressed by Italian citizens and their political élite, the lower their feeling towards Germany. This result is consistent, including a control for the impact of ideology, which is never significantly related to Italians' views of Germany. Not surprisingly, the negative association between the perceived threat of the economic recession for Italy/Europe and feeling towards Germany is significant only after the onset of the economic crisis. In contrast, the perceived cultural threat posed by immigration is never significantly associated to the dependent variable. Finally, the negative evaluation of the influence exerted by Germany within the EU expressed by Italian public opinion and its élite is strongly associated with the negative feeling of Italians towards the former.

Table 1. Main Regression Results

Italian public opinion				
	View of Germany			
	2006	2008	2012	2016
Negative attitudes towards the EU	-	-	-	-
Economic downturn is a threat to Europe/Italy	n.s.	n.s.	n.s.	-
Immigration is a threat to Europe/Italy	n.s.			n.s.
Negative evaluation of Germany's influence in Europe			-	-
Italian national MPs				
	View of Germany			
	2006	2008	2012	2016
Negative attitudes towards the EU	-	-	-	-
Economic downturn is a threat to Europe/Italy	n.s.			n.s.
Immigration is a threat to Europe/Italy	n.s.			n.s.
Negative evaluation of Germany's influence in Europe				-

Note: -: negative and significant regression coefficient; n.s.: not significant regression coefficient.

Source: Transatlantic Trends Survey (2006; 2008; 2012); LAPS, PRIN-PEI (2016).

112 Detailed information on the exact wording of different questions and their sources is provided in Olmastroni and Pellegata (2018) and its Online Appendix.

113 Because of the very low number of observations and in order to maximise the number of cases for each predictor, we have decided to omit controls from the regression models for political élites.

114 For a detailed presentation and discussion of all the regression results see Olmastroni and Pellegata (2018) and its Online Appendix.

Conclusions

The empirical results that emerge from this study undoubtedly represent a serious challenge to the integration process. The multiple crises that Europe is recently experiencing and the policy initiatives implemented by the EU to address them have detrimental effects not only on support for the EU and its institutions, but also on the laboriously accumulated capital of respect and mutual trust among both the national governments and the citizens of the different Member States. In particular, Italian citizens and their political élite are likely to assimilate the EU and its behaviour with Germany's "hegemonic" role within the EU institutions.

However, recent public opinion surveys also show that the EU is re-gaining confidence in the eyes of the citizens, and, more interestingly, that there is a broad support, even in core countries such as Germany, for policy initiatives aimed at strengthening pan-EU solidarity (Ferrera and Pellegata 2017; PEW Research Center 2017). Many European citizens still believe in the EU, provided that the EU changes its course, carrying on solidarity-enhancing measures to re-assure voters worried about the negative consequences of the integration process and the recent crises. Our results suggest that European leaders should follow this strategy with due diligence to avoid new losses of intra-European cohesion and the consequential damage to the stability, security and development of the EU community.

References

Anderson, C.J. 1998. "When in Doubt, Use Proxies: Attitudes toward Domestic Politics and Support for European Integration." *Comparative Political Studies* 31 (5): 569-601.

Anderson, C. J., and K.Kaltenhaler. 1996. "The Dynamics of Public Opinion toward European Integration, 1973-1993." *European Journal of International Relations* 2 (2): 175-199.

Bulmer, S. 2014. "Germany and the Eurozone Crisis: Between Hegemony and Domestic Politics." *West European Politics* 37 (6): 1244-1263.

Diedrichs, U. 2010. "Germany's View of Italy in the New Century: New Challenges and Old Stereotypes." *Modern Italy* 15 (3): 293-305.

Dinger, D. 2013. *From Friends to Collaborators. A Constructivist Analysis of Changes in Italo-German Relations with the End of the Cold War*. Baden-Baden: Nomos.

Ferrera, M. 2017. "The Stein Rokkan Lecture 2016. Mission Impossible? Reconciling Economic and Social Europe after the Euro Crisis and Brexit." *European Journal of Political Research* 56 (1): 3-22.

Ferrera, M., and A. Pellegata. 2017. "Can Economic and Social Europe Be Reconciled? Citizen Views on Integration and Solidarity." *REScEU Working Paper Series*. Available at: http://www.resceu.eu/events-news/news/can-economic-and-social-europe-be-reconciled-citizens%E2%80%99-view-on-integration-and-solidarity.html, last accessed 25 August 2017.

Friedrich-Ebert-Stiftung. 2016. "Amici distanti: un sondaggio d'opinione sul rapporto tra Germania e Italia" AbteilungInternationaler-Dialog. Available at: http://library.fes.de/pdf-files/bueros/rom/12989.pdf, last accessed 25 September 2017.

Grabbe, H. 2012. "The EU Must Re-create Trust between Member States if the Benefits of Integration Are Not To Ebb Away." *EUROPP – European Politics and Policy*. Available at: http://blogs.lse.ac.uk/europpblog/2012/03/15/eu-trust-institutions, last accessed 22 July 2017.

Hooghe, L., and G. Marks. 2009. "A Postfunctionalist Theory of European Integration: From Permissive Consensus to Constraining Dissensus." *British Journal of Political Science* 39 (1): 1-23.

Hooghe, M., and S. Verhaegen. 2017. "The Effect of Political Trust and Trust in European Citizens on European identity." *European Political Science Review* 9 (2): 161-181.

Hutter, S., E. Grande, and H. Kriesi. 2016. *Politicizing Europe. Integration and Mass Politics*. Cambridge: Cambridge University Press.

Kundnani, H. 2015. "The return of the German question: why conflict between creditor and debtor states is now the defining feature of European politics." *EUROPP – European Politics and Policy*, Accessed 25 September 2017. Available at: http://bit.ly/1uNCLMl, last accessed 25 September 2017.

Matthijs, M. and K. McNamara. 2015. "The Euro Crisis' Theory Effect: Northern Saints, Southern Sinners, and the Demise of the Eurobond." *Journal of European Integration* 37 (2): 229-45.

Meiers, F. 2015. *Germany's role in the Euro crisis. Berlin's Quest for a More Perfect Monetary Union*. New York: Springer.

Olmastroni, F., and A.Pellegata (2018) "Members Apart: A Mass-Elite Comparison of Mutual Perceptions and Support for the European Union in Germany and Italy." *Contemporary Italian Politics* 10(1): 56-75.

Paterson, W. E. 2011. "The Reluctant Hegemon? Germany Moves Centre Stage in the European Union." *Journal of Common Market Studies* 49 (1): 57-75.

Pew Research Center. 2012. "European Unity on the Rocks." Research report. Available at: http://

assets.pewresearch.org/wp-content/uploads/sites/2/2012/05/Pew-Global-Attitudes-Project-European-Crisis-Report-FINAL-FOR-PRINT-May-29-2012.pdf, last accessed 5 August 2017.

Pew Research Center. 2013. "The New Sick Man of Europe: the European Union." Research report. Available atL http://www.pewglobal.org/files/2013/05/Pew-Research-Center-Global-Attitudes-Project-European-Union-Report-FINAL-FOR-PRINT-May-13-2013.pdf, last accessed 5 August 2017.

Pew Research Center. 2017. "Post-Brexit, Europeans More Favorable Toward EU." Research report. Available at: http://assets.pewresearch.org/wp-content/uploads/sites/2/2017/06/06160636/Pew-Research-Center-EU-Brexit-Report-UPDATED-June-15-2017.pdf, last accessed 25 September 2017.

Rusconi, G.E. 2008. "Die politischenWurzelnder-schleichendenEntfremdung." In *Schleichen-deEntfremdung? Deutcshland und Ital-iennachdem Fall der Maurer*, edited by G.E. Rusconi, T. Schlemmer, and H. Woller, 9-16. Munich: Oldenbourg.

Stimson, J. A. 1999. *Public Opinion in America: Moods, Cycles, and Swings*. 2nd ed., Boulder CO: Westview Press.

THE POLITICAL SPACE IN ITALY AND GERMANY DURING THE CRISIS: ITALIAN AND GERMAN POPULISM COMPARED

Hanspeter Kriesi

European University Institute, Florence

1. Introduction: The General Background of the Recent Rise of New Challenger Parties

There are two sets of factors that determine the vote for new challenger parties from the radical left and the radical right in Western Europe. On the one hand, there are the *structural transformations of society* which create new societal conflicts, and which are at the origin of a set of new demands to be represented in the political system. On the other hand, there are the *political dynamics*, especially those within the party system, which create the supply-side conditions for the representation of these demands within the political system.

The long-term trends in the development of the cleavage structure constitute the starting-point for any discussion of the determinants of the vote for challenger parties. As has been argued by various authors, north-western Europe has been characterised by the rise of a "new" cultural divide that has emerged since the 1970s as the result of successive waves of mobilisation of new social conflicts by, first, the new social movements and the New Left (new radical left parties and Green parties) and then by the radical right. The cultural issues politicised by the two waves – issues related, above all, to cultural liberalism, immigration and European integration – transformed the meaning of the cultural dimension of the two-dimensional space of party competition in north-western Europe (see Kitschelt 1994, 1995; Kriesi et al. 2008, 2012; Hooghe et al. 2002; Hooghe and Marks 2017; Bornschier 2010, 2010a, 2015): from focusing on religion, this dimension was reshaped to refer to a new fundamental conflict between universalistic (cosmopolitan) and traditionalist-communitarian (nationalistic) values.

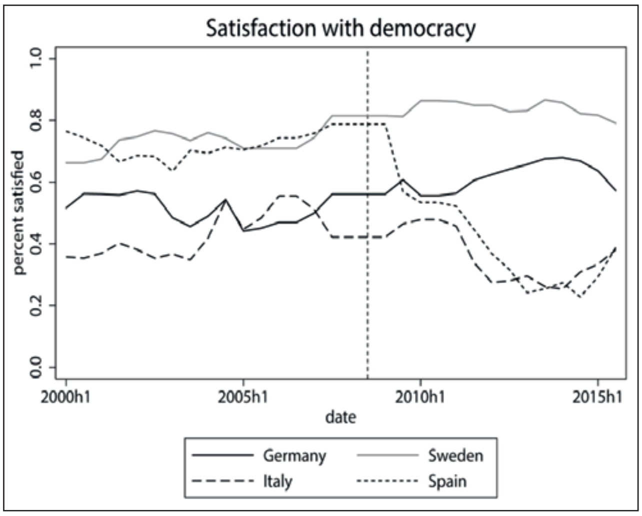
The established mainstream parties have not been able or are not ready to represent the rising demands linked to this structural conflict in society, and have also converged on the economic dimension of party competition, which has traditionally been their home turf. Accordingly, the representative function of established parties has been weakening: they have become increasingly remote from their constituencies, and their mobilising capacity has continued to decline (see Mair 2013). In particular, the fact that the mobilisation potentials created by the new fundamental conflict were largely neglected by the mainstream parties created a tension between the political representatives ("the élites") and the voters ("the people"). This made room for *the rise of new challengers within the party system*. Mair (2002: 88) has already pointed to the link between, on the one hand, the weakening of party democracy, as we knew it and, on the other, the rise of such new challengers. The new challengers not only articulate the new structural conflicts, but they also denounce the established parties for their incapacity to represent the voters' concerns. They pursue a double logic (Rooduijn et al. 2016: 34): on the one hand, they express the substantive concerns and the democratic dissatisfaction of the voters in question, while, on the other, they contribute to their voters' discontent by their populist rhetoric which claims that the established élites are betraying the people and that the sovereignty of the people ought to be restored.

As a result of the long-term trends, the dominant competition between the mainstream parties of the centre-left (Social Democrats) and the centre-right (Conservatives, Liberals and Christian-Democrats) on the economic dimension of the political space has been supplemented by the competition between the New Left (Greens) and the New Right (radical populist challengers – AfD in Germany) on the cultural dimension. While Germany saw the rise of a strong Green party, which emerged from the massive new social movements and experienced its breakthrough in the federal elections in 1983, the New Right only developed belatedly, primarily due to its national-socialist legacy. Ultimately, the *Alternative für Deutschland* (AfD) broke through in the context of the Great Recession. At its origin, the AfD opposed the repeated bailouts of Europe's crisis-ridden debtor countries. But rather rapidly, it muted into a typical populist radical right party, focusing on immigration issues and joining the ranks of the New Right that had already been established in other north-western European countries for more than thirty years. Even though it had just been founded only seven months before, and even though it had not yet developed the typical profile of a radical populist right party, the AfD obtained 4.7 per cent of the votes cast and only barely missed the five per cent threshold to enter the *Bundestag* in the 2013 federal elections. Subsequently, the party gained electoral ground in European and state-wide elections, both in West and East Germany. As argued by Bremer and Schulte-Cloos (2018), it probably benefited from the fact that it was initially not as closely associated with outright radical right positions as its predecessors from the New Right. For the outcome of the 2017 elections, it is important to keep in mind that Germany does not belong to the countries that were most heavily hit by the economic crisis. However, we should also keep in mind that, during the euro crisis, Germany became the most important representative of the "creditor" countries, and, as such, experienced the accentuation of domestic conflict over rescue measures for the "debtor" countries and institutional reforms of the Eurozone. Moreover, Germany is certainly one of the countries that has been most concerned by the refugee crisis, which first hit Europe in the summer of 2015.

Importantly, the impact of the two waves of mobilisation had been more limited in southern Europe – for reasons that have to do with the political legacy of southern European countries (long-lasting authoritarian regimes and strong communist parties, *i.e.*, a strong "old" left) and with the fact that they had been emigration countries until more recently. By contrast, southern Europe was particularly hard hit by the Great Recession – the financial crisis and eurozone crisis in the aftermath of the fall of Lehman Brothers in the autumn of 2008. These countries experienced a double crisis – an economic and a political crisis - which provided a unique opportunity for new challengers to articulate classic left-wing economic grievances and the widespread political dissatisfaction (see Hutter et al. 2018). The latter had both international and domestic origins. Internationally, the management of the eurocrisis led to interventions in national politics by supranational actors (the "*Troika*") and northern European "creditor" countries, and ended up pitting them against the southern European "debtor" countries. Domestic factors added to the resulting political discontent in southern Europe: structural problems, policy errors and misconceptions predated the euro crisis and left the southern European countries particularly ill-prepared to respond to the economic crisis. An overall sense of frustration with the political élites captivated a large share of the population and was translated into a wave of protest that swept across southern Europe (Kriesi et al. 2018). Moreover, as a result of the double crisis, southern Europe saw the rise of challengers from the radical left (such as *Podemos* in Spain, *Syriza* in Greece) or of purely populist challengers from "neither left nor right" such as the M5S in Italy.

Figure 1 gives an idea of the key political background conditions for the rise of these challengers – democratic dissatisfaction, which distinguishes north-western European countries from southern European countries. As the figure shows, the Great Recession led to a decline in democratic satisfaction in southern Europe, but not in north-western Europe. While democratic satisfaction in Germany never reached the very high levels of Sweden, it was not affected by the Great Recession and, if anything, increased until the refugee crisis broke. Only during the refugee crisis did it start to decline. By contrast, the level of satisfaction in Italy reached German levels only briefly in the mid-2000s, but then declined to very low levels in the course of the euro crisis. As is illustrated by the case of Spain, the decline in democratic dissatisfaction during the euro crisis was not an Italian speciality, but occurred throughout southern Europe. However, given that the level of satisfaction was already much lower in Italy before the crisis than in Spain, the decline of satisfaction was less precipitous in Italy than it was in Spain during the euro crisis.

Figure 1: The development of satisfaction with democracy in four European countries



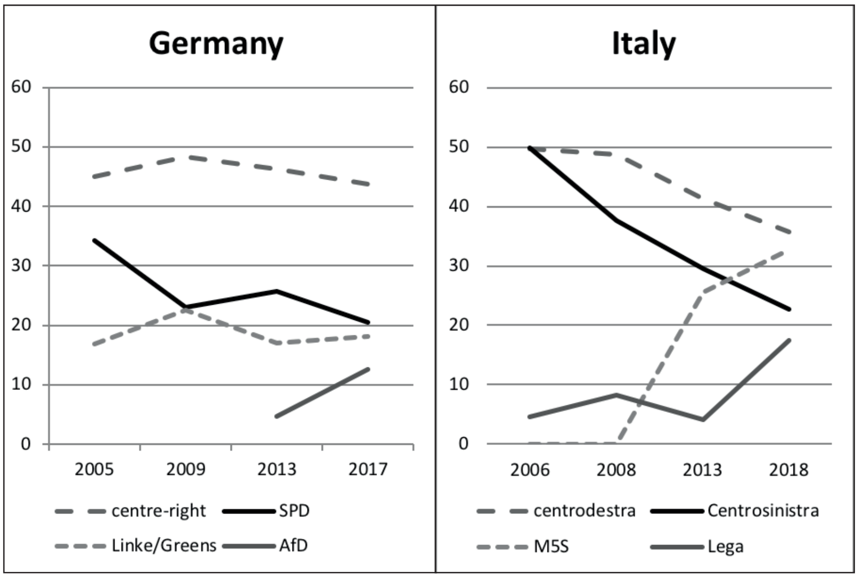
2. The Outcome of the German 2017 Elections and the Italian 2018 Elections

Against this background, let us now consider the outcome of the German 2017 elections and the Italian 2018 elections. In Germany, both incumbents lost about one fifth of their respective share of the vote. In absolute terms, the CDU-CSU was, however, punished more heavily, because its previous vote share had been far larger (41.5 per cent) than that of the SPD (25.7 per cent). Arguably, the CDU-CSU was, above all, punished for Angela Merkel's welcoming asylum policy, while the punishment of the SPD was more a sign of general wear. The SPD had suffered most in the first crisis-election in 2009, when it lost roughly a third of its share of the vote, a loss from which it never recovered. In addition to the general trends described above, the lack of a distinctive profile, a series of candidates for Chancellor (Steinmeier, Steinbrück and Schulz) who lacked any charismatic appeal, and the predicament of having to serve as a minority partner in a coalition dominated by Angela Merkel may go a long way to explain the decline of the SPD. The Liberals and, above all, the AfD were the beneficiaries of the punishment of the incumbents in the 2017 elections, while the radical and the New Left (*Linke* and Greens) stagnated.

The Italian elections resulted in the punishment of the governing PD (*Partito Democratico* - Democratic Party), the Italian equivalent of the SPD, and of the main centre-right party in opposition (Berlusconi's re-baptised *Forza Italia*, formerly *Popolo della Libertà*), as well as in the rise of the populists from both the radical right (*Lega* – the League, formerly *Lega Nord*) and the "neither left nor right" (*Movimento 5 Stelle* (M5S) - Five Star Movement). The PD lost roughly a fourth of its previous vote share (down from 25.4 to 18.7 per cent), *Forza Italia* more than a third (down from 21.6 to 14 per cent). Berlusconi's party had already lost more than 40 per cent of its vote share in the previous 2013 elections (down from 37.4 to 21.6 per cent). The PD's loss was partly due to a split: the anti-Renziani who split and campaigned under the name of "*Liberi e Uguali*" (Free and Equal) obtained 3.4 per cent. Together, the populists (M5S and *Lega*) won half of the vote (50.1 per cent in the Chamber vote), and a clear majority of the seats in both chambers. Note that, in the Italian case, the results of individual parties do not tell us as much as in Germany, because the parties form pre-electoral coalitions. As a result of these coalitions, there were actually three main electoral forces – the centre-right ("*centrodestra*"), the centre-left ("*centrosinistra*") and the M5S. Interestingly, among the three components of the centre-right we not only find *Forza Italia*, but also the *Lega* and "*Fratelli d'Italia*", an extremely nationalistic offshoot of the old *Alleanza Nazionale* created in 2014. In other words, the Italian centre-right includes the radical right populists, which would still be unthinkable in Germany. On the other side, the centre-left includes, in addition to the PD, the remnants of the Radical Party (*Più Europa*), and some other minor components, but no new populist challengers.

In order to compare the Italian electoral development with the German one, I propose to compare the combination of the CDU-CSU and the FDP with the Italian *centrodestra*, the SPD with the *centrosinistra*, and the combination of *die Linke* and *Grüne* with the M5S. Figure 2 presents the development of these camps over the last four elections. In addition to the development of these camps, the figure also presents the development of the AfD for Germany and the *Lega* separately. Looking at the two countries from this perspective, it becomes quite clear that what distinguishes the two countries is not so much the rise of the radical populist right, which rose to a similar extent in both countries in the most recent elections. What really distinguishes the two countries is *the rise of M5S* and *the spectacular decline of both the centre-left and the traditional centre-right*. While the combined radical and New Left in Germany stagnated throughout the 2000s, its functional equivalent in Italy – M5S – proved to be a spectacular success. Coming from nowhere it obtained a fourth of the vote (25.6 per cent) in 2013, and rose to a third (32.7 per cent) in 2018. Without any doubt, it benefited from the political dissatisfaction of the Italians, which reached new heights after the experience with the Monti government of technocrats (2011-2012) that was supported by all the mainstream parties. The decline of the traditional centre-right has been particularly spectacular and is, however, not fully represented in Figure 2. The reason for this is the above-mentioned inclusion of the *Lega* in the centre-right. Between 2013 and 2018, a shift in the relative power of the components of the centre-right occurred in Italy, with Berlusconi's *Forza Italia* losing its polar position to the *Lega*. Back in 2013, the *Lega* still had to recover from a major scandal in its own ranks that dates back to the spring of 2012. By 2018, however, its new leader, Matteo Salvini, had succeeded in re-positioning the former regionalist party as a classic radical populist right party that now mobilised across the entire country, above all on issues of immigration and Euroscepticism.

Figure 2: The outcome of the four most recent German and Italian elections



However, the *Lega* still kept its stronghold in northern Italy and met with great scepticism in the South. In order to appreciate the outcome of the Italian 2018 elections correctly, it is actually very important to take into account the *regional differences* in the electoral outcome. Figure 3 compares a typical northern district – Lombardia 3, which includes the cities of Brescia, Bergamo and Treviglio, with a central district – Toscana – and a southern district – Sicilia 2, which includes Messina, Catania, Ragusa and Syracusa. In Lombardy, the centre-right largely dominated, in Sicily, M5S took almost half of the vote, while in Tuscany the three camps of the current Italian party system were of much more equal strength. If we add the AfD to the centre-right to make it comparable to the Italian centre-right, the similarities between the electoral outcome in Germany and Lombardy are striking, as is also shown in Figure 3. Table 1 is added to clarify that the similarity between the two is more apparent than real, because the power relations within the centre-right are actually very different in Germany and Lombardy: while the mainstream CDU-CSU dominates the centre-right in Germany, it is the *Lega* that dominates it in Lombardy (and in Tuscany, too).

Figure 3: Regional differences in the Italian electoral outcome 2018, and German electoral outcome 2017

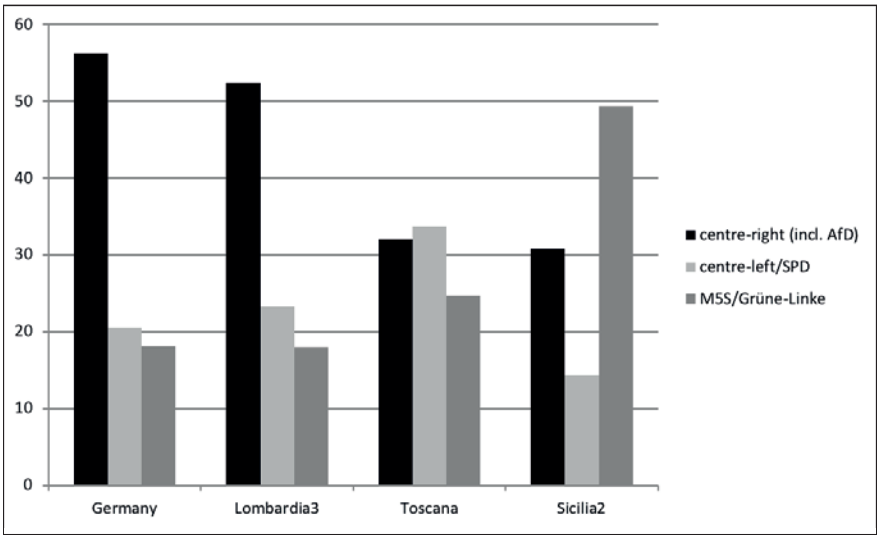


Table 1: Northern Italy vs Germany, outcome of last national elections

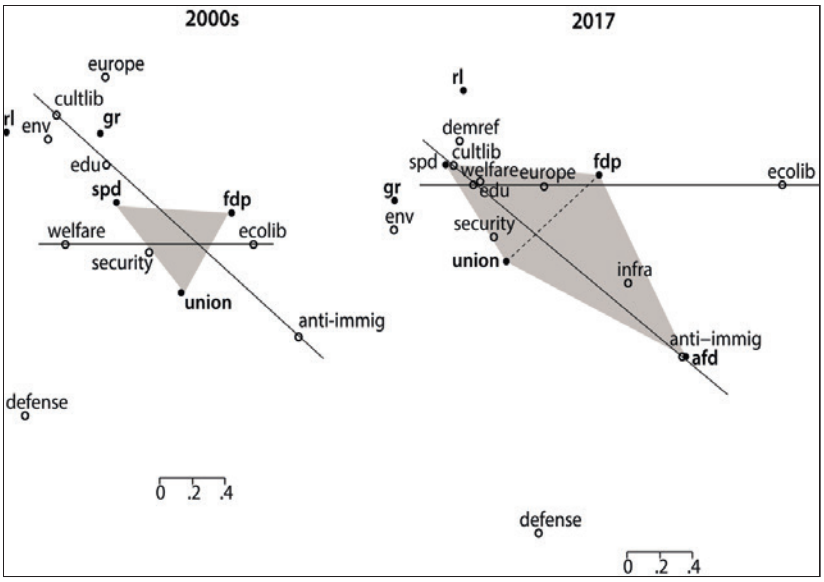
Party	Germany	Lombardia3
centre-right	56.3	52.4
Forza Italia-UDC/CDU-CSU Lega/AfD others	32.9 12.6 10.8	13.7 34.3 4.4
centre-left	20.5	23.3
M5S/Grüne-Linke	18.1	18.0

3. The Structure of the Party Systems in Germany and in Italy

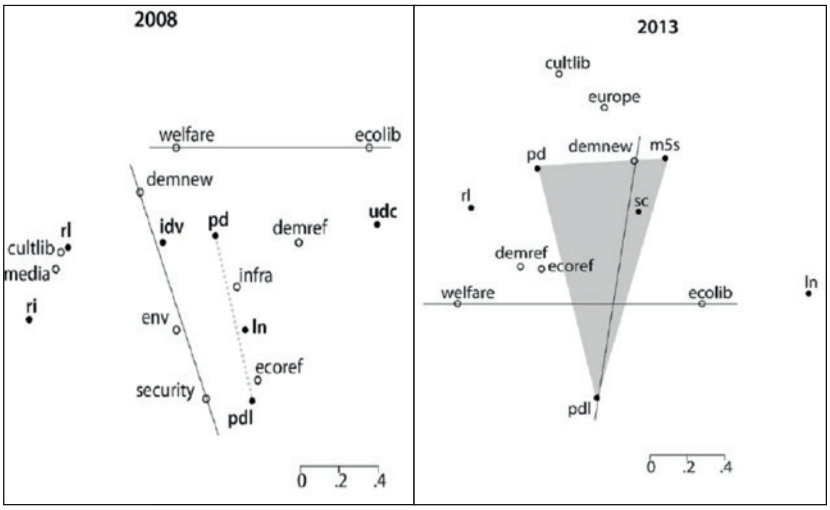
The return of the FDP to the German *Bundestag* did not change much in the structure of the party system, but the establishment of the AfD did. As is shown in Figure 4, the German party system is structured by an economic and a cultural dimension which is closely correlated, and appears to be multi-polar as well. However, this multi-polarity is more apparent than real: with the exception of the AfD, which occupies a similar position as the radical populist right parties in north-western Europe, all the parties are located in the upper left-hand corner of the space, relatively close to the pro-welfare pole of the economic dimension (with the exception of the FDP) and relatively close to cultural liberalism. It is the contrast between the New Right and the rest of the parties which serves as the crucial structuring device in the German party system today. We should, however, keep in mind that the AfD still has a somewhat limited electoral weight, which means that it contributes only to a limited extent to the polarisation of the German party system. Compared to the position of the New Right, the differences between the remaining parties appear of minor importance.

Figure 4: Political spaces in Germany and Italy

a) Germany



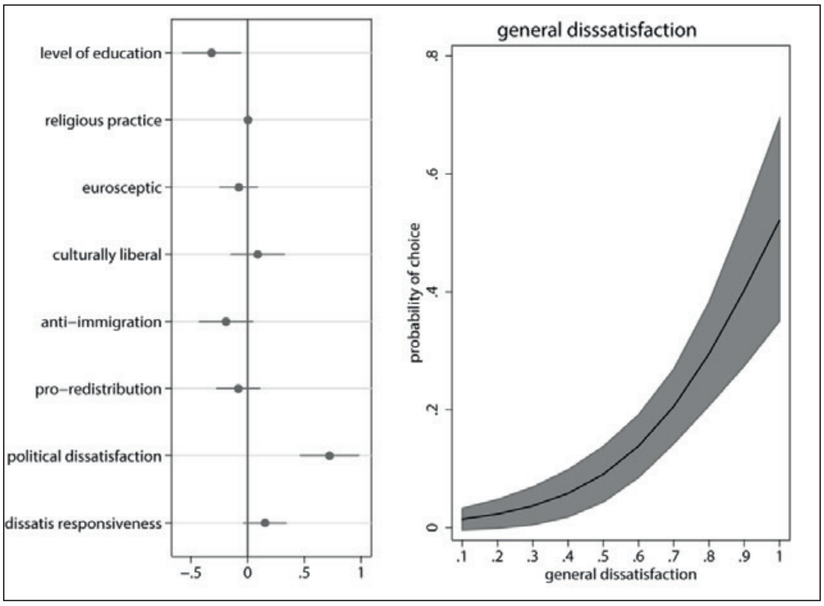
b) Italy



For Italy, we do not have the data for the 2018 elections yet, which is why Figure 4 presents the structure of the Italian party system before the initial rise of M5S (2008) and after its successive rise (2013) (see Karremans et al. 2018). Before the crisis and before the rise of M5S, the Italian political space was structured mostly around a bipolar opposition between the *centrosinistra* (PD, IdV) and the *centrodestra* (PdL + Lega), with issues of welfare, democratic renewal and cultural liberalism on one side, opposed to issues of security on the other. The rather unstructured configuration reflects the unique role played by Silvio Berlusconi, the leader of *Forza Italia* in Italian politics. The election of 2008 roughly coincides with the apex of Berlusconi's personal dominance over Italian politics. The rather unusual configuration of the political space at the time is likely to be related to the peculiarities of this unique period, during which political competition revolved more on the personality of individual leaders than on a programme or manifesto. The Berlusconi-factor, in turn, also had an important impact on the 2013 electoral campaign. While, in 2008, political competition tended to be one-dimensional, in 2013, it became two-dimensional. As shown in Figure 4, the economic and cultural dimensions only play a marginal role in the structuring of political competition in 2013. What really structures the political space, instead, are political issues, and, in particular, the issue of political renewal. On the one hand, we find the PD and M5S (and Mario Monti's *Scelta Civica*) pleading in favour of political renewal. On the other hand, the PdL represents the opposite pole with Berlusconi becoming an issue himself, as the main exponent of a political class that the challengers asked to be replaced.

The crucial role of the political crisis in the 2013 Italian elections is confirmed by an analysis of the determinants of the vote for M5S in the elections. This analysis is based upon the ESS6, which went into the field in Italy after these elections. While voters for parties on the radical left and the radical right typically make their choice based upon a combination of substantive concerns (economic concerns such as re-distribution for the radical left voters and cultural concerns such as opposition to immigration for the radical right voters) and of democratic discontent, the voters for M5S did not distinguish themselves from the mainstream voters with respect to any substantive preferences. Instead, the key determinant for the M5S vote was general dissatisfaction with the way democracy worked in Italy. This is illustrated by Figure 5, which presents the average marginal effects (estimated with logit models based upon ESS6 data) for some key substantive preferences and for two measures of democratic discontent (general political dissatisfaction and dissatisfaction with government responsiveness).

Figure 5: Effects of cultural/economic preferences and democratic dissatisfaction on vote for M5S (2013)



4. The consequences of these election outcomes

From these election results, we can observe a weakening of the government in both countries. The German elections resulted in a configuration in parliament which made coalition formation difficult and led to the Federal Republic's longest period without a government since World War II. A first attempt to form a so-called "Jamaica" coalition composed of the CDU-CSU, the Liberals (FDP) and the Greens spectacularly failed in late November 2017. After this failure, a grand coalition or a CDU-CSU minority government remained as the only option. Although the leader of the SPD had originally excluded a remake of the grand coalition between the CDU-CSU and the SPD, after the intervention of the President, the SPD's leadership reluctantly decided to enter coalition negotiations nevertheless. These negotiations dragged on until February and were eventually concluded with a coalition contract that still had to be approved by the two parties. In the case of the SPD, this meant consulting its 460,000 members, part of whom heavily contested the renewal of a grand coalition. After a four month stalemate, the SPD membership eventually approved the contract on 4 March 2018 by a two-thirds majority. The old and new chancellor, Angela Merkel, has paid a high price for the new coalition government. Although even more weakened in the elections than the CDU-CSU, the SPD obtained important concessions in the coalition negotiations and sees its position strengthened in the future grand coalition. After the installation of the grand coalition, there is the prospect of a sustained period of a stable, albeit weak, government.

In Italy, the configuration in Parliament resulting from the 2018 election made government formation equally difficult. No feasible combination of parties seemed to have the number of seats necessary to form a government. The centre-right, which claimed to have won the elections, fell clearly short of the necessary majority, as did M5S, which also claimed to have won the elections. A coalition between M5S and the centre-left, which was attempted by M5S was vetoed by the Renziani in the PD. After a protracted period of negotiations that lasted almost three months and a final stretch of extremely tense negotiations between the prospective coalition partners and the Italian President Sergio Mattarella, the originally rather unlikely combination of the two populist parties – the *Lega* and the M5S – succeeded in forming a government. This government promises to be weak as well, given its internal contradictions. Thus, the combination of the substantive economic demands of the two coalition partners promises to be explosive: while the *Lega* intends to implement the centre-right's key electoral promise of a flat tax for both individuals and corporations, which will reduce government revenue considerably, the M5S intends to implement a very costly social security project, the so-called *reddito di cittadinanza* (a sort of minimum income for the unemployed). Moreover, the *Lega* plans to tighten immigration legislation in a heavy-handed manner, whereas the M5S has been supported by many former voters from the left, who are rather opposed to such measures.

The latent Euroscepticism of both of these parties, but especially of the *Lega*, will make for difficult relations with Italy's European partners. Already, the new cabinet is seeking to re-negotiate the rules for the distribution of refugees as well as the rules for economic deficits in the EU. The new Italian government is likely to re-inforce German prudence which has already been putting the brake on the great plans for Europe of the new French President Emmanuel Macron. But given that Italy is one of the founding members of the EU, the sanctioning capacity of the EU, with regard to the difficulties which are likely to be created by the new Italian government, is likely to be rather limited. By contrast, the markets are likely to impose more strict constraints on this government, as was illustrated during the final phase of the government formation: the markets reacted sharply when the leaders of the two populist parties submitted a list of prospective ministers to the President of Italy which included a finance minister who was an explicit opponent of Italy's membership in the Eurozone: the two-year yield on Italian government bonds jumped from 0.27 to 2.72 per cent over three trading days at the height of the negotiations between the President and the two populist leaders. When the latter backed down and were prepared to compromise, the markets calmed down to some extent, although it remains to be seen how they will react to the economic policies, once the new government attempts to implement them.

5. Conclusion

After the last elections, Germany is once more governed from the centre, while Italy – a first in Western Europe – is governed by a coalition of populist parties. The German grand coalition is not so grand after all. It is based upon a tight absolute majority of 53 per cent of the vote. For the time being, the challengers from both left and right are marginalised in Germany, and the question is how they will react to their powerlessness. They might get another chance in the not too distant future. The fact that the German government rests on a rather small popular base suggests that the electoral situation in Germany is far from stable. The major conflict between the nationalist-conservative forces defending the nation-state and its citizens and the forward-looking forces promoting cultural liberalism, European integration, and openness to immigrants is far from settled in Germany.

In Italy, the new populist coalition is articulating both, the conflict between cosmopolitan and nationalist-conservative forces, and the economic conflict between the rich and the poor, which is also a regional conflict between the North and the South. In both of these conflicts, the two components of the governing coalition tend to defend opposing interests: while the *Lega* defends the nationalistic position, especially with regard to immigration, the M5S is more multi-culturally oriented, and, while the M5S defends the poor Southerners, the *Lega* defends the Northerners who are unwilling to pay for the South. How the two coalition partners intend to square the circle remains to be seen, but it is clear that the Italian electoral situation is also far from stable.

References

Betz, Hans-Georg (2015). "The Revenge of the Ploucs: The Revival of Radical Populism under Marine Le Pen in France", in: Hanspeter Kriesi and Takis Pappas (eds), *European Populism in the Shadow of the Great Recession*. Colchester: ECPR Press.

Bornschier, Simon (2015). "The New Cultural Conflict, Polarization, and Representation in the Swiss Party System, 1975-2011", *Swiss Political Science Review* 21, 4: 680-701

Bornschier, Simon (2010). *Cleavage Politics and the Populist Right. The New Cultural Conflict in Western Europe*. Philadelphia PA: Temple University Press.

Bornschier, Simon (2010a). "The New Cultural Divide and the Two-Dimensional Political Space in Western Europe", *West European Politics* 33 (3): 419-444.

Bremer, Björn, and Julia Schulte-Cloos (2018). "No Country for the New Right? Restructuring British and German Party Politics, in: *Restructuring European Party Politics in Times of Crises*, edited by Swen Hutter and Hanspeter Kriesi, unpubl. Ms, Florence: European University Institute.

Hutter, Swen, and Hanspeter Kriesi (eds) (2018). *Restructuring European Party Politics in Times of Crises*, unpubl. Ms., Florence: European University Institute.

Hutter, Swen, Hanspeter Kriesi and Guillem Vidal (2018). Old versus New Politics: The Political Spaces in Southern Europe in Times of Crises, *Party Politics* 24 (1): 10-22.

Kitschelt, Herbert (1994). *The Transformation of European Social Democracy*. Cambridge: Cambridge University Press.

Kitschelt, Herbert (1995). *The Radical Right in Western Europe: A Comparative Analysis*. Ann Arbor MI: University of Michigan Press.

Karremans, Johannes, Giorgio Malet and Davide Morisi (2018). Chapter 6: "Italy – The End of Bipolarism: Restructuring in an Unstable Party System", in: *Restructuring European Party Politics in Times of Crises*, edited by Swen Hutter and Hanspeter Kriesi, unpubl. Ms, Florence: European University Institute.

Kriesi, Hanspeter, Jasmine Lorenzini and Silja Häusermann (eds.) (2018). *Contention in Times of Crises. Comparing Political Protest in 30 European Countries: 2000-2015*, unpubl. Ms., Florence:European University Institute.

Kriesi, Hanspeter, Edgar Grande, Martin Dolezal, Marc Helbling, Dominic Höglinger, Swen Hutter and Bruno Wueest (2012). *Political Conflict in Western Europe*. Cambridge: Cambridge University Press.

Kriesi, Hanspeter, Edgar Grande, Romain Lachat, Martin Dolezal, Simon Bornschier, Timotheos Frey (2008). *West European Politics in the Age of Globalization*. Cambridge: Cambridge University Press.

Mair, Peter 2013. *Ruling the Void: The Hollowing of Western Democracy*. London, New York: Verso Books.

Mair, Peter (2002). "Populist Democracy vs Party Democracy", in: *Democracies and the Populist Challenge*, edited by Yves Mény and Yves Surel. Basingstoke: Palgrave, pp. 81-98.

Roodujin, Matthijs, Wouter van der Brug, Sarah L. de Lange 2016. "Expressing or Fueling Discontent? The Relationship between Populist Voting and Political Discontent", *Electoral Studies* 43 (1): 32-40.

THE POLITICAL ECONOMY OF RECOVERY IN SOUTHERN EUROPE

Manos Matsaganis
Politecnico di Milano

Has Southern Europe recovered from the Great Recession and the Eurozone crisis?

The question is simple, but the answer is complex – and differs from the point of view of the economy, the social situation, and politics. A laconic assessment, valid as of September 2018, would have to be 'partly', 'not much', 'not at all' respectively. For a slightly fuller one, read on.

1. The economy

In 2017, GDP in the EU grew faster than expected, by 2.4%. This may look rather modest, but represented, as DG-ECFIN pointed out, "the highest growth rate in 10 years". Furthermore, for the first time since the onset of the crisis, in 2017 growth was positive in all EU member states.

In 2013-2017, Southern Europe returned to positive rates of growth. The economy grew by a cumulative 11.5% in Spain, and 7.2% in Portugal. Italy (3.4%) and Greece (1.6%) did less well. Over the same period, the European economy as a whole (EU28) expanded by 8.7%.

Nevertheless, Southern European economies have not yet regained the ground they lost during the Great Recession and the Eurozone crisis. By the end of 2017, only in Spain had GDP surpassed its 2008 level (by a mere 1.6%). In Portugal, it was 1.2% lower. In Italy, the shortfall was 4.4%. In Greece, the size of the economy was 25.1% smaller than it was pre-crisis[115].

Why is it that the recovery has been so slow and uneven in Southern Europe?

In the short run, growth is driven by a combination of consumption, investment, and exports. In the longer run, growth depends on rising productivity (and more jobs created than destroyed). In turn, rising productivity depends once again on more (and more productive) investment.

On this count, the evidence gives plenty of cause for concern. As explained elsewhere[116], in the context of harsh, externally imposed austerity, national governments (and firms) have found it expedient to cut investment by more than they cut consumption spending.

This was true in all countries: gross fixed capital formation in the EU was cut back by 13.4% in 2008-2013, while over the same period final consumption expenditure held constant (-0.1%). In Southern Europe, where consumption fell quite significantly during the crisis, investment collapsed spectacularly: comparing 2008 and 2013, the cumulative decline was 25.5% in Italy, 35.0% and 36.5% in Spain and Portugal respectively, and a massive 61.3% in Greece.

In 2013-2017, investment bounced back in Europe, registering an increase of 14.4%, while consumption rose by half as much (7.1%) in the same period. By doing so, pre-crisis levels of gross fixed capital formation were almost fully restored (-1.0% in 2008-2017 in the EU28). During the recovery, investment also fared better than consumption in the four South European member states, but that was not nearly enough to make up for the losses of the previous period. By the end of 2017, gross fixed capital formation in Italy was 20.5% lower than it had been in 2008, 21.4% in Spain, 23.9% in Portugal, and as much as 59.1% lower in Greece (Table 1).

115 See Eurostat "GDP and main components (output, expenditure and income) [nama_10_gdp]", NA_ITEM: Gross domestic product at market prices, UNIT: Chain linked volumes, index 2010=100. Last update: 04/09/2018. Extracted on: 05/09/2018.

116 See Perez S.A. & Matsaganis M. (2018) The political economy of austerity in Southern Europe. New Political Economy 23 (2) 192-207.

Table 1: Consumption and investment (2008-2017)

Final consumption expenditure	2008-2013	2013-2017	2008-2017
EU28	-0.1	7.1	7.0
Greece	-24.3	-0.4	-24.6
Spain	-9.3	8.8	-1.3
Italy	-5.7	3.6	-2.3
Portugal	-9.4	7.3	-2.8
Gross fixed capital formation	2008-2013	2013-2017	2008-2017
EU28	-13.4	14.4	-1.0
Greece	-61.3	5.7	-59.1
Spain	-35.0	21.1	-21.4
Italy	-25.5	6.7	-20.5
Portugal	-36.5	19.9	-23.9

Note: The figures are cumulative rates of change in the end of a period relative to the start of the period, as a percentage of the latter.

Source: Eurostat "GDP and main components (output, expenditure and income) [nama_10_gdp]", NA_ITEM: Final consumption expenditure / Gross fixed capital formation, UNIT: Chain linked volumes, index 2010=100. Last update: 04/09/2018. Extracted on: 05/09/2018.

vvvReal labour productivity per hour worked improved throughout Europe during the crisis (+5.1% in the EU28 in 2008-2013). This implies that the jobs destroyed were less productive than those saved or created anew. This was even more the case in Spain (+10.0%) and Portugal (+6.7%). However, labour productivity barely increased in Italy (+1.1% in 2008-2013), and actually *fell* in Greece during the crisis (-8.4%).

As the economy picked up, creating more jobs (including some less productive ones), advances in labour productivity were slower (+3.7% in the EU28 in 2013-2017). Nevertheless, with the exception of Spain (+2.8%), real labour productivity per hour worked declined in Portugal and Greece (-0.9% and -0.6% respectively), and stagnated in Italy (0.0% in 2013-2017)[117]. In view of that, except in Spain, there was little evidence of a shift to a higher-productivity growth model (and, in the case of Greece, clear signs of a retreat to an even lower-productivity growth model).

In terms of export performance, the fortunes of South European economies began to diverge considerably during the crisis. The fall in domestic demand presented all firms in all countries with a strong incentive to switch to export markets. However, the degree to which they actually succeeded in doing so differed greatly between countries. In the EU as a whole, exports grew by 9.1% in 2008-2013. In Portugal and Spain, a strong export performance (+16.4% and +10.2% respectively) cushioned the effects of the crisis on employment and earnings. In contrast, exports decreased in Italy (-0.7%) and, especially, in Greece (-12.2%) over the same period, contributing to the recession instead of mitigating its impact.

More recently, exports increased significantly throughout Europe (+20.7% in the EU28 in 2013-2017). This was also the case in the four South European member states, although again at varying degrees: in 2013-2017, exports grew by 24.7% in Portugal, by 19.5% in Spain, by 16.5% in Greece, and by 15.8% in Italy.

Overall, relative to the EU as a whole, exports grew faster in Portugal, and just as fast in Spain. On the contrary, in Italy, and especially Greece, exports failed to provide the necessary stimulus. Comparing the latest figures with pre-crisis, in 2017 exports were 45.2% higher than they had been in in 2008 in Portugal, and 31.7% in Spain (same as the EU28 average). Over the same period, exports grew by only 14.9% in Italy, while they barely grew at all in Greece (+2.2%)[118].

Summing up, in terms of a range of economic indicators (economic growth, resumption of investment, increases in labour productivity, and export performance), Spain and Portugal did significantly better than Italy during the recovery, while Greece fell further behind.

117 See Eurostat "Labour productivity and unit labour costs [nama_10_lp_ulc]", NA_ITEM: Real labour productivity per hour worked, UNIT: Index 2010=100. Last update: 05/09/2018. Extracted on: 05/09/2018.

118 See Eurostat "GDP and main components (output, expenditure and income) [nama_10_gdp]", NA_ITEM: Exports of goods and services, UNIT: Chain linked volumes, index 2010=100. Last update: 05/09/2018. Extracted on: 05/09/2018.

2. The social situation

The rise in unemployment was the most characteristic feature of the Great Recession and the Eurozone crisis. There is no doubt that the unemployment rate is on the decrease in Europe, including in its Southern periphery. Nevertheless, because of recent changes in labour supply (demography and migration), there has been less net job creation than might be thought from inspection of changes in the unemployment rate alone.

In fact, focusing on the total number of workers in jobs makes it clear that fewer jobs have been created during the recovery in Southern Europe than were lost during the crisis (Figure 1).

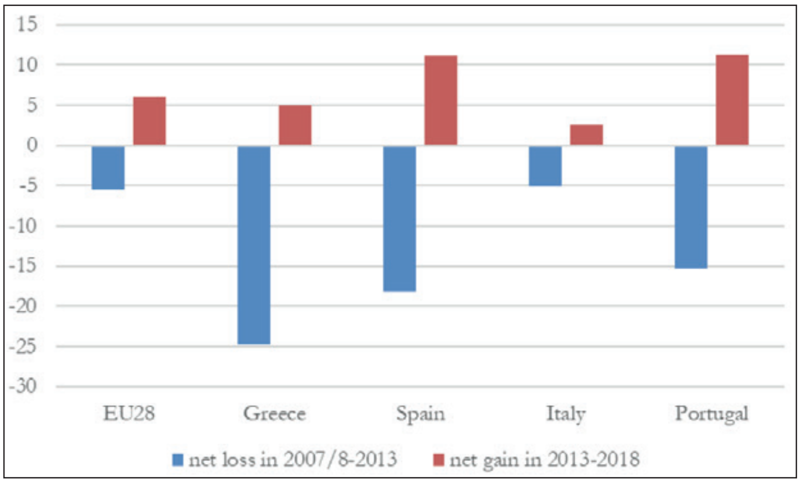
Specifically, in the EU as a whole, there were 13.43 million more workers in 2018q1 than there had been in 2013q1. By comparison, there were 12.25 million *fewer* workers in 2013q1 than there had been in 2008q3. In view of that, the ratio between net job creation in the recovery and net job destruction in the crisis for the European economy as a whole is 1.10 (i.e. 10% more jobs have been created in the recent period than were lost in the previous period)[119].

Repeating the exercise for the South European economies (and taking into account differences in the timing of peak and trough, and the latest data available) shows that none of the four has yet created as many jobs in the recovery as were lost during the crisis.

Portugal, with a ratio of 0.74, implying that 26% fewer jobs have been recently created than were previously lost, comes closest. The corresponding ratio in Spain is 0.61. In Italy, it is only 0.50 (i.e. only half the jobs lost have been recently created). In Greece, the ratio of net job creation to net job destruction is a disappointing 0.20 (i.e. for every five jobs lost in the crisis, only one has been created in the recovery).

Moreover, fewer of the jobs that have been created since the trough of the recession are full-time than used to be the case pre-crisis. Even though the share of part-time in total employment is still lower in the four South European economies than in the EU as a whole, it went up in all four at a faster rate than average between 2008 and 2013. Thereafter, it continued to rise in Italy and Greece, though it has fallen back in Spain and, especially, Portugal. In 2017, the share of part-time in total employment was 4.4 percentage points higher than in 2008 in Italy, 4.3 in Greece, 3.3 in Spain, while it was practically constant (+0.1 pp.) in Portugal. In the EU as a whole, the share of part-time in total employment rose by 1.9 percentage points in 2008-2017[120].

Figure 1: Net job creation (2007-2018)



Notes: The blue bars show the difference in numbers of workers in employment at the trough of the recession, relative to the pre-crisis peak. The red bars show the difference in numbers of workers in employment at the latest quarter for which data are available, relative to the trough of the recession. Both differences are normalised as a percentage of the number of workers in employment in 2008q3. Pre-crisis peak was 2007q3 in Spain, 2008q2 in Italy and Portugal, 2008q3 in Greece and EU28. The trough of the recession was 2013q1 in the EU28 and all South European countries except Greece (2013q4). The latest quarter for which data are available is 2018q2 in Spain and Portugal, and 2018q1 everywhere else.

Source: Eurostat "Employment by sex, age and citizenship (1 000) [lfsq_egan]", SEX: Total, AGE: From 15 to 64 years, CITIZEN: Total, UNIT: Thousand. Last update: 04/09/2018. Extracted on: 05/09/2018.

119 Note that job creation and job destruction take place simultaneously at all times in all economies. The difference between the two is 'net job creation' (or, when it is negative, 'net job destruction'). Note also that the terms 'net job creation' and 'net job destruction' are used a bit loosely in the text. Since it is possible for a worker to hold more than one job at the same time, changes in the number of workers in employment (as reported in the text) need not be identical to changes in the number of jobs.

120 See Eurostat "Part-time employment as percentage of the total employment, by sex and age (%) [lfsa_eppga]", SEX: Total, AGE: From 15 to 64 years. Last update: 03/08/2018. Extracted on: 05/09/2018.

Wage growth remained sluggish. In hourly terms, taking into account the growth in part-time work, between 2013 and 2016 there was virtually zero growth in real wages in Southern Europe except for Spain (1.7%). In the EU as a whole, real compensation of employees per hour worked increased by 3.3%. In 2008-2016, real hourly wages fell by 0.7% in Italy, 1.2% in Spain, 4.4% in Portugal, and 16.1% in Greece. In the EU as a whole, they rose by 4.2%[121].

Poor performance in terms of net job creation and sluggish wage growth contributed to rising inequality (except in Portugal). Between 2008 and 2013, the income quintile ratio (S80/S20) rose significantly in Greece (+0.7 points), Italy (+0.6) and Spain (+0.7). In 2013-2016 it continued to grow in Italy (+0.5) and Spain (+0.3), though it remained stable in Greece. In Portugal, the S80/S20 ratio fell by 0.1 points in each period. In the EU28, it increased slightly (by 0.1 and 0.2 points in 2008-2013 and 2013-2016 respectively), though at 5.2 in 2016 it still remained well below the levels of Southern Europe (5.9 in Portugal, 6.3 in Italy, 6.6 in Greece and Spain)[122].

Estimates of the Gini index revealed similar trends. In 2008-2016, the value of the index rose significantly in Greece, Spain and Italy, and fell slightly in Portugal. In 2016, all four Southern European countries were clustered together near the top of the income inequality league table in the EU, ranking 5th to 8th, that is between 2 and 4 percentage points above the EU average. Among all member states, the Gini coefficient was now higher only in Bulgaria, Lithuania, Romania and Latvia – and, in the latter two countries, only very slightly so[123].

121 See Eurostat "Labour productivity and unit labour costs [nama_10_lp_ulc]", NA_ITEM: Real compensation of employees per hour worked based on hCPI, UNIT: Euro (2015 prices). Last update: 20/12/2017. Extracted on: 30/12/2017.

122 See Eurostat "S80/S20 income quintile share ratio by sex and selected age group - EU-SILC survey [ilc_di11]", INDIC_IL: Inequality of income distribution (income quintile share ratio). Last update: 18/01/2018. Extracted on: 24/01/2018.

123 See Eurostat "Gini coefficient of equivalised disposable income - EU-SILC survey [ilc_di12]". Last update: 08/11/2017. Extracted on: 13/01/2018.

Summing up, in terms of a range of social indicators (net job creation, real wage growth, and income inequality), all four South European economies lost ground relative to the EU as a whole. Portugal did better in terms of net job creation and income inequality (though not as regards real wage growth), followed by Spain in terms of real wage growth and, partly, net job creation (though not as regards income inequality). Italy did less well, and Greece did worst.

3. Politics

This is not the right place (nor, for that matter, the right author) for a discussion of recent political developments in Southern Europe. However, it is to see that one common aspect is the rise of new political actors in the context of great political instability. Again, Portugal stands out, with a socialist minority government enjoying the external support of the two left parties in parliament since October 2015. In Spain, two new parties, the leftist *Podemos* and the centrist *Ciudadanos* are challenging the primacy of the socialist PSOE and conservative PP, in the context of a constitutional crisis provoked by the 'declaration of independence' of Catalonia. In Italy, the March 2018 general election brought to power a "souvranist" coalition of the populist *Five Star Movement* and the anti-immigration *Lega*. In Greece, a coalition of the radical left and the nationalist right is in power since January 2015. In all four countries, the political parties that introduced austerity policies, usually reluctantly, lost ground and were evicted from power.

Popular sentiments towards the EU partly reflect that reaction. In October 2008, the share of Eurobarometer respondents who 'tended to trust the EU' was 41% in Italy, 50% in Portugal, 55% in Spain, and 58% in Greece (relative to 47% across the EU as a whole). Within less than five years (in May 2013), trust in the EU had collapsed: it had fallen to 25% in Italy, 24% in Portugal, 17% in Spain, and 19% in Greece (31% in the EU as a whole). By May 2017, trust in the EU had bounced back, especially in Portugal (54%), and Spain

(40%), to a lesser degree in Italy (36%), and much less Greece (22%). In the EU as a whole, it stood at 47%.

It is difficult to miss the connection between the rise of anti-EU popular sentiments and political actors in Europe's Southern periphery on the one hand, and the management of the Eurozone crisis by Germany and other core countries on the other hand. For instance, Italy used to be one of the most pro-EU countries in Europe. In 2011-2018, successive Italian governments (headed in turn by Monti, Letta, Renzi, and Gentiloni) failed to find solutions within the constraints of EU commitments. Some of the reasons for that failure are obviously domestic. Some but not all: perhaps it is time we recognised that, given external constraints, being a pro-EU reformer in the European periphery is next to impossible.

ACCOMMODATING EU'S INFLUENCE VS PROTECTING NATIONAL SOVEREIGNTY.

THE FIGHT AGAINST POVERTY IN ITALY AND GERMANY AT THE TIME OF "EUROPE 2020"

Ilaria Madama and Matteo Jessoula
University of Milan

I. Introduction[124]

In the field of anti-poverty policies, which have constituted a major brick of 'social Europe' since decades (*cf.* Armstrong 2010), the EU's overarching strategy *Europe 2020* has actually marked a major discontinuity *vis à vis* the Social OMC of the Lisbon phase (2000–10). Not only did the new strategy provide an institutional framework – the European 'Semester' – for stronger (at least formally) *integration* between social – mainly anti-poverty – policies and the broader European framework for financial-economic governance. It also replaced the vague objective of 'eradicating poverty', included in the former Lisbon Strategy, with a possibly less ambitious but more realistic and potentially more incisive quantified poverty target. Lifting at least 20 million people out of poverty and social exclusion by 2020 is, in fact, one of the five targets as well as the main social innovation of Europe 2020. In order to reach the quantified poverty target, in 2012 a key link between the new strategy and European funds was introduced: within the 2014–20 multi-annual financial framework, Member States (MS) are actually required to allocate at least 20 per cent of European Social Fund's resources to combating poverty.

124 This text elaborates on the findings collected in the volume "Fighting poverty and social exclusion in the EU. A chance in Europe 2020" (Jessoula, M. and Madama, I., eds., Routledge, 2018) and has been written in the context of the RESCEU Project (Reconciling economic and social Europe, www.resceu.eu), funded by the European Research Council (Advanced Grant no. 340534).

As a result of these novelties, the new strategy was initially welcomed as a possible promising step towards a stronger social Europe (cf. Marlier *et al.* 2010). However, later contributions have cast doubts on the effectiveness of both the new strategy – and more generally the EU – in combating poverty and social exclusion (Pochet 2010; Copeland and Daly 2012 and 2014; Armstrong 2012; Peña-Casas 2012), due to limited progress along several dimensions (cf. Bouget *et al.* 2015; Frazer and Marlier 2016) and especially towards the target which seems, in fact, unreachable.

Against such backdrop, this chapter asks *whether* and *how* Europe has mattered in the fight against poverty and social exclusion under the novel Europe 2020 institutional framework, by comparing the effects entailed in Italy and Germany, during the first five annual cycles of the European Semester. The two countries allow for a particularly stimulating comparative assessement, as they represent two rather opposite worlds of implementation (*cf.* Jessoula and Madama 2018), featuring distinct domestic patterns and effects that call for interpretation.

The chapter is organised as follows. Section 2 offers a comparative overview of the empirical evidence about the reception of Europe 2020 in the two countries and the national-supranational interactions around the issue of poverty and social exclusion over the first five cycles of the Semester. Section 3 deals with the factors affecting the diverse implementation of EU inputs at the domestic level in the two countries, emphasising the relevance of national politico-institutional contexts, as filtering EU's influence. Section 4 concludes.

II. Accommodating EU's influence vs protecting national sovereignty: two worlds of domestic effects

The investigation of EU's impact in the context of non-binding, *soft* coordination processes is not an easy task. After the launch of the Lisbon Strategy in 2000s, an intense academic debate has flourished around the potential and the limits of policy coordination mechanisms based on soft-law, as those foreween by the social-OMC. The assessments of the effectiveness of such procesess to prompt national

social policy developments in line with common objectives and/or supranational guidelines and recommendations have however resulted in rather contrasting findings. Some authors have emphasized the weakness of the Social OMC, suggesting that both its non-binding nature and the lack of sanctions have hampered the attainment of commonly agreed objectives (i.e. Barbier 2005; Armstrong 2006). Others have interpreted the lack of coercion as a fruitful condition for the unfolding of experimentations and learning processes through deliberative forms of governance, while respecting MS heterogeneity (for a review, *cf.* Heidenreich and Zeitlin 2009) as well as sovereignty.

From an analytical standpoint, it must be acknowledged that the non-binding, *soft* nature of this kind of coordination processes, within the realm of European social policy governance, makes EU's impact more difficult to capture and isolate, because it tends to unfold *gradually* and rarely impacts on policy decisions, rather affecting 'less tangible' elements such as ideas, values and procedures. Furthermore, as argued by Barcevičius *et al.* (2014, p. 35), when processes of soft coordination are considered, 'influences on policy-making must be "domesticated" – that is must pass through national policy processes and be adapted to national contexts – before feeding into Member State policy decisions'. This branch of literature therefore comes with two main and opposite risks: on the one hand, the risk of downplaying EU-related factors in explaining domestic change; on the other, causal over-determination.

As argued by Lehmkuhl (2007, p. 342), the disentanglement of the *net effect* of Europe from other factors and the re-entanglement of mutually supporting or inhibiting factors remain at the top of the Europeanization research agenda. Yet, to avoid making 'EU influence a cause in search of an effect' (Graziano and Vink 2007, p. 9), research strategies must be designed carefully – both analytically and theoretically – and are required to rely on several methods, such as in-depth process tracing and careful triangulation of empirical evidences.

Situating within this strand of research and drawing from the above mentioned considerations, the analytical framework used to investigate the (possible) effects triggered by Europe 2020 at the national level aimed at shortening the causal chain by exploring *procedural* (i.e. related to governance and policy-making processes), and *substantive* changes at the national level (i.e. policy reforms), rather than outcomes (i.e. poverty trends).[125] More precisely, the empirical investigation of national-supranational interactions in the field of anti-poverty policy was driven by five original expectations concerning the possible impact of the supranational anti-poverty strategy. Drawing from the literature on Social-OMC and on the key institutional novelties of the EU2020 strategy we expected that, compared to the OMC-Lisbon phase, the Europe 2020 strategy could more likely produce substantive effects due to the existence of EU's hard poverty target – also combined with growing 'problem pressure'. This may have increased the salience of poverty (*substantive effect no. 1*), as well as prompted – under favourable conditions – *agenda shifts* and revision of *national legislation* (*substantive effect no. 2*). As for *procedural effects*, we expected an impact on both the integration and participation dimensions, but in opposite directions: increased cross-sector and cross-department coordination, that is *more integration* across policy sectors triggered by the Semester governance architecture (*procedural effect no. 3*) versus a step back in (*multi-*)*stakeholder* involvement (*procedural effect no. 4*), due to

125 From a methodological standpoint, the study relied on qualitative research methods, primarily 'process tracing' (Collier 2011), based on the analysis of several primary and secondary sources, complemented by a large number of semi-structured interviews with key informants – i.e. institutional, political and social actors at different government levels. Interviews were conducted between October 2012 and December 2015. For details, see Jessoula and Madama (2018).

the switch from the OMC to Europe 2020 governance framework. Last, we expected that effects might unfold slowly over time, from the first to the fifth cycle (*procedural effect no. 5*), as a consequence of both the institutionalization of the iterative governance processes and on-going supranational actions aimed at reinforcing governance mechanisms and EU's steering power.

Field research has shown that significant *variation* has characterized the implementation of the Europe 2020 anti-poverty component at the national level in Italy and Germany. The main findings are summarized below, starting from substantive effects[126].

Substantive effects: two diverse implementation patterns

With regard to effects in the political sphere entailed by Europe 2020 implementation, Germany and Italy have followed two rather different implementation patterns. In Germany the launch of Europe 2020 prompted a lively reaction by the national government aimed at tackling supranational 'intrusion' in domestic social policy-making. Such resistance, as well as opposition, by national governments was particularly strong in the initial phase of the new overarching strategy: the inclusion of the poverty target among the five main Europe 2020 quantitative objectives was actually perceived to have the potential of greatly increasing the visibility of the issue at the supranational level, thus legitimizing further interference by European institutions in domestic anti-poverty agendas.

In the Bundestag, the Conservative-liberal coalition (CDU-CSU, FDP) overtly supported the first three Europe 2020 headline targets – concerning employment, R&D/innovation and climate change/energy – but clearly rejected the social dimension of the overarching supranational strategy – addressing education and poverty/social exclusion – and especially the anti-poverty target. Chancellor Angela Merkel herself explicitly affirmed, in March 2010, 'I will not give any support for a quantitative target' to be included in the European strategy against poverty (*cf.* Zimmermann and Petzold 2018). The government somehow exploited the critical juncture represented by the genetic moment of Europe 2020, and especially the launch of the strategy implementation at the national level, to strongly filter supranational 'soft' but strengthened pressures aimed to support the achievement of the Europe 2020 'hard' poverty target. As further evidence of such resistance against the perceived EU 'intrusion' in a field of national sovereignty, not surprisingly Germany did not define the national anti-poverty targets in accordance with AROPE indicators agreed at the EU level and opted for quantified targets that better matched national priorities and strategies, setting the reduction of long-term unemployment as the national objective in the Europe 2020 framework. Therefore, claims about the defense of national 'social' sovereignty went in parallel with the domestic reframing and reinterpretation of the EU anti-poverty target in accordance with the national approach as well as government' orientations to combat poverty and social exclusion.

The reactions were radically different in Italy, where the launch of Europe 2020, with its poverty target, was much less politically contentious. The country had broadly supported the introduction of a common quantified EU anti-poverty target (Copeland and Daly 2012), and the politicization of the matter during the critical juncture was low. When drafting the first NRP in 2011, the issue was mostly dealt with at the administrative level, with limited (or no) direct engagement of the main politico-institutional actors. Italy also complied with European prescriptions by setting the anti-poverty goals in congruence with agreed indicators: lifting 2.2 million people out of poverty or social exclusion by 2020.

Interestingly, Italy is one of the countries where the Europe 2020 strategy has produced the most relevant substantive effects in the subsequent

126 The comparative evidence presented here elaborates on the findings of the researches conducted by Zimmermann and Petzold (2018) and Madama, Natili and Agostini (2018).

cycles. From the first to the fifth cycle, anti-poverty policies gained momentum and substantive effects could be detected in the ideational sphere, partly percolating into national legislation. This happened, first, through the initiatives aimed to re-direct the usage of ESF funds in order to tackle the poverty challenge in accordance with the national anti-poverty target; second, through the reform and the gradual expansion of the newly launched anti-poverty national measure (the *Social Card* pilot project, soon re-named *Support for Active Inclusion*, SIA).

Procedural effects: a mixed picture after a weak start

When considering procedural effects, the implementation of the Europe 2020 strategy at the national level appears heterogeneous, and initial expectations about both (increased) cross-sectoral integration and (reduced) multi-level and multi-stakeholder involvement were only partly confirmed.

With regard to the strategy potential to trigger more *integration*, and possibly coordination, across different policy fields and departmental (mainly, ministerial) structures, findings are mixed. In Germany NRP drafting was a centralized process in the hands of finance ministries, with only poor inter-ministerial coordination/integration between economic (and even employment) policies and social/anti-poverty measures. In Italy, an attempt to strengthen cross-sector policy integration was made in ESF planning for the 2014–2020 budget cycle, a process which registered higher coordination and cooperation across ministries and government levels than in drafting NRPs.

With regard to the second dimension of procedural effects, both *horizontal* (multi-stakeholder) and *vertical* (multi-level) *participation* once more revealed substantial variation. Our initial expectation about the possible reduction of stakeholder involvement – in light of the relatively weak Europe 2020 governance structure compared to the Social OMC – was confirmed in both Italy and Germany. The shift from the Lisbon-OMC period to Europe 2020 actually resulted in very limited, and in fact diminished, stakeholder involvement – especially NGOs and anti-poverty groups. The drafting of the first NRPs in 2011 constituted a centralized exercise, which involved ministries and peak bureaucracy only in both countries. However, from the second cycle in 2012, things have slightly changed in Germany. This gradual change is in line with our fifth expectation about the effects unfolding slowly over time due to iterated multi-level and multi-stakeholder interactions. According to an institutionalized national procedure known as 'Social Monitoring' (*Sozialmonitoring*), the Federal Ministry of Labor and Social Affairs invited several actors to hearings aimed at discussing the preparation of national reports. The audience was quite broad – including NGOs, social partners, the national network of EAPN and municipalities – and some organizations were also asked to comment on draft NRPs (cf. Zimmermann and Petzold 2018)[127].

In Italy, stakeholder involvement and actor participation in drafting NRPs has remained limited, thus shaping a visible step back compared to the Social OMC. The Italian case however is more complex, and actually two-faced. On the one hand, openness to societal interests was low in drafting NRPs, especially in the area of poverty and social exclusion; on the other, this was in sharp contrast with the highly participatory approach adopted, still within the Europe 2020 framework, but in relation to the planning of structural funds for the 2014–2020 cycle (*cf.* Madama *et al.* 2018).

III. Two worlds of domestic effects: investigating the factors behind

The empirical evidence presented in the previous section shows that Italy and Germany represent

127 Although the European Semester cycles did actually provide opportunities to societal interests operating in the area of poverty and social exclusion of being heard by policy makers, in some cases stakeholders complained that their chances to influence governments' decisions remained weak.

two rather distinct worlds of implementation of the Europe 2020 anti-poverty strategy. In Germany the elaboration as well as the initial implementation of the supranational anti-poverty strategy substantially increased the political salience of the poverty issue. This did not pave the way, however, for a smooth implementation of the strategy, or the setting of the national poverty target in accordance with EU's guidelines. Nor did increased political salience favour, especially in the initial phase, more actor participation and coordination across the different policy sectors and government levels. Rather, research findings revealed the *emergence of a main line of tension* between the MS and the EU, related to *national sovereignty/autonomy* vs. *European coordination mechanisms* in the field of social and especially anti-poverty policies. The setting of the quantified poverty target within the Europe 2020 institutional framework actually provoked a government reaction in defense of national social sovereignty. The new Europe 2020 strategy was actually perceived as a potential 'Trojan horse' for competence creep in the social field and the government explicitly opposed it.

By contrast, in Italy governments showed a more positive attitude *vis à vis* the new European strategy in the field of anti-poverty policies, and the national-supranational 'competence clash' did not materialize. The strategy implementation was therefore non-contentious, and its effects turned out more far reaching especially along the substantive dimension.

How can we solve the puzzle implied by such diverse effects, and consequent very different implementation, of the Europe 2020 anti-poverty strategy in the two countries? By integrating the main findings of the consolidated strand of literature that has shed light on the major role of domestic factors in 'filtering' supranational pressures (*cf.* Graziano *et al.* 2011; De la Porte and Heins 2016; Heidenreich and Zeitlin 2009), with more recent studies on the social dimension of Europe 2020 (*cf.* Jessoula 2015), and insights from comparative welfare state research, we contend that (i) domestic policy/institutional arrangements; (ii) national attitudes towards Europe; and (iii) domestic politics dynamics are key to explain the implementation of Europe 2020 at the national level (cf. Jessoula and Madama 2018).

On that respect, the two countries presented very different configurations. Germany was characterized by robust national institutional legacy in fighting poverty and social exclusion and can thus be conceived as a typical case of 'institutional pre-emption' with governments actually reacting harshly against the perceived EU 'intrusion' in a sector of national sovereignty. The national government in fact acted as '*institutional gatekeeper*' within the Europe 2020 framework by 'domesticating' the anti-poverty target (Jessoula 2016), limiting both stakeholder involvement and multi-level coordination, centralizing NRP drafting in the hand of economic ministers. Furthermore, the fact that EU funds are not particularly relevant in the country, as well as the prevalence of centre-right governments in the considered period, further contributed to national government behaviour, and the strategy implementation was overall weak: effects emerged almost solely in the political sphere, with argumentative/ideational clashes along the vertical axis (national/supranational) and the horizontal one (opposition parties vs. governing coalitions).

Quite the opposite, in Italy the launch of the novel supranational anti-poverty strategy and especially the quantitative target did not prompt a political conflict along the vertical dimension, that is along the national sovereignty vs. EU integration (possible) line of tension, in the Europe 2020 genetic moment. Here, domestic political actors and national governments did not act as gatekeepers *vis à vis* the new European strategy, and the latter actually provided an institutional framework that was exploited by domestic (institutional, political and social) actors in order to reinforce national anti-poverty measures. Why did the national governments in Italy not worry about the reinforced supranational framework and potential EU intrusiveness in a typical national competence domain such as anti-poverty policies? The three explanatory factors seem to have played a key role in this respect. On the one hand, the absence of a robust national anti-poverty legacy explains the lack of institutional pre-emption. On the other, empirical investigation revealed that such development must be understood in light of the high relevance of EU structural funds for active inclusion policies in the country: in a perspective of reciprocal acknowledgement of their respective institutional roles, the opportunity to access EU funds for social inclusion strategies actually pushed national governments to behave as 'good pupils', leading to a sort of 'Europe is where money is' effect. Notably, this dynamic fully appeared only when a pro-EU government came into power in 2011[128].

IV. Conclusive remarks

The analysis presented in the previous pages prompts some final reflections on the potential relevance of the EU in the fight against poverty within the novel overarching Europe 2020 institutional framework. First and foremost, it must be said that, when looking at *outcomes*, figures are disappointing. In 2015, that is halfway through the Europe 2020 decade, the results produced by the new strategy were not satisfactory. Although the overall scenario was severely affected by the Great Recession and the Euro-crisis, the EU target of lifting 20 million individual out of poverty and social exclusion was out of reach: indeed, people in poverty or social exclusion have increased between 2008 (the reference year to assess progress towards the poverty target) and 2015: 1.8 million more individuals were at risk of poverty and social exclusion in 2015, and 8.1 per cent of the EU28 population (40.4 million) experienced severe material deprivation. More recent figures show a slight improvement, but still 118 million people are at risk of poverty or social exclusion, with an increase of about 800,000 individuals compared to 2008. The trend was therefore opposite to what was expected and desired.

When looking at the domestic effects triggered by the EU strategy in terms of policy *outputs* and *procedural dynamics* – which have been at the core of our analysis – the picture is, however, less clear-cut.

Policy coordination based on soft-law mechanisms may well be ineffective. Acknowledging the EU's 'social competence gap' also implies recognizing that overcoming sovereignty and political constraints posed by reluctant MS (i.e. the German case) is de facto impossible. Our analysis however suggests that Europe 2020 anti-poverty strategy, under favourable conditions, had the chance to produce more significant effects in the country presenting a weaker 'safety net' (i.e. the Italian case), where in combination with EU fund allocation, Europe 2020 actually provided resources and an innovative institutional framework that contributed to strengthen its national anti-poverty model. In particular, such institutional framework – resting on soft- law mechanisms, but backed by a 'hard' target – has allowed the EU and especially the Commission to act as an anti-poverty, social policy advocate through iterated interactions in the Semester. Parallel to this, supranational target and agency provided an opportunity for – as well as strengthened – national actors that exploited the Europe 2020 institutional framework to 'voice' in favour of more effective measures to achieve national(/EU) poverty targets. Without indulging in excessive optimism, adopting a 'systemic' perspective one could say that were the EU's social strategies more effective in pushing policymakers to reinforce welfare arrangements and anti-poverty policies (at least) where the latter were less robust, that would be already an important result for the Union as a whole.

128 We do refer to the technocratic government led by Monti, in office from November 2011 till April 2013.

References

Armstrong, K.A. (2006) "The 'Europeanisation' of Social Exclusion: British Adaptation to EU Co-ordination", *British Journal of Politics and International Relations*, 8: 79-100.

Armstrong, K.A. (2010) *Governing Social Inclusion. Europeanization through Policy Co- ordination*, Oxford: Oxford University Press.

Armstrong, K.A. (2012) "EU social policy and the governance architecture of Europe 2020", *Transfer: European Review of Labour and Research*,18(3): 285-300.

Barbier, J.C. (2005) `*The European Employment Strategy: a Channel for Activating Social Protection*?', in J. Zeitlin and P. Pochet (eds.) *The Open Method of Coordination in Action: the European Employment and Social Inclusion Strategies*, Brussels: PIE-Peter Lang, pp. 417-46.

Barcevičius, E., Weishaupt, J.T. and Zeitlin, J. (eds.) (2014) *Assessing the Open Method of Coordination: Institutional Design and National Influence of EU Social Policy Coordination*, Basingstoke: Palgrave.

Bouget, D., Frazer, H., Marlier, Sabato, S. and Vanhercke, B. (2015) *Social Investment in Europe , A study of national policies 2015*, European Social Policy Network (ESPN) - Synthesis Reports, European Commission, Brussels.

Copeland, P. and Daly, M. (2012) 'Varieties of poverty reduction: Inserting the poverty and social exclusion target into Europe 2020', *Journal of European Social Policy*, 22(3): 273–287.

Copeland, P. and Daly, M. (2014) 'Poverty and social policy in Europe 2020: Ungovernable and ungoverned', *Policy and Politics*, 42(3): 351–366.

De la Porte, C. and Heins, E. (eds) (2016) *The sovereign debt crisis, the EU and welfare state reform*, London: Palgrave.

Frazer, H. and Marlier, E. (2016) *Minimum Income Schemes in Europe - A study of national policies*, European Social Policy Network (ESPN) - Synthesis Reports, European Commission, Brussels.

Graziano, P. and Vink, M.P. (eds.) (2007) *Europeanization: new research agendas*, Basingstoke and New York: Palgrave MacMillan.

Graziano, P., Jacquot, S. and Palier, B. (eds.) (2011) *The EU and the Domestic Politics of Welfare State Reforms. Europa, Europae*, Basingstoke: Palgrave MacMillan.

Heidenreich, M. and Zeitlin, J. (eds.) (2009) *Changing European Employment and Welfare Regimes: the Influence of the Open Method of Coordination on National Reforms*, London: Routledge.

Jessoula, M. and Madama, I. (eds.) (2018) *Fighting poverty and social exclusion in the EU. A chance in Europe 2020.* London/New York: Routledge.

Jessoula, M. (2015) 'Europe 2020 and the fight against poverty: beyond competence clash, towards hybrid" governance solutions?', *Social Policy and Administration*, Europeanization of welfare regional Issue, 49(4): 490-511.

Jessoula, M. (2016) Killing, domesticating or feeding the snake. The implementation of the Europe 2020 anti-poverty component at the national level, in R. Halvorsen and B. Hvinden (eds), *Combating poverty in Europe: Active inclusion in a multi-level and multi-actor context*, Cheltenham: Edward Elgar, pp. 133–156.

Lehmkuhl, D. (2007) *Some Promises and Pitfalls of Eureopeanization Research*", in P. Graziano and M. P. Vink (ed.), *Europeanization: New Research Agenda*, New York: Palgrave Macmillan, pp. 337-353.

Madama, I., Natili, M. and Agostini, C. (2018) Lucky timing and propitious conditions: Italy's anti-poverty policy under Europe 2020, in M. Jessoula and I. Madama, I. (eds.) *Fighting poverty and social exclusion in the EU. A chance in Europe 2020.* London/New York: Routledge, pp.

Marlier, E. and Natali, D. with R. Van Dam (eds.) (2010) *Europe 2020: Towards a More Social EU?*, Brussels: P.I.E. Peter Lang.

Peña-Casas, R.(2012) *Europe 2020 and Fight* *against Poverty and Social Exclusion: Fooled into Marriage?*, in D. Natali and B. Vanhercke (eds.), *Social Development in the European Union 2011*, Brussels: OSE, ETUI, pp. 159-185.

Pochet, P. (2010) "What's wrong with EU2020?", *European Social Policy*, ETUI Policy Brief Issues, 2: 1-7.

Zimmermann, K. and Petzold, N. (2018) The German way: reaffirming sovereignty, while accommodating the EU anti-poverty strategy in M. Jessoula and I. Madama, I. (eds.) *Fighting poverty and social exclusion in the EU. A chance in Europe 2020.* London/New York: Routledge, pp.

EUROPEAN INTEGRATION AND POLITICAL OWNERSHIP: FICTION AND REALITY BEHIND STRUCTURAL REFORMS AND RISK-SHARING

Filippo Taddei[129]

Johns Hopkins School of Advanced International Studies (SAIS)

"In politics, nothing happens by accident. If it happens, you can bet it was planned that way."

Franklin D. Roosevelt

Introduction

It has been some years since Europe lost its central role in world affairs. While the economic rise of Asia is mostly responsible for this outcome, today Europeans are facing a new challenge: the combination of unfavourable demography, volatile migration flows and technological disruption, which questions the traditional economic identity of the European economy and the sustainability of the social standards that we take for granted. Enhanced European integration is often presented as an effective tool to respond to these challenges. This article discusses what is missing in our policy perspective in order to develop integration seriously and make sure it helps to address the combined challenges of globalisation and technological change.

European integration advances only if it secures stability and comparable economic development across Member States and regions. Both stability and economic growth are fed by structural reforms and risk-sharing. This is easier said than done: the discussion that follows wants to advance two very simple, fundamental and related points. The first is that advocating structural reforms at the national level without improving the European institutions that facilitate risk-sharing across the Member States is completely unrealistic. At the same time, demanding risk sharing in the absence of structural reforms is simply unsustainable.

Therefore, if we want to accelerate the path of structural reforms at the national level, we have to increase the pace of risk-sharing at the European level in at least one of the crucial areas. If, *vice versa*, we want to increase the degree of risk-sharing and make this sustainable, we have to strengthen the economic fibre of member countries by speeding up structural reforms. The bottom line is that risk-sharing and structural reforms must advance hand-in-hand in order to happen. In the absence of their co-ordinated advancement, neither can persist and European integration cannot advance. In order to make sure integration does happen, we have to correct the general perspective on what structural reforms and risk-sharing really entail. Let us analyse each of these issues in turn.

Structural Reforms Taken Seriously: The Importance of Political Ownership

If European integration requires structural reforms, structural reforms are the result of political decisions at the national level and their often complex dynamics. Although structural reforms are one of the pre-requisites of European integration, the reasons behind them are deeper and broader: the European socio-economic model is under threat and urgently needs to be reformed to retain a satisfactory level of social protection. As member countries struggle to change their economies and welfare states, changes are progressing slowly. By today, Europeans have been talking about reforms for so many years that the European political discourse has developed its own rhetoric about the importance and centrality of *structural reforms*.[130]

129 I am grateful to Mark Gilbert, Erik Jones and Alberto Martin for comments and discussions on an earlier draft. Contact info:SAIS Europe, Johns Hopkins University, Via Andreatta 3, 40125 Bologna, Italy. Email: ftaddei@jhu.edu.

130 For a discussion of the current prospects, it is useful to refer to Erik Jones and Anand Menon, "Europe: the Once and Future Union", 2018 Annual Meetings American Political Science Association.

As is often the case, this rhetoric is not helping. It is creating a perception of a continent split between a group of member countries that appears more eager to change and take responsibility, and another group that is doing anything it can to postpone the reforms and relies on others to bail them out. Although it is true that political will varies across countries, this perception is actually confusing our discussion rather than helping us focus to on the nature, the benefits, and the costs of reforming a country. Let us abstract from this misleading rhetoric to take two steps back and make an effort to ask two apparently simple questions. First, what is necessary for a reform to be structural? Second, why are structural reforms so difficult and slow?

We should refer to a structural reform as any change in institutions or legislation that is thorough enough to deal with a fundamental factor in the economy or society, a factor that we could identify as an existing legacy. Negative legacies are the result of consolidated forms of behaviour that accumulated their effects through the years and turned out to be detrimental to either equality or growth or both. Rents inherited by groups or individuals, rules and incentives detrimental to equality of opportunities, large public debt, retirement requirements responsible for generational inequality, welfare benefits addressed to politically active minorities rather than to those in need and inconsistencies in the tax system would all fall into the broader category of negative legacies. Although a reform needs to address a negative legacy in order to be structural, I want to argue that this is *not* a sufficient condition to define it as such. In the general political discourse, this is very often a point of confusion. Any change – reform -of a negative legacy is considered a structural reform. This is conceptually misconceived and it is an important mistake. In fact, this perspective is delaying the reform of European governance, and it is generating ineffective policies to support national reforms.

It is important to spend some time on this issue – what is sufficient to define a reform as being *structural* - because it is instrumental to provide a proper answer to the second question – why are structural reforms so difficult. In order to illustrate the point, it may be useful to draw from some of the latest experience of reform-making in Europe during and after the Great Recession. Italy can provide a very insightful dichotomy with two reforms that were deemed *structural*: the pension reform in December 2011, and the *Jobs Act* in 2015. As I will argue, only one, though- the *Jobs Act* - possesses the degree of political ownership that makes it truly structural.

The Italian Pension Reform

In December 2011, only three weeks after Senator Mario Monti had been sworn in as Italian Prime Minister following Silvio Berlusconi's resignation, his new government presented to the Italian Parliament a radical pension reform - the *Fornero Reform*, named after the Minister of Labour, Social Policies and Gender Equality, Elsa Fornero. The reform increased, with immediate effect, the statutory retirement age to 66 years of age and linked it, from that moment onwards, to the evolution of life expectancy. If Italians, as is the case today, continue to be one of the most longevous people in the planet, their retirement age will continue to rise together with life expectancy.

The changes in 2011 put the Italian pension system among the most sustainable across developed economies and certainly as one of the most forward looking in Europe. The Italian Parliament, on the brink of political collapse and under pressure by the threat of rising government debt spread, weak growth and unsustainable public finances, approved the Government proposal with virtually no changes and with one of the largest majorities in the history of the Italian republic. By any metric, this reform addressed a negative legacy in the Italian economy and, thus, it fulfilled the necessary condition to be defined as structural: retirement rules have always overprotected the interests of the incumbent old generations at the expense of the young generations. Since

2011, this overprotection is definitely more difficult, although the Italian government has recently announced a partial reversal of the reform, which highlights, as we will discuss below, that a reform cannot be easily categorised as structural if it lacks political ownership.[131]

The Italian Jobs Act

Few years later, in December 2014, following the initiative of Prime Minister Matteo Renzi, leader of the Democratic Party, and his government, the Italian Parliament approved the framework legislation determined to reform labour market institutions comprehensively – the *Jobs Act*. The vote in Parliament came after a very heated debate, one that divided the Democratic Party and which could only be recomposed through party loyalty. While the Pension reform was approved by a super majority, the *Jobs Act* was passed in the Senate with a very small margin. Shortly before and after this approval, the Prime Minister had organised and supervised, together with the Minister of Labour and Social Policies, Giuliano Poletti, a small group of policy experts to achieve a quick implementation of the framework legislation.

In the nine months that followed, at a pace unparalleled in other structural reforms in Europe, the Italian labour market experienced the introduction a new paradigm: protection of workers would be delivered *in the market* rather than centred *in the job post*. Dismissal rules were changed and simplified to increase flexibility, unemployment insurance was extended in both coverage and duration, wage supplementation scheme were better protected from abuses and moral hazard, and active labour market policies were brought under national co-ordination for the first time. The reform was thorough and fast while the political process that led to it was cumbersome and divisive.

131 As this paper is being finalised, the Italian Budgetary Plan for 2019 is in preparation. Although the policy reversal has not been finalised yet, the Italian Government and the parties in the supporting coalition have made clear announcements regarding their intention to reverse this reform.

Political Ownership, the Emergency Threat and Structural Reforms

As problematical as the political process behind the *Jobs Act* was, it delivered political ownership of the labour market reform. A political party – in this case, the Italian Democratic Party, which was ruling at the time – claimed ownership of the reform and invested the political capital (*i.e.*, consensus) raised in the political market (*i.e.*, elections) in a change in legislation that could produce the desired effects and rebuild the political capital. This is a striking difference with the pension reform. In fact, the pension reform was introduced after almost no discussion and voted within three weeks by an overwhelming majority ranging from left to right parties. Apparently uncontroversial and solid, it did not seek any popular support but was pushed through by the urgency created by the growing financial tensions surrounding Italian public debt. As a result of this process, the pension reform had no political capital invested in it and, therefore, could not have any political ownership. Since no political group *owns* it, no political subject is responsible for its survival and everyone may feel tempted to modify it or even cancel it, as the currently ruling coalition is already proposing to do in the budgetary plan for 2019. As current events show, when no political actor is ready or willing to defend a reform, its persistence over time becomes uncertain.

It therefore seems quite misleading to define these kinds of reform, even if they address an important negative legacy, as "structural". They lack the necessary political ownership to survive over time. The Italian Pension Reform, soon to become a political orphan, was implemented and is still producing its effects. It is nonetheless continuously under threat of cancellation and contributes to produce a sense of disenfranchisement in the citizens of its country. This is a common outcome: lack of political ownership quickly translates into lack of national ownership. This generates a disenfranchisement that fails to overturn the practices and forms of behaviour of citizens which lie at the root of the legacy that the reform was set to correct.

Comparing two Italian reforms – the Pension Reform and the *Jobs* Act – highlights a general point and a crucial distinction: a reform cannot be considered "structural" unless a sufficiently large share of the citizens feel to have a stake and a say in the process that determined it. Otherwise, the reform lacks the national ownership that only a fully-fledged democratic process may provide and remains inherently fragile. Incidentally, this also helps to answer our second question: why structural reforms are so difficult and slow. The reason is that building up sufficient political capital to avoid citizen disenfranchisement is a costly and often lengthy process. There are no short cuts, though. Relying on the push of emergencies to facilitate structural reforms is only an *apparent* short cut: it is a misconception that comes from confusion in the definition of structural reforms. Reforms motivated by some perceived national emergency are always at risk of being withdrawn once the perception of the emergency fades away. If we want to incentivise the development of properly defined structural reforms, capable of changing – both in depth and permanently - the fundamentals of society, we must understand that such reforms require the political ownership that only a thorough and often controversial political process may offer. As this process is already difficult *per se*, it is worthwhile thinking about how European institutions can help this. We turn to this issue now.

Risk-Sharing and Uneven Recovery: The European Level

The Great Recession has been followed by an uneven economic recovery within the European Union. This inequality is slowing down structural reforms. It is also hindering the development of a common and consistent perspective regarding the role of European institutions. When we ponder the likelihood of national reforms, we often confuse legacy – how severe problems are - and will – how quickly political capital can be invested to address them. The question that we should be asking is therefore how we can facilitate the emergence of the political will necessary to produce structural reforms in countries that are hampered by negative legacies.

In the face of the severe economic shock that hit the continent, the weaknesses of individual member countries have emerged, in some cases dramatically. We have observed the emergence of important regional asymmetries both as a consequence of the common shock and in the policy responses that have emerged. It should be clarified that this heterogeneity is mostly due to the different legacies present in the different European countries. These legacies are the reasons for reforms, structural reforms, but we have to evaluate whether mechanisms such as fiscal convergence or the capital market union that insure and protect member countries from the asymmetric and country-specific effects of common shock can accelerate the domestic reform process.

Politics, like economics, forces decision-makers to address many objectives with limited resources. In policy-making, structural reforms remain a matter of prioritising medium- and long-term results over short-term responses. Some European policy-makers seem to believe that the pressure of national emergencies could fast-forward structural reforms in member countries. As previously argued, this point of view is due to a conceptual mistake: such reforms, even when they happen, remain inherently fragile. Only reforms investing political capital and gathering consensus in their scope can persist in time and affect ordinary economic and social behaviour. Only these reforms can have the ambition to become structural. This paper has argued that enhancing risk-sharing to offer protection to the member countries from the severe effects of common shocks allows European countries to focus resources and efforts in raising the political capital necessary to advance structural reforms.

European Integration Taken Seriously: Combining Risk-Sharing and Structural Reforms

Not a single month goes by without an informal or formal invitation by some branch of the European institutions to increase the "pace of structural reforms" in the different Member States. Almost not a single day goes by without a national government responding to this invitation with more or less eagerness.

Notwithstanding this, Europe is not changing at the pace we had hope for, democratic institutions are perceived as being less effective at addressing citizens' demands, and concomitantly citizens feel increasingly disenfranchised from the political process and discourse. We have been here before in our common history: these are the fundamental factors and policy mistakes behind the rise of populist movements and parties, a rise that is taking place – unsurprisingly – in almost every major European country as European integration seem troubled and regional disparities consolidate.

This state of European affairs is not random but rather the consequence of a conceptually flawed definition of what a structural reform really means. It is not enough for structural reforms to address a fundamental weakness, they must also be characterised by political ownership. It is very difficult for member countries to raise political capital if they are dealing with the tail-effects of the most severe economic recession since World War II. This is the reason why risk sharing at the European level and structural reforms at the national level can only progress together: by supporting each other, only their combination can advance European integration.

D THE LEGACY OF THE WELFARE STATE IN EUROPE

AN ALTERNATIVE TO THE CONSTITUTION OF THE EU'S SINGLE MARKET?

Florian Rödl

FU, Berlin

1. The "European Pact for Social Progress"

For decades the question of whether, and, if so, how, the European Union can become not only an economic and subsequently a currency union, perhaps also a community of shared values, but also a social union, has been the subject of political and scientific debate. For a long time, a predominantly optimistic scenario dominated. This was based upon the conviction that the steps towards integration in the internal market and then the common currency would simply compel further and substantial integration steps in social areas (including labour law and collective-bargaining agreements). In this phase, it was appropriate for unions and Social Democratic parties in particular to welcome every move towards integration, because, with each deepening, the overall dynamics would also be propelled forward. Ultimately, this would lead to the "United States of Europe", to a "European Republic", in other words, to a state entity that would be politically and democratically integrated and able to act effectively in the social domain. Finally, the social control capacity lost in the meantime at the national level would be successfully recovered at a higher level.

After the Constitutional Treaty failed, the labels of the "United States of Europe" or a "European Republic" initially ceased to be used in the political sphere and in the meantime have also fallen out of use in scientific discourse. Furthermore, the view that the emergence of a democratic and social union is not a necessity for the integration dynamic, but which is confronted by serious obstacles, has gained ground. It has become increasingly clear to open-minded observers that these hurdles are not based solely or primarily upon the provincial narrow-mindedness of the political representatives of the Member States. Rather, they are rooted in the complex heterogeneity of the 28 Member States, which, for their part, do not operate in a vacuum but within the framework of a globalised world economy.

Upon this basis, many political and scientific observers have realised that – whatever form the Union may take in the more distant future – at present, a policy of strengthening social issues in the Union must always focus on the necessity that, at the very least, the law of the Union does not limit welfare state options at the national level too severely.[132] There is every reason for this focus. After all, the pursuit of the common good in the Member States, particularly the labour and social law of the Member States, and finally parties to collective-bargaining agreements, have to comply with the strict requirements of the constitution of the internal market, in other words, market freedom and competition law. In addition, there are the functional imperatives of the euro, which impose strict compliance burdens on the deficit countries, which they must fulfil not least by re-structuring their collective-bargaining systems at the expense of the trade unions and by reducing social security.

Only rather naïve observers oppose this.[133] However, they do not support their arguments by referring to current developments or structures, but rely on the texts of the EU treaties: The Union is said to be a social market economy (Article 3 (3) (2) TEU); the social cross-sectional provision is argued to enshrine a kind of welfare state principle (Article 9 TFEU); the EU Charter of Fundamental

132 Sacha Garben, in: European Constitutional Law Review 13 (2017), 23 ff.; Christian Joerges, Social Justice in an ever more diverse Union, in: Vandenbrouke, Barnard, De Baere (eds.), *A European Social Union after the Crisis*, 2017, 92 ff.; groundbreaking: Fritz Scharpf, Regieren in Europa: Effektiv und demokratisch, 1999.

133 Among them are, specifically, the judges of the Second Senate of the Federal Constitutional Court, who made the decision on the Treaty of Lisbon: BVerfG, ruling dated June 30, 2009, 2 BvE 2/08 at al., in: BVerfGE 123, 267, 427 ff. – *Treaty of Lisbon*.

Rights is claimed to contain fundamental social rights (Articles 27-38 EU-GRC), and recently a new "European Pillar of Social Rights"[134] has been proclaimed; there is a chapter on employment (Articles 145-150 TFEU); there is a social chapter (Article 151 TFEU) and related EU legislation; equal pay is guaranteed (Article 157 TFEU), and so on. These rather naïve observers seek to counter the limitations of social achievements under EU law with the usual demands for "more integration", *i.e.*, the transfer of further powers to the Union, and "more democracy", meaning the strengthening of the European Parliament.[135] But this does not work in the social field. This has been explained many times[136] and will thus only be briefly repeated here:

The economic, regulatory and political heterogeneity in the Union is too great for a social policy to be formulated at Union level, let alone, enforced, which could even approach the levels in the developed welfare states within the Union. Consequently, it would be of no help if the Union acquired very comprehensive powers in the field of social affairs as well. The Union would not be able to use them. In addition, developments that are problematical for social issues are often the product of "integration through law",[137] and this means integration not through political legislation but through judicial application of the law by the European Court of Justice. But the European Parliament has had no political access to the juridical mode of integration from the outset, at least when – as is often the case – the application of primary law is concerned.

Given the impracticality of these typical pro-European responses, unions and social-democratic parties from Austria, Sweden and Germany want to adopt a different course. At a summit meeting in late November 2016, they decided on the "European Pact for Social Progress".[138] This pact builds on the demand of the European Trade Union Confederation (ETUC) for the adoption of a "Protocol on Social Progress".[139] The ETUC had initiated this demand in 2008 in response to ECJ rulings on EU-law restrictions on collective-bargaining autonomy, in order to correct these decisions by amending primary legislation. The demands of the social progress protocol have now been taken up by trade unions and social democrats in the three-country initiative, and specified and further developed in the "European Pact for Social Progress" just mentioned.

In Section 2, the European Pact emphasises the following demands based upon primary legislation:

1) The obligations of the Union regarding social market economy and social progress must be formulated so that these concepts clearly include strong workers' rights, and should exclude competition at the expense of wages and working conditions.

2) The economic freedoms of the internal market should not be understood as a ban on unjustified restrictions but instead they should only ensure rights to equal treatment.

134 Available at https://ec.europa.eu/commission/publications/european-pillar-social-rights-booklet_en.

135 HaukeBrunkhorst is representative of this in his article "Auswegeaus der technokratischenFalle," in: Leviathan 42 (2014), 508 ff.

136 For example: Wolfgang Streeck, GekaufteZeit: Die vertagteKrise des demokratischenKapitalismus, 2013, 141 ff.; Claus Offe, The European Model of "Social Capitalism": Can it Survive European Integration, in: Journal of Political Philosophy 11 (2003), 437 ff.; Alexander Somek, Concordantia Catholica. Exploring the Context of European Anti-Discrimination Law and Policy, in: Transnational Law and Contemporary Problems 15 (2005), 959 ff.; Florian Rödl, Arbeitsverfassung (labor constitution), in: Bogdandy/Bast (eds.), Europäisches-Verfassungsrecht, 2009, 855 ff., see especially 877 ff.

137 The title of the anthology Mauro Cappelletti/Monica Seccombe/Joseph Weiler (eds.), Integration Through Law, makes the point. Vol 1, 1986; see Ulrich Haltern, Integration by Law, in: Bieling/Lerch (eds.), Theories of European integration, 2006, 399ff.

138 Alliance for a Social Europe formed from the SPD, SPÖ, SAP, DGB, ÖGB, and LO, A European Pact for Social Progress, Vienna 2016, available at: http://www.dgb.de/themen/++co++14093cce-b620-11e6-a970-525400e5a74a.

139 The fully worked out proposal is available here: https://www.etuc.org/sites/default/files/social_progress_protocolEN_1.pdf.

3) In cases of conflict, fundamental social rights must take precedence over economic freedoms of the market and competition rules.[140]

These demands constitute a political programme to strengthen social rights and protect social achievements. However, they require further legal elaboration. This can be specifically gauged by whether or not they really do provide remedies for the problematical development of the legal integration dynamics identified here. Upon such a basis, the demands of the "European Pact for Social Progress" may eventually become a well-founded negotiating position.

The history of the previous dispute over anchoring the claim of a more social orientation of the Union has shown the need for such an examination. For example, with social democratic governments predominating in the European institutions, a chapter on employment was inserted into the Treaty of Amsterdam (1997). It had no effect. Especially in the negotiations on the Constitutional Treaty (2003), much effort was devoted to individual treaty provisions, such as the specification that the Union is a social market economy or the so-called social cross-sectional provision, or even the social rights in the EU Charter of Fundamental Rights. At no point has there been systematic examination of what legal force the relevant standards could actually develop. The results were ultimately sobering.

2. Implementation Prospects

The prospects of enforcing the programme are better than might be expected, given the political will on the part of unions and social-democratic parties, for a further deepening of economic and monetary union (as such) is on the agenda. With the presidency of Emmanuel Macron in France and a, certainly also in the future, pro-European government, new political scope has been created for this.

Like every previous amendment to primary law, the enforcement of a future treaty change will depend crucially on the approval of European trade unions. The history of the recent amendments made to the treaties, notably the failure of popular referendums, has demonstrated this impressively: if the trade unions (and social democratic parties that are not in power) do not stand up in the Member States for the necessary changes, ratification will be very difficult.

This constellation actually provides the unions with a strong negotiating position. All that is needed is for them to mobilise their power for a politically convincing and legally sustainable programme. The accusation of having switched over to the anti-European camp need not be feared. For a commitment to the programme of the European Pact for Social Progress would certainly not be an expression of a nationalist attitude. Against the backdrop of the legitimacy crisis of the Union, which is reflected not least in the political gains of right-wing populist parties, the programme of the European Pact is decidedly pro-European, because only upon this basis will it be possible to preserve what has been achieved and avoid squandering the opportunity for further integration.

3. Outline

The following outlines the results of a study concluded in 2018 which was conducted to elaborate the demands of the "European Social Progress Protocol" in legal terms:

1. In November of 2016, the EU Member States Sweden (LO and SAP), Austria (ÖGB and SPÖ) and Germany (DGB and SPD) signed a European Pact for Social Progress, which seeks to carry out a reform of the constitution of the internal market of the Union.

2. In concrete terms, the European Pact calls for the law of the internal market to be adjusted in such a way as to give its employees strong rights and priority over

140 A European Pact for Social Progress, 2016, p. 3.

market freedoms and competition rules. Furthermore, transnational competition upon the basis of labour costs should be excluded. Finally, it demands that the market freedoms that are constitutive for the internal market should be reduced to a legitimate level, and that they should no longer be regarded as banning restrictions, but only as requiring equal treatment.

3. Thus, the “European Protocol for Social Progress” is a response to a social and democratic problem of the integration process that has long been diagnosed in politics and political science. This has its origin in the liberalistic form of the legal constitution of the internal market. Consequently, it cannot be remedied by deepening integration or by strengthening the rights of the European Parliament.

4. The European Court of Justice has subjected the constitution of the internal market of the Union to liberalisation through its case law on market freedoms. It has conceived market freedoms as super freedoms for companies, which they may use, in addition to their guarantees, in the constitutions of Member States, of ownership and freedom of acquisition, to bring down Member State rules for promoting the common good and social equality. Such a shift of emphasis in favour of enterprises and at the expense of the common good and social balance was neither intended nor provided for by European market integration.

5. A conception of market freedoms as principles of equal treatment would be correct: No company based in another Member State and no cross-border entrepreneurial service should be treated less favourably than domestic companies and domestic services. Thus, on the one hand, market freedoms would prevent protectionism on the part of Member States, as required by a supranational internal market. On the other hand, they would lose their de-regulatory prevalence, a general shift in emphasis at the expense of the common good and social compensation.

6. The conception of market freedoms as super-civil liberties for companies is particularly difficult in the area of labour and social constitutions, which are primarily structured by Member State law. While, at the Member State level, the respective purview of economic constitutions, on the one hand, and labour and social constitutions, on the other, is determined by simple legislation and thus upon the basis of political-democratic decision-making, within the framework of the Union‘s internal market the economic constitution takes legal priority over the labour and social constitutions of the Member States. The national regulations that have been overturned cannot normally be compensated for by EU legislation, mostly because of the lack of jurisdiction of the Union, but also because of the wide institutional and economic diversity of the Member States.

7. Development is driven to the extreme by the fact that not only state law, but also – through a questionable binding of private interests to market freedoms – the processes of setting collective agreement standards within the framework of the autonomy of collective bargaining guaranteed by EU law are equally obliged to respect market freedoms.

8. The liberalist transformation of the Union’s single market constitution has given market freedoms considerable de-regulatory power, and thus today limits the social and democratic powers of the Member States to a considerable degree. This is also seen everywhere in European law. The legal proposals in this context to contain this de-regulatory force of market

freedoms (the keywords are "Keck exemption" and "market access criterion") have already proved ineffective. Therefore, a correction of the internal market constitution in primary law is needed.

9. The proposal by the former constitutional judge Dieter Grimm for a "de-constitutionalisation of the internal market" does not remedy the situation. Even if market freedoms were to fall within the scope of secondary legislation, the restrictions on regulatory freedoms of Member States would continue, because secondary legislation also takes precedence over Member State law. A subsequent more regulatory-friendly re-adjustment of market freedoms by means of ordinary EU legislators is not to be expected given the divergence of interests of the Member States.

10. One remedy would be to scale back market freedoms from fundamental entrepreneurial rights to equal treatment. In this case, Member State rules would have to justify market freedoms only if they resulted in discrimination. A mere restriction of transnational enterprise, irrespective of unequal treatment in comparison to domestic companies or services, would automatically be lawful.

11. Discrimination that continues to be prohibited can occur openly (direct discrimination) or covertly (indirect discrimination). Conceiving indirect discrimination as factual discrimination fits in with the anti-discrimination law for the protection of socially-disadvantaged groups, but not with the rule of equal treatment in a supra-state internal market. However, the reproach of covert discrimination is not dispelled by the defence by Member States that they had good intentions, but instead when the arrangement pursues a rational purpose (public interest or social compensation) and is appropriate and necessary for this purpose.

12. The conception of fundamental freedoms as principles of equal treatment is compatible with the basic structure of established internal market law. In particular, it does not undermine the principle of mutual recognition. On the contrary, it ensures that it only comes into effect if the interests of the receiving Member State are already completely fulfilled by the regulations of the Member State of origin. Nor does it undermine the so-called free movement of persons within the internal market (freedom of movement for workers, freedom of establishment), but it restricts the guarantee to a legitimate level which complies with the guarantee of domestic freedom of movement.

13. Such a reduction of market freedoms to the principles of equal treatment would also remove the concern of the ETUC's "Social Progress Protocol", which maintains that social rights, and, in particular, the exercise of collective bargaining, would remain unaffected by market freedoms.

14. Alternatively, the reduction of market freedom to equal treatment principles could be confined to the field of employment and social legislation of Member States, as defined in the competence standard of Article 153 TFEU. This would continue to address the concerns of the ETUC's "Social Progress Protocol", but Member State arrangements for the common good and social equality beyond those under the labour and social constitution of the Member States would remain difficult.

15. Although it lies outside the focus of the "European Pact on Social Progress", considering the interests of employees in the Union, it would be very urgent to remove the labour and social constitution of the Member States from the scope of competition law and from actions sanctioned by macro-economic surveillance to stabilise the euro.

16. The principle of territorial equal pay, which is expressed by the formula "equal pay for equal work in the same place", is central to preventing transnational competition based solely upon labour costs. This, in turn, is a pre-requisite for the continuation of, or at least slow development in Member States of the welfare state, which can continue provided the internal market does too.

17. Market freedoms and current secondary legislation (Posting of Workers Directive, Regulation on Co-ordination of Social Security Systems) place legal limits on the implementation of the principle of territorial wage equality. On the one hand, the principle requires, in part, treatment that is openly different and which would not allow market freedoms even after a reduction to equal treatment principles. On the other hand, secondary legislation exists which does not acknowledge the significance of the principle of territorial wage equality.

18. Anchoring the principle of territorial wage equality in primary law promises justification for open differences in treatment. It must be added to the existing justifications for open differences in treatment provided by the applicable primary law for each of the market freedoms (Articles 36, 52 (1), 62, 65 (1) (b) TFEU). In order to correct the misaligned secondary legislation as well, Member States would have to be allowed, by way of a protocol statement, to deviate from these rules, to the extent that they serve to implement the principle of territorial wage equality.

INDUSTRIAL RELATIONS AND LABOUR LAW IN THE EU ECONOMIC GOVERNANCE MECHANISMS: THE CASES OF ITALY AND GERMANY

Francesco Costamagna[141]*

University of Turin & Collegio Carlo Alberto

1. The Reform of the European Economic Governance: Strengthening the Disciplinary Powers of EU Institutions

1.1 The Co-ordination of Economic Policies within the European Semester

When the crisis struck, the Commission, backed by some Member States, was swift to point to the defects of the EMU legal framework as the main cause for the instability of the common currency. This argument, which conveniently overlooked the structural economic imbalances affecting the EMU, quickly became part of the dominant narrative and paved the way for subsequent reforms which aimed at strengthening the disciplinary powers of EU institutions.

In 2011, the European Parliament and the Council adopted a package of six legal acts – the so-called Six Pack – in order to strengthen budgetary discipline, introduce a new surveillance mechanism on macroeconomic imbalances and enhance the co-ordination of economic policies. The reform of the Stability and Growth Pact (SGP) went hand-in-hand with the adoption of the *Treaty on the Stability, Co-ordination and Governance in the Economic and Monetary Union* (TSCG) by 25 Member States.[142] These reforms strengthened the rules that guarantee budgetary discipline and changed the way in which decisions are taken at various stages of the surveillance procedures. In particular, the Six Pack established that sanctions in the context of the Excessive Deficit Procedure were to be decided by reverse qualified-majority.[143] This means that Commission recommendations proposing to sanction a Member State is adopted unless a qualified-majority of Member States within the Council votes against it.

The hardening of budgetary rules and procedures was associated with the revamping of economic policy co-ordination through the creation of the European Semester. The Semester brings under the same umbrella different strains of EU policy co-ordination and surveillance that touch upon both economic and social policies.

If compared with previous co-ordination processes, the Semester sensibly enhances the capacity of policy formulation, guidance and monitoring of EU institutions in virtually the entire spectrum of Member State economic and social policies. This is mainly due to the combination of soft co-ordination processes with hard surveillance mechanisms. Despite nominally retaining a non-binding character, the recommendations adopted in this context engender a level of compliance that is higher than that which may be inferred from Article 288 TFEU. Indeed, hard-law processes can be used to put pressure on national authorities so as to make them adopt the recommended reforms in the social and labour fields. As plainly put by the Commission:

> "[i]t is primarily in Member States' own interests to implement the reforms that will help them recover from the crisis and create the foundations for sustainable

141* The paper has been written in the context of the RESCEU project (Reconciling Economic and Social Europe, www.resceu.eu), funded by the European Research Council (grant no. 340534).

142 Signed on 2 March 2012 and entered into force on 1 January 2013.

143 Article 6(2) Regulation (EU) 1173/2011. See, generally, Rainer Palmstofer, "The Reverse Majority Voting Under the 'Six Pack': A Bad Turn for the Union?", (2014) 20 *European Law Journal*, 186-203.

growth. […] As a last resort, there is the prospect of sanctions if Member States repeatedly fail to take action on public finances or macroeconomic imbalances (under the Excessive Deficit Procedure and the Excessive Imbalance Procedure, respectively)."[144]

Furthermore, the Semester allows EU institutions to exercise quasi-normative functions, by issuing recommendations that are very detailed and that are not just "broad guidelines", as envisaged by Article 121 TFEU. For instance, in 2017, the French government was recommended to:

> "Consolidate the measures reducing the cost of labour to maximise their efficiency in a budget-neutral manner and in order to scale up their effects on employment and investment. Broaden the overall tax base and take further action to implement the planned decrease in the statutory corporate-income rate."[145]

These recommendations constrain the autonomy of national authorities, leaving non-compliance as the main way out. Yet, this option is not readily available to all Member States. Due to its power-based nature, the effectiveness of the mechanism depends on the vulnerability of the Member State to this threat. Those Member States at risk of being put under an excessive deficit procedure have few other options but to comply with the supranational recommendations.

The case of France and, more specifically, the adoption of the so-called *Loi Khomri* (or *Loi Travail*) offers a good example in this regard.[146] After the onset of the crisis, the French budgetary position was problematical, and, in 2009, the Council formally opened an excessive deficit procedure against France.[147] Little happened until 2013, when the Commission and the Council started to put greater emphasis on the link between the "correction of the fiscal imbalances" and "a credible implementation of ambitious structural reforms to increase the adjustment capacity and boost growth and employment".[148] In particular, France was recommended to reduce the cost of labour and to "ensure that developments in the minimum wage are supportive of competitiveness and job creation".[149] The same occurred, with only minor terminological variations, in 2014[150] and 2015.[151] All these recommendations were adopted upon the basis of Article 6 Regulation (EU) No. 1176/2011. In February 2015, the French Government bowed to the pressure, passing a law that aimed at rendering the labour market more business-friendly. The law was adopted by an executive order,[152] so as to avoid the possibility of the *Assemblée Nationale* rejecting it and thus sending "the wrong signal to the European Commission, a week before deciding whether to fine France for missing its deficit targets".[153] The decision paid off as the Commission refrained from penalising

144 http://europa.eu/rapid/press-release_MEMO-14-388_en.htm.

145 Council Recommendation of 11 July 2017 *on the 2017 National Reform Programme of France and Delivering a Council Opinion on the 2017 Stability Programme of France*, OJ C 261 of 09.08.2017, 39.

146 R. Erne, "A Supranational Regime that Nationalizes Social Conflict: Explaining European Trade Unions' Difficulties in Politicizing European Economic Governance", (2015) 56 *Labor History*, 345, 348.

147 Council Decision No. 2009/414/EC of 27 April 2009 *on the existence of an excessive deficit in France*, OJ L 135 of 30.05.2009, 19-20.

148 Council Recommendation of 9 July 2013 *on the National Reform Programme 2013 of France and Delivering a Council Opinion on the Stability Programme of France*, 2012-2017, OJ C 217 of 30.07.2013, 31.

149 Ibid.

150 Council Recommendation of 8 July 2014 *on the National Reform Programme 2014 of France and Delivering a Council Oopinion on the Stability Programme of France, 2014*, OJ C 247 of 29.07.2014, 47-48.

151 Council Recommendation of 14 July 2015 *on the 2015 National Reform Programme of France and Delivering a Council Opinion on the 2015 Stability Programme of France*, OJ C 272 of 18.08.2015, 55.

152 The *Loi Travail* was published in the *Journal officiel* only on 6 August 2016, after several versions had been rejected either by the *Assemblée Nationale* or by the *Senat*.

153 A-S. Chassany, "French Government Overrides Parliament to Ram though Reforms", *Financial Times*, online edition, 17 February 2015, available at: https://www.ft.com/content/3e2f4314-b67b-11e4-a5f2-00144feab7de.

France, despite its failure to bring the deficit under the 3 per cent threshold.[154]

1.2 Financial Assistance Programmes and Conditionality

The strengthening of capacity of supranational institutions to intrude into the regulation of national labour markets is even more intense in the context of financial assistance programmes. As is well known, each bailout entailed that the beneficiary Member State respected a set of policy conditions agreed with EU institutions, acting on behalf of the donors. Conditionality entrusts supranational institutions with an unprecedented capacity to engage in close surveillance and micromanagement of social policy, placing powerful constraints on the autonomy of national authorities in managing their social systems. This capacity hinges upon the uncertain legal location of the instruments governing the definition of the conditions attached to financial assistance packages.[155] This allows EU institutions to exploit fully the political and economic power asymmetries between them and any Member State that is facing extreme financial difficulties.

The main legal source of bailout programmes is the Memorandum of Understanding (MoU), which details the requirements that the beneficiary Member State must meet in order to receive financial assistance. The legal nature of this document, and even its capacity to set legally-binding obligations, has long been – and, to some extents, still is – highly controversial. It was just in June 2017, nine years after the launch of the first bailout programme, that the CJEU made it clear that the MoU is mandatory and "constitutes an act of an EU institution", according to Article 267 TFEU.[156] However, the case in question concerned a specific financial assistance programme that, directed towards a non-euro Member State facing difficulties with its balance of payments, was set up upon the basis of Article 143 TFEU and Regulation 332/2002. As for non-EU-based bailout programmes, the CJEU has traditionally adhere to the vision according to which the Memorandum's provisions fall outside the EU legal framework. Upon this basis, the CJEU rejected all the annulment actions brought by private applicants against these provisions and all the requests for preliminary rulings which sought to ascertain the compatibility, with the EU Charter on Fundamental Rights, of national measures adopted to implement the conditions set out in the MoU. The Court has recently been given the chance to shed more light on this issue, but it deliberately avoided it.[157]

2. The Subordination of Social Objectives to Economic Ones: Labour Reforms as Tools for Pursuing EMU-Related Objectives

Both the European Semester and bailout mechanisms were created to consolidate the EMU, by filling structural gaps. Thus, it is hardly surprising that they tended to focus on a narrow set of objectives – such as budgetary discipline and competitiveness – that are directly linked to the consolidation of the EMU. Other conflicting objectives, such as social ones, have been mainly relegated to second-tier status, in a way that flies in the face of

154 European Commission, *Recommendation for a Council Recommendation with a View to Bringing an End to the Excessive Government Deficit in France*, 27 February 2015, COM(2015) 115 def.

155 Claire Kilpatrick, *The EU and its Sovereign Debt Programmes: The Challenges of Liminal Legality*, (2017) EUI Working Paper 2017/14, 3-8. See, also, Agustín José Menéndez, "The Crisis and the European Crises: From Social and Democratic Rechtsstaat to the Consolidating State of (Pseudo-)technocratic Governance", (2017) 44 *Journal of Law and Society*, 74-78 (hereinafter Menéndez, "The Crisis and the European Crises"); Francesco Munari, "Crisi dell'Euro e crisi delle regole: Rule of Law o ragion politica? Il diritto dell'Unione europea dinanzi a nuove sfide", in: Ornella Porchia (ed), *Governance economica europea. Strumenti dell'Unione, rapporti con l'ordinamento internazionale e ricadute sull'ordinamento interno*, (Torino: Giappichelli, 2015), pp. 33-56.

156 *Florescu* [2017] ECLI:EU:C:2017:448, para. 35. See Menelaos Markakakis and Paul Dermine, "Bailouts, the Legal Status of Memoranda of Understanding, and the Scope of Application" (2018) 55 *Common Market Law Review* 643, 643-671; Alberto Miglio, "La condizionalità di fronte alla Corte di Giustizia", (2017) 11 *Diritti umani e diritto internazionale* 763, 763-770.

157 Judgment of 27 February 2018, *Associação Sindical dos Juizes Portugueses*, C-64/16.

the equal ranking model enshrined in the Treaties. In this context, labour market reforms have been mostly conceived as tools that should contribute to the pursuit of EMU-related objectives. The cases of Italy and Germany make no exception in this regard, even though the recommendations directed at the two countries are divergent as far as their content is concerned.

2.1 The Case of Italy

Italy was put under strong pressure to adopt reforms that could remove those elements that were perceived as "rigidities", so to make its regulatory framework more flexible and, thus, capable of contributing to enhance the competitiveness of the national economic system. These reforms should foster internal devaluation, which, in a monetary union in which currency devaluation is no longer an option and in which there is no centralised fiscal capacity, has seemingly become the only adjustment variable to respond to structural imbalances.

This was the case of the (in-) famous letter[158] sent to the Italian Government by the ECB President and the Governor of the Bank of Italy in August 2011. In particular, the letter urged "to further reform the collective wage-bargaining system allowing firm-level agreements to tailor wages and working conditions to firms' specific needs and increasing their relevance with respect to other layers of negotiations", and to engage in a "thorough review of the rules regulating the hiring and dismissal of employees [that] should be adopted in conjunction with the establishment of an unemployment insurance system and a set of active labour market policies capable of easing the reallocation of resources towards the more competitive firms and sectors".

A similar approach was followed in the context of the co-ordination of national economic policies, especially in its early cycles. For instance, in 2011, the Council recommended Italy to "reinforce measures to combat segmentation in the labour market, also by reviewing selected aspects of employment protection legislation including the dismissal rules and procedures and reviewing the currently fragmented unemployment benefit system taking into account the budgetary constraints". For greater certainty, the Council made clear that these reforms, to be carried out in consultation with the social partners, had to be primarily aimed at ensuring that "wage growth better reflects productivity developments as well as local and firm conditions, including clauses that could allow firm level bargaining to proceed in this direction".

The situation changed in 2015: from that cycle onwards, supranational institutions started to pay greater attention to other issues, such as promoting active labour market policies or enhancing labour market participation by women. This change is due to two main factors.

First, it reflects the push toward the so-called "socialisation" of the Semester, a process that started in 2013, which touches upon both its organisational and its substantive components.

With regard to the first aspect, since 2013, there has been an attempt to make the drafting of the CSRs more collaborative, involving Commission Directorates General other than just ECOFIN. Moreover, the Commission has tried to enhance the participation of national and EU social partners in various supranational phases of the co-ordination process, establishing new venues for involvement and providing better access to decision-making *fora*. These changes, while potentially interesting, have had only a limited impact on the way in which the Semester works, at least to date. For instance, looking at the involvement of the social partners, a recently paper published warns against the risk that all these reforms may well end up increasing the opportunities for the social partners to be listened to, while leaving their capacity

158 The letter can be found here: http://www.corriere.it/economia/11_settembre_29/trichet_draghi_inglese_304a5f1e-ea59-11e0-ae06-4da866778017.shtml?refresh_ce-cp.

to be heard substantially unchanged.[159]

Turning to the substantive dimension, the Commission sought to reinforce and deepen social and employment surveillance and co-ordination within the Semester. This mainly materialised in the introduction of new scoreboards and indicators to monitor employment and social developments, confirming the Commission's highly technocratic approach towards social policy and its continuous faith in numbers as governing tools. For instance, in 2014, the Commission included a number of auxiliary employment and social indicators within the group informing the Alert Mechanism Report of the macroeconomic imbalance procedure (MIP) to complement the only social indicator already existing in that context, which focused on unemployment.[160] This evolution is set to be bolstered by the adoption of the European Pillar of Social Rights, proclaimed with much fanfare in November 2017.[161] According to the Annual Growth Survey (AGS) 2018, the Pillar should "serve as a point of reference for the further implementation of the European Semester", as it is "a compass for renewed convergence towards better working and living conditions".[162] Concretely, the document is set to inspire a further set of indicators aiming at "monitor[ing] 'societal progress'" and detecting "the most significant employment and social challenges facing the Member States, the EU and the euro area, as well as progress achieved over time".[163]

Second and, to some extent, more importantly, the decision to reduce the pressure on the Italian government with regard to the adoption of competition-enhancing reforms of the labour market is due to the fact that, in 2014 and 2015, Italian law-making authorities adopted a series of statutes and decrees commonly known as the "Jobs Act". This reform transposed most of the recommendations issued by EU institutions into the Italian system, especially with regard to the flexibilisation of the labour market.

2.2 The Case of Germany

The recommendations addressed to Germany confirm the tendency to subordinate labour market reforms to the logic and objectives of EMU, even though, in contrast to the case of Italy, they do not aim to make the labour market more flexible or to reduce wages. On the contrary, Germany has been considered a role model for all the other Member States with regard to the adoption of labour market reforms primarily directed at enhancing the competitiveness of the national economic system. Indeed, in 2003 and 2005 the German authorities had already adopted sweeping measures increasing the flexibility of the labour market through, *inter alia*, the de-regulation of mini-jobs.

However, starting from the 2013 cycle of the Semester in particular, the EU institutions began to put pressure on the German authorities to adopt measures that could enable wage growth and facilitate the transition from non-standard employment, such as mini-jobs, into more sustainable forms of employment. These recommendations were issued upon the basis of Article 6 of Regulation 1176/2011, in the context of the preventive arm of the Macroeconomic Imbalances Procedure. The main aim of these recommendations is not to improve the situation of mini-workers, although this would be an inevitable side-effect, but to stimulate internal demand and, consequently, reduce the current account surplus run by Germany.[164] The adoption of expansive measures with regard to

159 S. Sabato, B. Vanhercke and S. Spasova, *Listened, but not Heard? Social Partners' Multilevel Involvement in the European Semester*, OSE Paper Series, Paper No. 35/2017.

160 European Commission, *Alert Mechanism Report 2014*, Brussels, 13 November 2013, COM(2013) 790 final, 10.

161 S. Garben, "The European Pillar of Social Rights: Effectively Addressing Displacement?", (2018) 14 *European Constitutional Law Review* 215.

162 European Commission, *Annual Growth Survey 2018*, 22 November 2017, COM(2017) 290 final, 3.

163 Commission Staff Working Document, *Social Scoreboard*, Brussels, 26.04.2017, SWD(2017) 200 final, 2.

164 As confirmed by the 2018 In-Depth Review carried out by the Commission, the German current account surplus is edging down, but it remains well above the 6 per cent MIP threshold.

labour market regulation is, thus, primarily meant to address these imbalances, thereby contributing to reinforce the stability of the EMU.

The main problem lies with Germany's compliance with these recommendations and, more in general, with the credibility of the whole process. An assessment carried out by the Commission in March 2018 admitted that Germany has made only limited progress in promoting the transition towards more stable forms of work and in promoting real wage growth, among the other things. This could be partially attributed to the choice made by the EU institutions, and the Commission in particular, to consider Germany to be in a situation of "macroeconomic imbalances" and not in one of "excessive macroeconomic imbalances". This means that there are no signs that Germany might be placed under an Excessive Deficit Procedure any time soon and, thus, be forced to adopt corrective actions. From a legal perspective, there are no obstacles for this step to be taken: the notion of "excessive imbalances" is vague enough to cover situations such as the one in hand.

WHAT TO EXPECT FROM GERMANY FOR THE EUROPEAN PILLAR OF SOCIAL RIGHTS AND BEYOND?

Marcel Hadeed

Hertie School of Governance, Berlin

"Everywhere in Europe I said: a German finance minister is a German finance minister, regardless of his party card. I believe the message was well received"[165]

-Olaf Scholz, German finance minister, 22.03.2018

It is my aim to highlight some of the guiding principles of the German position towards the EMU's social dimension in order to ascertain what can be expected from the German government for its development. The paper begins by contextualizing Germany's current macroeconomic position. It then elaborates on cornerstones of Germany's policy towards the EMU's social dimension. These are exemplified in the case study of the German position towards the European Pillar of Social Rights (EPSR). It concludes with expectations this position raises for the future of German efforts towards strengthening the EMU's social dimension.

Background – Germany's position and priorities

In order to assess the German position, it is important to first realize the current socio-economic reality in Germany. The employment statistic looks historically well. 2017 not only marked the record year in terms of employment – with 44.28 million employed – but also a record low in terms of unemployment (2.53 million or 5.7%)(Bundesregierung 2017a). With growth of 2.3% of GDP projected for 2018 and 2.1% for 2019 (Bundesministerium für Wirtschaft und Energie 2018), decreasing sovereign debt (Reiermann 2018) and increasing national budget (increase from €329.1 billion in 2017 to 335.5 in 2018), (Bundesfinanzministerium 2017) Germany has every reason to feel assured of the aptness of its social market economy, the success of its growth model and its economic policies. With the current budget, it can thus confidently respond to calls for both fiscal prudence and more investments and continue the status quo politics Angela Merkel has attained notoriety for (Kohler 2013; Sirleschtov 2017).

Accordingly, strengthening the EMU's social dimension is not a policy priority for the German government. In his speech in May 2018, the German minister for Labor and Social Affairs, Hubertus Heil, identified four priorities for his department: reserves for cyclical unemployment; structural unemployment; digital upskilling of the labor force; and the integration of people with disabilities into the labor market (Heil 2018). None of them relate to the EU.

Beyond these issues of system maintenance and incremental improvements, forward-looking debates are taking place in German ministries. These revolve around broader considerations about the future sustainability of the German social market economy. Managing digitalization and coping with demographic change are priority issues, as evident from constant debates about the sustainability of the pension systems and the comprehensive consultation activity in connection with the "forth industrial revolution" (e.g. "Work 4.0"; "Industry 4.0"; "*Mittelstand* 4.0"). The necessity to update employment- and social policy for the 21st century also informs Germany's position towards the European level, where it calls for a comprehensive update of the European *Social Acquis* (Bundesregierung 2016). Any revision of the social model on national level, or further development on the European level has to pay due diligence to the trends that are expected to transform the world of work.

Nonetheless, whoever had hoped for the pro-European focus the SPD appeared to promise in the run-up to the elections was left disappointed. Not only the lacking portfolios from the Ministry

165 Translation by the author

of Labour and Social Affairs, but the reassurance of finance minister Scholz that "*a German finance minister is a German finance minister, regardless of his party card*" (Scholz 2018) confirm the Grand Coalition's outlook on the Eurozone has not changed much since its reelection. In its coalition agreement, the relevant portfolio remains meager and vague.[166]

Ascertaining that Germany's position will likely not change significantly leads to the question of what this position rests on. The next section identifies cornerstones of the German position towards developing the EMU's social dimension and relate them to current debates.

Cornerstones of the German position towards the EMU's social dimension

The German position towards the EMU's social dimension shaped by a number of constraints on the national and European level that prevent it from taking meaningful action to address the asymmetry between economic and social integration. On the European level, one core dictum is compatibility with its overall approach towards the governance of the EMU.

The German imprint on the EMU is often said to be ordoliberal (Blyth 2013; Dullien and Guérot 2012; Stiglitz 2015). Although clear differences between the post-crisis EMU and the ordoliberal ideal type can be distinguished (Hadeed 2017; Hien and Joergesn 2018), the strengthening of the ostensible rule-based system that marked crisis-resolution adheres on first glance to the de-politicization of economic decisions already envisioned by the ordoliberal founding fathers (Böhm, Eucken, and Grossmann-Doerthe 1989[1936]). Regardless of the ideological (in)coherence of those reinforcing measures, they fit the pervasive German narrative member states as virtuous savers or undeserving rule-breakers (Offe 2015). Ordoliberalism thus lent the theoretical justification of German crisis politics that focused on austerity and structural reforms.

Germany invested much political capital in upholding these imperatives: both domestically – the contestation of which brought forth the *Alternative für Deutschland* as anti-Euro party, and in Europe - where its approach reaped particular scorn from southern Europeans (for the Italian case see Olmastroni and Pellegata 2018). Compatibility with it is the underlying theme was a therefore a precondition for any measure in social- and employment policy. Any initiative in this domain has to be evaluated on terms of financial sustainability and international competitiveness, and must not relieve pressures for national structural reforms or induce moral hazard (Bundesregierung 2016).

The protection of the post-crisis architecture as first cornerstone is reflected in the German policy priorities, (Scholz 2018) and in its discourse. Whereas the completion of the Banking Union is an often-discussed priority, distinctly social portfolios receive very little attention.[167] Instead, the German discourse about a more social Europe draws on a variety of portfolios, such as the Banking Union and the transformation of the ESM to an EMF that are regarded as instruments for "help to help themselves"[168] (Schäuble 2014), and thus contributing indirectly to social justice. Secondly, dossiers with questionable social implications receive a distinctly social framing. This became clear in the debate surrounding the Posted Workers Directive, which was hailed by the government as an advancement of the social rights of posted workers (Bundesregierung 2017b). The alternative view that the aim of the revision was the protection of domestic workers from "undue"

166 It includes the vague calls for fair conditions for workers, better coordination of employment policies, a framework for minimum wage and national basic social security schemes, as well as better comparability of education standards (Coalition Agreement 2018, 7)

167 Incidentally, Angela Merkel abstained from the Gothenburg Social Summit to oversee the coalition talks, leaving Germany without a representative at the occasion (Riegert 2017)

168 Translation by the author.

competition and indeed impeding on the social rights of posted workers – a position articulated by seven particularly affected Member States[169] in an open letter to the Commission (Kalfin et al. 2015) – received rather little attention.

The second principle shaping Germany's general outlook on the EMU's social dimension revolves around the *protection of its national socio-economic system* from outside reform pressures. Its insistence on the primacy of national competencies relies on three distinct concerns. *Legal limitations* arise not only in view of the Treaties, but also of the German Basic Law. This insistence is backed by the German Constitutional Court in the EMU case: As long as there is no democratic equivalent to national parliaments on EU level and an expansion of competencies through new legal bases, a transfer of competencies in employment- and social policy cannot be compatible with Germany's democratic character (Bundesverfassungsgericht 1998). Neither can it change the constitutional identity, in which pillars of the social market economy are enshrined (ibid). Particularly, the status of the social partners, which have the constitutional right to free collective bargaining (*Tarifautonomie*) limits the instruments that can be used to foster convergence by excluding the possibility of wage-coordination regimes, a vital tool to address divergence in the Eurozone (e.g. Johnston, Hancké, and Pant 2014; Manow 2016).

Beyond these legal concerns, the German government fears forced convergence might lead to *downward pressure* on the German social system, and disregard the institutional particularities in which policies must be evaluated (Bundesregierung 2016). In an environment of such institutional divergence, fear of such pressures is a powerful constraint on German policy. Lastly, a red line for the German government is the idea of a *transfer union* (Bollmann and Kloepfer 2018). It opposes German economic orthodoxy (Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung 2017), and is politically toxic. Transfers are interpreted broadly, spanning not only direct payments but also those that result from differences in the quality of social structures. An ardent argument against a European Unemployment Insurance has long been that it would disproportionately benefit member states with weaker active labor market policies. This would not only relieve reform pressures but also induce *moral hazard* (Feld and Osterloh 2013).

Combined these constraints result in a reluctant Germany that focuses on maintaining and consolidating its own socio-economic model, as well as the general thrust of the EMU post-crisis governance.

Nonetheless, drivers for reform also exist. the German government is not unaware of the social challenges and the need for socio-economic convergence in the EU. It sees the social challenge on the European level as twofold: (1) coping with the persistent challenges of the crisis and divergence; and (2) making employment- and social policy future-proof with regard to globalization, digitalization and demographic change (Bundesregierung 2016).

To address the former, Germany argues for continued structural reforms, particularly in Member States with persistent struggles. The recent proposals by Angela Merkel for a new investment budget and the development of the ESM into and EMF are the core of the German vision for convergence (Gutschker and Lohse 2018). In contrast, realigning social- and employment policies, convergence of social standards and living conditions and "future-proofing" of social systems should be pursued through softer instruments, particularly the development of benchmarks and best-practice exchange (Bundesregierung 2016). The constraints elaborated above prevent any meaningful action towards addressing the EMU's social imbalance with the same type of rigidity as issues of competitiveness.

The result is a German approach towards the development of the EMU's social dimension that is both, endorsing in principle, and rejecting in

169 Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia

effect. The elaborated drivers and constraints create the following dilemma: Germany's constraints prevent it from committing to strong instruments for convergence, which is – by alleviating concerns of downward pressure or transfers – simultaneously a precondition to agree on binding measures. The failure of convergence is thus at the same time the source and the result of the German inhibition (Bundesministerium der Finanzen and DIW Berlin 2018). This circular reasoning has yet to be broken.

Naturally, there are also political drivers. The uptick in populism in recent years, not least the elections in Italy, combined with an ambitious and increasingly impatient French president Macron undoubtedly pressure the German government to "do more". Between the ongoing MFF-negotiations, the upcoming European Parliament elections in 2019, and the official British withdrawal, a window of opportunity is for decisive action is still open, but quickly closing.

The extent to which these political considerations motivate Germany to agree to concessions in its position is yet unknown. Movement can be observed on the dossier of a European Unemployment *Re*insurance scheme. The German government had consistently rejected proposals made first by then Commissioner László Ándor (Wettach and Krumrey 2014) and later Italian finance minister Pier Carlo Padoan (Maggiore and Leontopoulos 2017). With its labor market in excellent shape, the German government fearing that such an arrangement would induce moral hazard and result in permanent transfers, thusly rejecting the proposal – a position shared by the German Council of Economic Experts (Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung 2017). The recent endorsement for an unemployment reinsurance by finance minister Scholz (Reiermann and Sauga 2018) might be a nod to the elaborated political drivers, and skepticism about the economic benefit still exists in the German finance ministry (Bundesministerium der Finanzen 2017).

This can be viewed as an encouraging sign for a more accommodating German vision for the future of the Eurozone, but it is only one of three concrete proposals of the German government, and the remaining, the ESM's transformation into an EMF, and the investment budget for the Eurozone reinforce the mantra of the cash-for-reform approach as path towards improved living conditions in the EMU (Gutschker and Lohse 2018). This is in line with the overall German mantra of boosting competitiveness and consolidating the "achievements" of crisis politics. The German position towards the Commission's initial proposal for a European Pillar of Social Rights (EPSR) exemplifies the discussed factors and gives a comprehensive view on a German vision for fostering social convergence.

The German assessment of the EPSR

In April 2016, the European Commission published a Communication introducing a first draft for the EPSR, kicking of a comprehensive consultation process to which stakeholders, member states and ordinary citizens could contribute (European Commission 2016). In December that year, the government of the previous Grand Coalition submitted its comprehensive assessment of the EPSR to the Commission. It welcomed the Pillar's basic orientation as a step towards strengthening and operationalization the EMU's social dimension (Bundesregierung 2016). This endorsement was, however, conditional on keeping the current division of competencies and the absolute prevention of pooling of costs for social systems. This relates to the constraints of preventing outside reform pressure and being drawn into financial obligations. A categorical no was directed at any transfer of competences to the European level and the primary "*Gestaltungskompetenz*" was to remain with Member States (Bundesregierung 2016). It concluded that therefore the EPSR could only take the form of a recommendation, (ibid.) which is by nature non-binding. The pillar is viewed as useful to foster upwards convergence of social security systems in specified domains, improve coordination between Member States and identify common principles. Crucially, this upward convergence is understood to be achieved through structural reforms targeting efficiency and effectiveness of national social systems. This speaks to the alignment of social policy portfolios with the general thrust of the post-crisis EMU. The government therefore ensured that no binding measures could exert pressure on its social system, while encouraging such pressures in other Member States. It saw austerity politics and efficient social policy as intrinsically linked with each other. Only fiscal sustainability, achieved through structural reforms, can guarantee efficient social systems. Conversely, the efficiency of social systems contributes to competitiveness and thus fiscal sustainability of member states(ibid.). In this view, austerity and social convergence are compatible. The government made a compelling leap to connect conceptually what opposed each other empirically: austerity and social progress. Thereby moving into a policy stance in which it could well declare its support for the initiative while insisting on its compatibility with the dominant governance regime.

In this light, the EPSR's integration into the European Semester via the Social Scoreboard can be viewed as a consolidation of the structural reform approach. Its integration and its non-binding legal character ensure both the general thrust of the post-crisis EMU governance structure remained unchallenged by social considerations, ostensibly resolving the dichotomic relationship between fiscal and social demands. This position equally secured the maintenance of Eurozone governance' character and safeguarded the German social market economy from outside pressure, adhering to the German cornerstone of system maintenance.

In substance, too, the German position follows a logic of safeguarding its own institutional structures. Endorsement was given to the coordination of active employment policy and minimum standards of social security.[170] Here, Germany sees great potential for improvement, primarily not with its own institutional structures, but especially in those countries that suffer most from high unemployment (ibid.). Other policy fields, chief among the pension systems, would not lend themselves to any kind of coordination, due to the difference in their institutional anchoring. Outright rejected are those proposals concerning the coordination of wage-setting processes, such as on minimum wages. Both of the elaborated cornerstones of German policy thus become visible in the approach and substance endorsed by the German position.

Conclusion – what to expect from Germany for the EPSR and wider social integration?

What can be drawn from these considerations to assess what can be expected from Germany for the future of the EPSR and the social dimension of the EMU more broadly?

Boosting the EMU's social dimension is not a priority for the German government, and is not featured in the coalition agreement, the relevant ministry's list of priorities, or the increasingly visible vision for reforming the EU in the coming years. The example of the EPSR shows how the dilemma of the German position towards social convergence prevents it from committing to binding measures. Consent for dossiers to strengthen the EMU's social dimension can only be expected where German particularities and national competencies remain shielded, and the overarching goals of convergence through structural reforms remains unchallenged. These are the preconditions for purposeful German endorsement. They dim hopes for German efforts towards meaningful social convergence in the EMU. Polit-

170 This is not surprising insofar as Germany had previously also supported the Youth Guarantee, the Recommendation on the integration of the long-term unemployed into the labor market, and the Skills Agenda.

ical drivers, and a window of opportunity have led to limited movement on the issue of a European Unemployment Reinsurance scheme, but the main thrust of Germany's recent proposal underscores its insistence on the primacy of structural reforms, and the preference for non-binding measures as the core mechanisms to achieve social convergence in the EMU. It falls in line with and must be compatible with the German overall approach towards the Eurozone and must protect the German social market economy from outside pressures. The verdict is thus a rather gloomy one: without resolving the constraint dilemma, one cannot expect much from Germany in the quest for a more social EMU.

References

Blyth, Mark. 2013. *Austerity: The History of a Dangerous Idea*. New York: Oxford University Press.

Böhm, Franz, Walter Eucken, and Hans Grossmann-Doerthe. 1989. "The Ordo Manifesto of 1936." In *Germany's Social Market Economy: Origins and Evolution*, eds. Alan Peacock and Hans Willgerodt. NewYork: St. Martin's Press, 292.

Bollmann, Ralph, and Inge Kloepfer. 2018. "Interview Mit Olaf Scholz: 'Europa Muss Schneller Reagieren Können.'" *Frankfurter Allgemeine Sonntagszeitung*. https://www.bundesregierung.de/Content/DE/Interview/2018/04/2018-04-15-scholz-fas.html.

Bundesfinanzministerium. 2017. "Eckwerte Zum Bundeshaushalt 2018 Und Finanzplan Bis 2021." https://www.bundesfinanzministerium.de/Content/DE/Bilderstrecken/Mediathek/Infografiken/bundeshaushalt-2018-2021-regierungsentwurf.html?notFirst=true&docId=120660#photogallery (June 14, 2018).

Bundesministerium der Finanzen. 2017. *Non-Paper for Paving the Way towards a Stability Union*.

Bundesministerium der Finanzen, and DIW Berlin. 2018. *Finanz- Und Sozialpolitik - Ein Spannungsfeld Im Europäischen Binnenmarkt*. Berlin.

Bundesministerium für Wirtschaft und Energie. 2018. "Wirtschaftliche Entwicklung Und Konjunktur." https://www.bmwi.de/Redaktion/DE/Dossier/wirtschaftliche-entwicklung.html (June 14, 2018).

Bundesregierung. 2016. "Stellungnahme Der Deutschen Bundesregierung Im Rahmen Der Konsultation Zur Europäischen Säule Sozialer Rechte." : 1–61.

———. 2017a. "Ein Starkes 2017 Am Arbeitsmarkt." https://www.bundesregierung.de/Content/DE/Artikel/2018/01/2018-01-03-arbeitsmarkt-jahresbilanz-2017.html (June 14, 2018).

———. 2017b. "Gleicher Lohn Für Gleiche Arbeit." https://www.bundesregierung.de/Content/DE/Artikel/2017/10/2017-10-24-entsenderichtlinie.html (June 14, 2018).

Bundesverfassungsgericht. 1998. *Beschluss Des Zweiten Senats Vom 31. März 1998 - 2 BvR 1877/97 Und 2 BvR 50/98*.

Dullien, Sebastian, and Ulrike Guérot. 2012. *The Long Shadow of Ordoliberalism : Germany ' s Approach to the Euro Crisis*. London.

"Ein Neuer Aufbruch Für Europa, Eine Neue Dynamik Für Deutschland, Ein Neuer Zusammenhalt Für Unser Land - Coalition Agreement between the CDU, CSU and SPD." 2018. https://www.bundesregierung.de/Content/DE/StatischeSeiten/Breg/koalitionsvertrag-inhaltsverzeichnis.html (June 14, 2018).

European Commission. 2016. "Communication Launching a Consultation on a European Pillar of Social Rights." SWD(2016)(50, 51).

Feld, Lars P, and Steffen Osterloh. 2013. *Is a Fiscal Capacity Really Necessary to Complete EMU?* Freiburg im Breisgau.

Gutschker, Thomas, and Eckart Lohse. 2018. "Interview with Angela Merkel: Existenzfragen Für Europa." *Frankfurter Allgemeine Zeitung*.

Hadeed, Marcel. 2017. "The Ordoliberal Ghost." *Social Europe*. https://www.socialeurope.eu/the-ordoliberal-ghost (September 4, 2018).

Heil, Hubertus. 2018. "'Mit Vereinten Kräften.'" http://www.bmas.de/DE/Presse/Reden/Hubertus-Heil/2018/rede-2018-05-18.html;jsessionid=8EDF44BA738150AD7ECB7C204EAD25EF.

Hien, Josef, and Christian Joergesn. 2018. "Dead Man Walking? Current European Interest in the Ordolierbal Tradition." *European Law Journal* 24(2–3): 142–62.

Johnston, Alison, Bob Hancké, and Suman Pant. 2014. "Comparative Institutional Advantage in the European Sovereign Debt Crisis." *Comparative Political Studies* 47(13): 1771–1800.

Kalfin, Ivailo et al. 2015. "Letter to Commissioner for Employment, Social Affairs, Skills and Labour Mobility." (July).

Kohler, Berthold. 2013. "Die Schutzherrin Des Status Quo." *Frankfurter Allgemeine Zeitung (online)*. http://www.faz.net/aktuell/politik/inland/kommentar-zur-wiederwahl-von-angela-merkel-die-schutzherrin-des-status-quo-12715473.html (June 14, 2018).

Maggiore, Maria, and Nikolas Leontopoulos. 2017. "Italiens Finanzminister Forder Eine Europäische Arbeitslosenversicherung." *Tagesspiegel*. https://www.tagesspiegel.de/politik/pier-carlo-padoan-italiens-finanzminister-fordert-eine-europaeische-arbeitslosenversicherung/20328310.html.

Manow, Philip. 2016. "Uniform Monetary Policy , Non-Uniform Wage Policy : How Rules and Discretion Get into Conflict in the Eurozone (and What – If Anything – Ordoliberalism Has to Do with It)."

Offe, Claus. 2015. "Narratives of Responsibility: German Politics in the Greek Debt Crisis." *Cassa della Cultura*: 1–30. http://www.casadellacultura.it/pdfarticoli/Claus-Offe-Narratives-of-Responsibility.pdf.

Olmastroni, Francesco, and Alessandro Pellegata. 2018. "Members Apart : A Mass-Elite Comparison of Mutual Perceptions and Support for the European Union in Germany and Italy." *Contemporary Italian Politics* 10(1): 56–75.

Reiermann, Christian. 2018. "Deutschlands Staatsverschuldung Sinkt 2019 Unter 60 Prozent." *Spiegel Online*. http://www.spiegel.de/wirtschaft/soziales/deutschland-staatsverschuldung-sinkt-2019-unter-60-prozent-a-1201557.html (June 14, 2018).

Reiermann, Christian, and Michael Sauga. 2018. "Interview Mit Olaf Scholz: Deutschland Hat Eine Besondere Verantwortung." *Spiegel*. http://www.spiegel.de/plus/olaf-scholz-deutschland-hat-eine-besondere-verantwortung-a-00000000-0002-0001-0000-000157769163.

Riegert, Bernd. 2017. "EU Social Summit: Fair Jobs, Fair Growth Must Be a Priority." *DW News*. http://www.dw.com/en/eu-social-summit-fair-jobs-fair-growth-must-be-a-priority/a-41430438 (June 14, 2018).

Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung. 2017. 2017/18 *Für Eine Zukunftsorientierte Wirtschaftspolitik*. Wiesbaden. https://www.sachverstaendigenrat-wirtschaft.de/fileadmin/dateiablage/gutachten/jg201718/JG2017-18_gesamt_Website.pdf.

Schäuble, Dr. Wolfgang. 2014. "Noch Nicht Über Den Berg - Zur Krise in Der Eurozone." https://www.bundesfinanzministerium.de/Content/DE/Reden/2014/2014-07-11-Stiftung-Ordnungspolitik.html.

Scholz, Olaf. 2018. "Regierungserklärung von Olaf Scholz, Bundesminister Der Finanzen, Zur Finanz- Und Haushaltspolitik Der Bundesregierung Am 22. März 2018 Im Deutschen Bundestag." https://www.bundesfinanzministerium.de/Content/DE/Reden/2018/2018-03-22-Aussprache-Regierungserklaerung.html.

Sirleschtov, Antje. 2017. "Wahlprogramm Der Union: Eine Politik Für Bewahrer Des Status Quo." *Tagesspiegel*. https://www.tagesspiegel.de/politik/wahlprogramm-der-union-eine-politik-fuer-bewahrer-des-status-quo/20014452.html (June 14, 2018).

Stiglitz, Joseph. 2015. "Europe's Lapse of Reason." *project-syndicate.org*. https://www.project-syndicate.org/commentary/european-union-austerity-backlash-by-joseph-e--stiglitz-2015-01.

Wettach, Silke, and Henning Krumrey. 2014. "Andors Pläne Stoßen Auf Breite Ablehnung." *Wirtschaftswoche*.

THE EU POLITICAL CULTURE OF TOTAL OPTIMISM IS NOT DEAD: REFLECTIONS ON THE EUROPEAN PILLAR OF SOCIAL RIGHTS

Vladimir Bogoeski

Hertie School of Governance

Introduction

In his "State of the Union Address" of September 2015 the President of the Commission Jean-Claude Juncker made a sincere confession, admitting that the Union was not in a good state.[171] But his speech was not entirely pessimistic, not even when he addressed the economic crisis. Rather, he announced a set of ambitious proposals, one of which was the European Pillar of Social Rights.[172] Reminiscent of the Maastricht pillars and their not so long history, it drew the attention of stakeholders, civil society and academics to speculate about what was behind this pompous announcement. By now, almost three years from its first announcement, the Social Pillar has not only been pinned down in an official Document, with stated principles and rights, but it has also been solemnly proclaimed by the Commission, the Council, and the European Parliament.[173] The intention behind the Social Pillar, as initially expressed by the Commission, is to respond to the social consequences of the economic crisis, on the one hand, and to contribute to the completion of a deeper and fairer EMU, on the other,[174] for which a social dimension is understood to be necessary.[175]

However, the optimism of the EU institutions, which accompanied the creation of the Social Pillar from its first announcement by President Juncker to the Proclamation of the final text in Gothenburg, might seem not to be coherent with what their ultimate accomplishment has to offer.[176] The final result strongly resembles a non-legally-binding declaration of rights which, for the most part, already exist,[177] and raises scepticism about the Pillar's capacity to remedy the problems that it has identified effectively.[178] Thus, this contribution looks behind the enthusiasm accompanying the Pillar, and sets out to examine its value through the concept of the "EU political culture of total optimism", as defined and elaborated by Giandomenico Majone.[179] The contribution argues that the Social Pillar is another example of the EU political culture of total optimism, rather than being capable of adding a genuine social dimension to the European integration project. The argument will proceed in three steps. (1) First, the EU culture of political optimism and its three main features, according to Majone, will be outlined. (2) The second section analyses the Pillar's objectives and its capacity to meet them, showing why it reflects the EU political culture of total optimism in exemplary fashion. (3) The last section concludes by considering the possible consequence.

171 President Jean-Claude Juncker, State of the European Union (SOTEU) Address, European Parliament, Strasbourg, 9 September 2015.

172 Ibid.

173 Proclamation of the European Pillar of Social Rights (EPSR), Gothenburg, 17 November 2017.

174 COM(2016) 127 final, Launching a consultation on a EPSR, at 3.

175 EPSC Strategic Note No. 5, (2015) "The Social Dimension of Economic and Monetary Union: Towards Convergence and Resilience".

176 See Florian Rödl, Soziale Rechte in Europa: Von irreführenden Versprechen und notwendigen Kämpfen, WSI-Herbstforum 2017; Martin Höpner, "Mogelpackung: Warum soziale Individualrechte die Europäische Union nicht sozialer machen", 25 May 2017, available at: http://www.ipg-journal.de/rubriken/europaeische-integration/artikel/mogelpackung-2047; Simon Deakin, "What Follows Austerity? From Social Pillar to New Deal", in: Frank Vandenbroucke, Catherine Barnard and Geert De Baere (eds), *A European Social Union after the Crisis*, (Cambridge: Cambridge University Press, 2017).

177 The Pillar does introduces a few new rights; see more in Zane Rasnača, "Bridging the gaps or falling short? The European Pillar of Social Rights and what it can Bring to EU-level Policymaking", ETUI Working Paper 2017.05.

178 See note 6 above.

179 Giandomenico Majone, "The Deeper Euro-Crisis or: The Collapse of the EU Political Culture of Total Optimism," Working Paper, 2015, http://cadmus.eui.eu//handle/1814/35281.

1. The EU Political Culture of Total Optimism

In a paper entitled “The deeper Euro-crisis or: The collapse of the EU political culture of total optimism”, Giandomenico Majone argues that one of the multiple dimensions of the euro-crisis has been its impact on the political culture of EU leaders.[180] His central thesis is that, during the euro-crisis, the previously dominating EU political culture of total optimism was replaced by “panic-driven austerity”.[181] Majone understands the concept of political culture as a collective property, “a system of empirical beliefs, expressive symbols, and values which defines the situation in which political action takes place”.[182] As the European Union (still) consists of 28 Member States, in which political culture varies greatly both across and within polities, he recognises that it would be misleading to speak of a political culture of the EU as a whole. In Majone’s understanding the concept of political culture, in the case of the EU, makes sense only if it is applied to the élites operating in the EU framework.[183]

Majone identifies three defining characteristics of the EU political culture of total optimism amongst the political élites, which also constitute the outcomes of the same mindset: 1) the emphasis on the process rather than the results; 2) the ignorance of feasibility constraints and possible risks; and 3) the disregard for the limits of collective action.[184] The following section analyses the goals and the content of the European Pillar of Social Rights in accordance with these characteristics of total optimism, in order to answer the question of whether the Pillar itself is a reflection of this political culture, or whether it entails some genuine potential to strengthen the social dimension of the EU and tackle the problems that it identifies.

180 Ibid., Abstract.

181 Ibid.

182 Majone relies on Verba’s definition of political culture as in Sidney Verba, “Comparative Political Culture”, in: Lucien W. Pye and Sidney Verba (eds), *Political Culture and Political Development*, (Princeton NJ: Princeton University Press, 1965), pp. 512-60.

183 Majone, note 9 above, at 2.

184 Ibid.

2. The European Pillar of Social Rights as a Reflection of the EU Political Culture of Total Optimism

The optimistic aura of the Social Pillar has been evident since it was first mentioned by President Juncker as a way forward after a decade of economic crisis.[185] The term Pillar, which apart from the reminiscence of the Treaty of Maastricht pillars might bring to mind the biblical pillar of strength,[186] also implies that it is an instrument with a certain political weight and with certain ambitions, which should bolster and mean progress for Social Europe. Europe-wide consultations took place over the course of ten months in 2016, stakeholders provided around 200 position papers, and 16,500 replies to the online dedicated questionnaire were received, upon the basis of which the Commission has recommended a final text for the Pillar.[187] This provided for a wide presence of the Pillar in various EU and Member State level debates. Finally, the optimism came full circle at the Social Summit in Gothenburg on 17 November 2017, where the EU institutions expressed support for and commitment to the Pillar in signing the official Proclamation.[188] But what is actually in the final text of this instrument, which has, for a moment, raised the hopes of affected stakeholders, civil society and Social Europe advocates? Did the mountain that shook bring forth a mouse? What can the final instrument, which we now call the Social Pillar - a non-legally-binding declaration of (mostly) already existing individual rights – actually do?

185 SOTEU Address in note 1 above.

186 “The Lord is my pillar, and my fortress …”, Psalm 18:2-4, The Holy Bible, Modern English Version.

187 SWD(2017) 206 final, Report on the public consultation, Brussels, 26.4.2017, at 5.

188 Note 3 above.

The Social Pillar as a Process

The consultations that took place between March and December 2016 identified four broad trends that the Pillar should address: (i) the social consequences of the crisis, including increasing poverty and exclusion, inequalities and unemployment, and low growth and competitiveness; (ii) the future of work and the emerging digital labour market; (iii) demographic developments, that is to say, the ageing of Europe's population; and (iv) economic divergence across the Member States.[189] Their common denominator is the Pillar's ambition to complement the existing EU "social *acquis*" by "giving new and more efficient rights to citizens, which set an agenda for better performing economies and more equitable and resilient societies".[190] This ambition becomes more flawed and ambiguous in the course of development of the several documents accompanying the Pillar. At certain point, in a contradictory manner, one of the documents says that the recognition of new rights is not the focus, but rather the enforcement of rights (the take up).[191] However, the documents repeatedly state that the Pillar needs to be seen as an instrument which will serve as a compass of convergence within the Euro area,[192] which brings us to the first feature of Majone's culture of total optimism, namely, the focus on the process, rather than the outcome. The Pillar aims to steer a process of further social convergence among the Member States of the Eurozone, which should eventually lead to deeper economic and monetary integration. The Pillar should guide both the EU's and the Member States' social policy choices towards achieving the ideals of the social rights that it contains, and they should - one day - converge under this guidance. The focus on social convergence as a process overshadows the concrete goal to which all the Member States *and* the EU itself should converge. This paradigm seems to be the contested "flexicurity" model that the Pillar intends to petrify as the European recipe for balancing social rights and economic freedoms,[193] by fostering the already well-known discourse of, in the words of Ruth Dukes, the "overestimation of the extent of shared interest between workers and employers".[194] Nonetheless, it becomes clear that the Pillar intends to activate a continuous process, but what remains unclear is its operative part, as well as when and what kind of concrete results should be expected.

The (In-) Feasibility of the Pillar

The question of results requires an inquiry into the feasibility of the Pillar's goals. The feasibility problem that Majone identifies with the EU political culture of total optimism arises due to the ignorance of the existing constraints and the possible risks when political decisions are made. In the case of the Pillar, we could talk of the factual or given constraints, on the one hand, and the feasibility constraints directly attributable to the Pillar's approach, on the other. As to the factual or pre-existing constraints, the Pillar does recognise the limits to common European social policy due to the high level of diversity of the national social models and the different levels of economic development among the Member States.[195] It even emphasises that the diversity of Member States' social models needs to be respected, thus allocating most of the implementation tasks to the Member States themselves.[196] Notwithstanding this, the most relevant constraint to the Pillar's

189 COM(2017) 250 final, Establishing a European Pillar of Social Rights, Brussels, 26.4.2017, at 4.

190 Note 19 above, at 4.

191 Ibid, at 7.

192 SOTEU Address in note 1 above; COM(2016) 127 final, note 4 above; COM(2017) 250 final, note 19 above; COM(2018) 130 final, Monitoring the implementation of the European Pillar of Social Rights.

193 COM(2016) 127 final, at 5; SWD(2017) 201 final, at 22 ff.

194 Ruth Dukes, "From the Labour Constitution to an Economic Sociology of Labour Law", final draft of a contribution to a Book Symposium, forthcoming in the journal *Jurisprudence.*

195 Rec. 19, Preamble, EPSR.

196 COM(2017) 250 final, at 2.

objectives to countervail successfully the social consequences of the economic crisis, market integration and labour market developments, is its inadequate approach to remedy these problems by declaring individual social rights.

Despite its solemn proclamation, the Pillar nonetheless remains a non-legally-binding document that declares 20 principles containing 35 individual social rights.[197] Many of these can be found in pre-existing documents, such as the EU Charter of Fundamental Rights, the European Social Charter of Turin 1961, and the Community Charter of the Fundamental Social Rights of Workers of 1989.[198] The language interchangeably referring to principles and rights is itself obscure.[199] However, it is not its non-legally-binding nature, but its approach to addressing the structural challenges of market integration and the years of austerity policies, such as inequality, poverty and inclusion, through individual rights, that is the Pillar's main weakness.

In his latest book, entitled *Not Enough: Human Rights in an Unequal World*, Yale's professor of Law and History, Samuel Moyn, argues that economic and social rights have failed to challenge inequality and distributive fairness both in the national and in the global political economy.[200] In a similar manner, the Pillar fails to recognise the constraints of the rights approach, thus possibly foreclosing on searching for other visions for serious re-distributive politics. Florian Rödl describes the pursuit of structural social objectives merely through the language of rights as the "juridical misconception" of social rights.[201] Social rights are different in nature from civil and political rights, as their effective realisation requires not only absence of arbitrary state action, but also elaborate legal structures and material resources.[202] The Social Pillar could neither make a considerable contribution to the establishing of the required legal framework and institutional structure, nor could it respond to the most critical point of weakness of such previous declarations of social rights, namely, that Member States could still invoke the pretext of "maximum available resources".[203]

As the effectiveness of most of the Pillar's rights and principles will depend on creating the necessary institutional set up mainly at Member State level, both the diversity of the national social models and the differences in economic development will probably be echoed in the Pillar's outcome. The Pillar itself acknowledges that judicial recognition and enforcement will not be enough to realise its programmatic principles effectively,[204] but does not give a clear lead as to how Member States are to establish and sustain the structures imperative for actualising rights and entitlements, such as childcare and support for children, social protection, unemployment benefits, minimum income, old age income and pensions, *etc*.[205] These concerns question the Pillar's capacity to deliver on its commitment to social convergence in the Eurozone and/or the EU in general.

The Limits of Collective Action

As Majone submits, collective actors face limitations compared to individual decision-makers, and "the larger the group, the further it will fall short of providing an optimal amount of a collective good".[206] In the case of the Pillar, however, we could not talk of a *total* disregard of/for the limits of collective action. What its approach finally shows us is the acknowledgement of the contradiction between the accepted diversity of national social models and the advancement of the idea of a fully-harmonised social sphere at supranational

197 See Höpner, note 6 above.

198 Rec. 3, Preamble, EPSR.

199 Frank Hendrickx, "Editorial: The European Pillar of Social Rights: Interesting Times Ahead", (2017) 8 *European Labour Law Journal*, 191-92.

200 Samuel Moyn, *Not Enough: Human Rights in an Unequal World*, (Cambridge MA: Harvard University Press, 2018).

201 Florian Rödl, note 6 above.

202 Ibid.

203 SWD(2017) 201 final, at 4.

204 Preamble recital (14), EPSR.

205 Chapter III "Social Protection and Inclusion", EPSR.

206 Majone, note 9 above, at 6.

level.[207] It is not only the budgetary constraints, but also the accepted varieties of capitalism[208] and socio-economic cultures within the EU that have lead researchers to recognise that full social harmonisation will not be the blueprint solution for the European social model.[209] In the light of this, in the pursuit of the collective good, defined as upward social convergence for better performing economic and monetary integration, the Pillar might downplay the diversity of the challenges that the different Member States are facing. Promoting this collective good of social convergence, the Pillar fails, first of all, to offer concrete and adequate protection to the existing Member States' social models from the potential negative effects of economic and monetary integration. It provides clear and concrete response to none of the two most pressing issues, namely, neither to the *Viking-Laval* controversy which has accompanied the decade of austerity policies, nor to the scenario in which future austerity policies could override national social objectives.[210]

Conclusion

As decision-makers in a political culture of total optimism would focus on the process rather than on concrete results, lessening the relevance of the existing feasibility constraints and the limits of collective action, offering some kind of a response might seem preferable to not offering a response at all. The Social Pillar represents this political culture in an exemplary fashion. It has come as a result of the necessity to act against the rising EU scepticism, attempting to countervail the arguments that the EMU, on the one hand, and the single market, on the other, have had negative consequences for social justice at both EU and Member State level.[211] The ubiquity of the debate on the Social Pillar together with its inter-institutional proclamation, have, without doubt, raised hopes, as we can, for example, observe in an official statement from a recent conference of trade union leaders from the Visegrád countries,[212] where, in support of their plea for an upward wage convergence and reduction of the East-West gap, they explicitly referred to Principle 6 of the Pillar.[213] However, as the disappointment of broken promises may easily result in increasing, rather than decreasing, Eurosceptic sentiments, the future of the EU's social dimension will largely depend on both the EU's and the Member States' capacity to go *beyond* the Pillar when developing and implementing concrete social policies in order to set and achieve social objectives. The Pillar leaves us with more questions than answers, but the political actors and stakeholders should nonetheless explore further the possible productive ways of using it, which should in no way foreclose on pursuing more progressive alternatives, following the latest example of the "European Pact for Social Progress".[214]

207 See Höpner, note 6 above; Christian Joerges, "Social Justive in an Ever More Diverse Union", in: Frank Vandenbroucke, Catherine Barnard and Geert De Baere (eds), *A European Social Union after the Crisis*, (Cambridge: Cambridge University Press, 2017).

208 Peter Hall and David Soskice, *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*, (Oxford: Oxford University Press, 2001).

209 See more on the concept of European Social Union in Vandenbroucke et al., note 6 above.

210 See Marcel Hadeed, "What to Expect from Germany for the European Pillar of Social Rights?", Paper presented at the conference, "Responses of European Economic Cultures to Europe's Crisis Politics: The Example of German-Italian Discrepancies", Villa Vigoni, 26-27 June 2018.

211 On the context of the Pillar, see Sacha Garben, "The European Pillar of Social Rights: Effectively Addressing Displacement?", (2018) 14 *European Constitutional Law Review*, 210-230, at 212 ff.

212 Statement, Meeting of trade union leaders of the Visegrád countries, Budapest, 10-11 May 2018.

213 Principle 6, EPSR: "Workers have the right to fair wages that provide for a decent standard of living."

214 A European Pact for Social Progress, Vienna, 29 November 2016. See Florian Rödl, "Austerity and Marketisation: *Viking, Laval* and the Proclamation of the New Social Dimension", Paper presented at the conference"Responses of European Economic Cultures to Europe's Crisis Politics: The Example of German-Italian Discrepancies", Villa Vigoni, 26-27 June 2018.

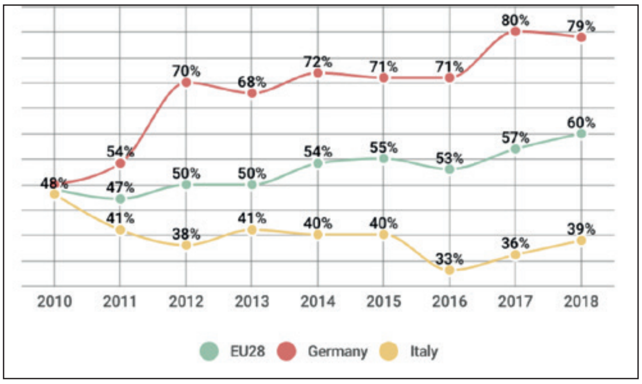
A 'MORE POLITICAL' LEADERSHIP FOR THE PRESIDENT OF THE COMMISSION? A MIXED-METHODS LANGUAGE-BASED ANALYSIS

Pamela Pansardi, University of Pavia

The multiple crises that have been affecting the EU since 2008 – the Eurozone crisis, the refugee crisis, the Brexit, to name a few – and the failure of EU institutions in effectively addressing them have posed a severe challenge to very foundations of the project of European integration (Börzel 2016: 25) and have led to what Juncker described as an 'existential crisis' (Juncker 2016). A crisis, first of all, in legitimacy and support, made more severe by the 'blame-shifting' model that permeates the rhetoric of Eurosceptic parties and movements.

In spite of this, the registered level of support for the EU and EU institutions varies greatly among member states. When comparing Germany and Italy, we immediately notice that these two countries align themselves on the opposite side of the continuum between a full and a scarce support. Data from EP Eurobarometer 2018 allow for an immediate comparison: While, between 2010 and 2018, Germany steadily attests itself above the means of EU countries, Italy constantly shows a level of support inferior to the average level (and, even more significantly, always below the 50%). Figure 1 presents the results for these two countries contrasted with the EU overall level.

Figure 1. Support for the EU: comparison between Italy and Germany



Source: Socio-demographic trendlines -EP Eurobarometer 2017-2018. Item: Membership of the European Union.

Given the legitimation crisis that has been affecting the European Union in the last years, the way in which EU institutions, and in particular, the President of the Commission as the EU main representative, communicate with the public plays a fundamental role in fostering reclaiming legitimacy not only for EU decisions, but for the EU integration process as a whole. Accordingly, the aim of this paper is to study the communicative strategies of the two latest Presidents of the Commissions to investigate their active role in reclaiming legitimacy and support for the EU.

Since the onset of the Eurozone crisis, the leadership role of the Commission amongst EU institutions has been deemed to be in decline (Bauer and Becker 2016). On the one hand, the difficult governance of the crisis witnessed the relative weakening of the supranational *vis-a vis* the intergovernmental approach, with the emergence of the European Council as the key political player (Dinan 2016; Fabbrini 2015). On the other hand, the political governance of the crisis has been to an extent replaced by an economic governance, strengthening, and to an extent, ‚politicizing' (Verdun 2017), the role of the European Central Bank (Tortola and Pansardi 2018).

A number of commentators (Christiansen 2016; Dinan 2016; Kassim 2017; Kassim et al. 2017), however, have highlighted a change of direction in the leadership role of the Commission after the appointment of Jean-Claude Juncker as its President. In particular, the literature suggests the emergence of a visible difference between Barroso's and Juncker's overall approaches to the Presidency (Kassim 2017; Kassim et al. 2017). Juncker himself, in the first of his State of the Union Addresses (2015), appeals to the Treaties in claiming for his mandate a ‚more political' role - implicitly intending, according to Dinan (2016), ‚more political' than the leadership style adopted by his predecessor, José Manuel Barroso, often accused of lacking assertiveness and being too deferential in dealing with national leaders, in particular those of Germany and France (Dinan 2016: 103). What has changed with Juncker's presidency, however, does not entirely derive from personal styles and choices: the introduction of the *Spitzencaditaten* system, in fact, and the President's possibility to claim for a personal, and more ‚democratic', mandate, has somehow contributed in strengthening the role of the President. While individual agency, characterized by differences in personality and individual leadership style certainly has an effect on the role that leaders claim for themselves, the introduction of the *Spitzencaditaten* procedure undoubtedly had an effect of Juncker's interpretation of his role, providing him with a different opportunity structure than the one of his predecessor.

In this paper, my aim is to empirically investigate and assess the presence of visible differences in the leadership styles of the two latest Presidents of the Commission as they emerge from their use of language in official speeches. While the content - in terms of topics touched and the relevance given to each of them - is undoubtedly fundamental in assessing the political perspective of a leader and his/her political goals, in this paper my focus will be rather on the rhetorical aspects of the speeches, with a particular focus on the tone of the language used: in particular, whether the language can be deemed to be a neutral, descriptive and unemotional language or whether it is closer to the ideal-type of charismatic, politicized language that often accompanies political leadership. While starting by summarizing the main points of previous work (Pansardi and Battegazzorre 2018) on the so-called ‚discursive strategies' of the two Presidents - based on a qualitative content analysis of a small number of highly significant speeches (the seven State of the Union Speeches from 2010 to 2017) aimed at investigating the rhetorical strategies used by the speakers in defining and reclaiming legitimacy for the EU -, the current work focuses on a quantitative assessment of the tone of the language used by the two Presidents in all of their official speeches (2010-2017) thanks to a dictionary-based analysis performed with the software DICTION 7. The paper will accordingly offer a mixed-method interpretation of the changes in the two Presidents' communication, and the results of these two strains of analysis will jointly allow us to empirically verify the claims of a greater ‚politicization' of Juncker's Presidency in terms of the use of language.

The paper is structured as follows. In the first section, I present the theoretical framework and main results of the analysis of the discursive legitimation strategies developed in Pansardi and Battegazzorre (2018) based on a qualitative analysis of the ‚symbols' included in the speeches. In the second section, I introduce the methodological perspective that shape the original software-based quantitative analysis of ‚charismatic language' in details. In the third sections, I present the results and offer a first assessment of the empirical findings. The last section discusses the results and concludes.

1. The study of the discursive legitimation strategies (SOTEU 2010-2017)

As expounded in Pansardi and Battegazzorre (2018), a way to investigate the Presidents' role in communicating the EU is to analyse how they have attempted to discursively represent and reclaim legitimacy for the EU in a particularly significant institutional setting: the delivery of the State of the Union Address (SOTEU). The SOTEU speech, first introduced in 2010, is the institutional occasion on which the President of the Commission openly addresses the past achievements, the most pressing challenges that the EU is currently facing, and sets the Union's priorities for the years to come. It is thus a public occasion for reflection on the identity and the future of the European Union. Accordingly, the SOTEU speech provides the paramount opportunity for the President of the Commission to speak not only to EP members and national governments, but also – to an extent – directly to European citizens, and to communicate his/her view on the nature and legitimacy of the European project, as well as to engage in rhetorical attempts to reclaim legitimacy for the EU.

Whilst *legitimacy* concerns the actual assessment of a particular state of affairs, *legitimation* consists in the process by which the belief in the rightfulness of the authority is claimed or conferred (Barker 2001; Hurrelman 2016). Top-down legitimation strategies should be understood as activities – institutional or discursive (Gronau and Schmidtke 2016) – distinct, at least in analytical terms, from the other activities of a political body. Following Gronau and Schmidtke, Pansardi and Battegazzorre (2018) define top-down legitimation strategies as: "goal oriented activities employed to establish and maintain a reliable basis for diffuse support for a political regime by its social constituencies" (Gronau and Schmidtke 2016: 541).

The particular need for top-down legitimation activities in the case of the EU, sometimes interpreted in terms of "political community-building and/or mythical foundations of identity" (Hansen and Williams 1999: 235) has always been recognized, and it proves of the utmost importance in dealing with the current crises. As Theiler writes: "fostering political legitimacy always has a 'top-down' symbolic dimension. This entails elite-driven construction and dissemination of symbolic categories which, if successful, stimulates more 'bottom-up' communicative and deliberative processes" (2005: 4). Legitimizing discourses are an integral aspect of political communication, and they consist of references to "specific linguistic resources and configurations of linguistic resources" (Van Leeuwen 2007: 92). In order to analyze the discursive legitimation strategies employed by the two Presidents of the Commission, Pansardi and Battegazzorre (2018) employed a typology formulated by Van Leeuwen (2007; see also Vaara 2014) that differentiates among four legitimation strategies. These strategies can be present separately or in combination, and consist in: 1) Authorization; 2) Moral evaluation; 3) Rationalization; 4) Mythopoiesis.

The conception of legitimacy that the speaker endorses undoubtedly affects how s/he shapes his/her discursive strategies. In particular, in this case, it is possible to identify a relation among the three conceptions of the EU's legitimacy present in the literature and the four discursive legitimation strategies listed by Van Leeuwen. While the prevalence of references to goals and effects, which indicates *legitimation through rationalization*, may reveal an output-based conception of legitimacy, the prevalence of references to (democratic) rules and procedures, which indicates a case of *legitimation through authorization*, may be seen in connection to an input-based conception of the EU's legitimacy. Moreover, an extensive reference to moral values – which characterizes *legitimation through moral evaluation* – and the presence of mythopoetic elements may denote an understanding of legitimacy of a substantial, Weberian kind (Cerutti 2008: 10; Schmidt 2013:11).

The investigation of the discursive legitimation strategies in the SOTEU speeches proposed by Pansardi and Battegazzorre (2018) consists in a qualitative content analysis of the evaluative aspects of a speech, which includes: "assignment of categories to text as qualitative step, working through many text passages and analysis of frequencies of categories as quantitative step" (Mayring, 2014: 10). In practice, the method consists in the manual coding of the evaluative content of speech transcripts in light of a classificatory grid.[215] The grid – the coding scheme – was built on the basis of a deductive and inductive process. General distinctions derived from overall accepted categories in the study of politics. The distinction among the political (at the EU level and at the Member State level), economic, social and intellectual spheres was based on the Weberian classification of the value-spheres, understood as the *loci* of value rationalization in which individual action is shaped through the capacity to *take a position* on the world and ascribe a *meaning* to it (Weber 1949; Oakes 2003). Specific categories resulted from the analysis and identification of significant recurrent elements in the seven Speeches on the State of the Union and a number of

215 Texts were coded with NVivo 10. The work of the two independent coders showed a good degree of inter-coder reliability, with a Kappa coefficient ranging from 0.76 to 0.94 for the various symbols categories.

other speeches by the Presidents of the Commission. Definition of the categories and sub-categories and the allocation of ‚symbols' (the unit of analysis) among the relevant categories allows for quantification and overall comparison of the content of the speeches.

To investigate the understandings of legitimacy present in the seven SOTEU speeches delivered between 2010 and 2017[216], Pansardi and Battegazzorre (2018) rely on the frequency[217] of specific categories and sub-categories of symbols in the total of symbols registered in the single speech. The choice of the relevant symbolic categories is guided by the intent to operationalize Van Leeuwen's (2007) typology of discursive legitimation strategies in light of the three different conceptions of legitimacy (*input*; *output*; *substantial*) expounded in the previous section. The categories identified as relevant to the study of legitimacy are: 1) values; 2) goals; 3) sources of legitimacy; 4) interpretations of the political community (Pansardi and Battegazzorre 2018: 9).

The empirical study of the frequency of symbols conducted by Pansardi and Battegazzorre (2018) allows us to identify clear differences, in terms of symbolic content, between the speeches by Barroso and the more recent speeches delivered by Juncker. Barroso's speeches make predominant reference to *economic goals* and *values*, while devoting little attention to symbols concerning the sources of the EU's legitimacy – privileging, in this case, the reference to 'Treaties' – and providing an interpretation of the *political community as a beneficiary* of the EU's decisions and of the European integration process. Referring to the typology of discursive legitimation strategies identified by Van Leeuwen (2007), Barroso's speeches comprise a discursive strategy mainly directed at legitimation through *rationalization* given by the predominance of symbols belonging in the 'goals' category, especially 'economic goals'. The legitimacy of the EU is asserted through 'rationalist' and 'utilitarianist' arguments (Thelier 2005: 22), and it is attested insofar as the EU produces beneficial outcomes *for* the 'political community'.

Barroso's speeches, moreover, present elements of *authorization*. The kind of authority evoked, however, is predominantly the authority of economic expertise (Reyes, 2011) supported by the high frequency of references to economic values.

What emerges from Barroso's choices in terms of discursive legitimation strategy is an underlying *output* conception of legitimacy (Scharpf 1999; Schmidt 2013): the community is not the source of power *per se*; it is, by contrast, the ultimate recipient and judge of the activities and decisions of the EU. In this perspective EU authority and procedures are then motivated and justified in light of their capacity to make 'good decisions' for EU citizens. In Barroso's speeches, the legitimazing principle is accordingly the classic, functionalist interpretation of the 'rationality' of the EU's decisions in terms of, mainly, economic outputs, supported by reference to merely economic principles and values – as well as by a non-conflictual, technocratic language (Olsson and Hammargård 2016: 552-3): Barroso's attempt to reclaim legitimacy for the EU in times of crises thus goes in the direction of the depoliticization of current conflicts in light of the rationality of EU decisions.

The findings for the SOTEU speeches delivered by Juncker allow us to depict a quite different picture. Juncker's speeches devote little attention to the economic sphere in general, and to symbols concerning economic goals and values in particular. Juncker's reference to values is made predominantly in terms of *ethical, social* and, especially in the last two speeches, *political values*. Symbols concerning the EU political sphere are overall predominant, and particular reference is made to symbols concerning the *sources of legitimacy*. Despite differences between Juncker's three

216 Speeches were downloaded from the European Commission Press Release Database: http://europa.eu/rapid/search.htm

217 The relative frequency of a category is obtained in relation to the entire symbolic content of the speech. Symbols that do not pertain to any of the categories relevant to this investigation are included in the category 'Other'.

SOTEU speeches – concerning mainly the 2016 speech, where was registered a slight increase in the reference to economic values and goals and a decrease in the reference to the sources of legitimacy – the overall similarities hold in the comparison with Barroso's speeches.

The discursive legitimation strategies employed by Juncker can thus be described as rather different from those used by Barroso. Firstly, the frequency of symbols of the sub-categories 'political community' and 'popular sovereignty' as sources of legitimacy indicates a legitimation through *authorization* in terms of (democratic) rules and procedures, where authority is understood in terms of the classic repertoire of democratic legitimacy. The underlying conception of legitimacy that shapes Juncker's discursive strategies thus seems to consist in an *input*-based understanding of legitimacy whereby citizens are not only the judges of, but also the prime actors in, the decision-making process.

Secondly, the frequent reference to symbols in the 'values' category, in particular the reference to values pertaining to the ethical sphere - almost absent in Barroso's speeches - highlights the presence of a strategy of legitimation through *moral evaluation*, where actions and decisions are explained and justified by reference to a commonly shared set of values. Lastly, Juncker's speeches include also elements of legitimation through *mythopoesis*, supported by the high rate of symbols concerning the 'common historical experience and memory' (especially in the SOTEU 2015) and by the inclusion of actual mythopoetic narratives. The following passage from Juncker's 2015 speech exemplifies this point:

Pushing back boats from piers, setting fire to refugee camps, or turning a blind eye to poor and helpless people: that is not Europe. Europe is the baker in Kos who gives away his bread to hungry and weary souls. Europe is the students in Munich and in Passau who bring clothes for the new arrivals at the train station. That's those at the Munich rail station applauding and welcoming refugees. The Europe I want to live in is illustrated by those who are helping. The Europe I don't want to live in is a Europe refusing those who are in need (Juncker 2015: 6).

The use of these two latter discursive strategies seems intended to provide and reinforce thicker symbols of identification and narratives for legitimizing the EU, and upholding, as well as reproducing, a *substantial* conception of legitimacy of the Weberian kind described by Cerutti (2008) as based on collective identification and shared beliefs.

On the basis of these findings, we can thus highlight a clear shift in the overall legitimizing strategies of the two Presidents. Whereas Barroso's speeches are designed to depoliticize conflicts and reproduce the commonly held assumption of the EU as "a polity based on rationality and functional interests, not emotional appeals" (Della Sala 2010: 2), Juncker's speeches are 'more political' and characterized by 'a marked assertiveness' and 'bold proposals' (Dinan 2016: 103) associated with stronger legitimacy claims.

2. The study of the Presidents' of the Commission charismatic language (2010-2017)

While the discursive legitimation strategies chosen by the Presidents (together with their speechwriters and presumably attesting the line of the Commission as a whole) in the particular occasion of the State on the Union Addresses tell us part of the story of their attempts to have a public political impact on national governments' and EU citizens' attitudes on the EU project as whole and on the role of the Commission in particular, the assessment of the overall tone of the Presidents' communication is fundamental in understanding the styles of leadership that the Presidents reclaim for themselves. In particular, in the investigation of leadership styles, whether the language used can be claimed to proximate an idealtype of charismatic, politicized language, or whether it should be deemed to consist in a neutral, descriptive and technical language devoid of emotional appeals, may allow to provide a fuller picture of the leadership role that the President choses for himself, and accordingly, allows us to test, for one, whether the ‚more political' role that Juncker claimed for himself is attested by the tone of his overall communication.

While charisma, in the classical Weberian interpretation, consists in exceptional qualities of the leader, which manifest themselves especially in his/her action, language represents a fundamental aspect of charisma, because only through language the charismatic actor is able to attest and reclaim its leadership role. It is primarily through communication that charismatic leaders represent themselves as such, and transmit their values and vision to followers (Tucker 1968; Antonakis et al. 2011; 2016).

Shamir, House and Arthur (Shamir et al. 1993; 1994), have identified seven principal traits that distinguish charismatic language:

1. More references to collective history and to the continuity between the past and the present;

2. More references to the collective and to collective identity, and fewer references to individual self-interest;

3. More positive references to followers' worth and efficacy as individuals and as a collective;

4. More references to the leader's similarity to followers and identification with followers;

5. More references to values and moral justifications, and fewer references to tangible outcomes and instrumental justifications;

6. More references to distal goals and the distant future, and fewer references to proximal goals and the near future; and

7. More references to hope and faith (Shamir et al. 1994: 29).

The studies by Shamir have been the basis for a number of empirical analyses of charismatic leadership in times of crisis (e.g. Bligh et al. 2004; Bligh & Hess 2007; Davis & Gardner 2012; Bastardoz et al. 2015). Recently, this theoretical framework has also been applied to the case of the euro crisis to study the charismatic rhetoric and leadership of the President of the European Commission (Olsson and Hammargård 2016). The study of Olsson and Hammargård, which provides an analysis of all the speeches delivered by Barroso between 2006 and 2011, offers some unexpected result. In contrast with the common theoretical assumption of a positive effect of crises on charismatic leadership, they found that in the cases under investigation the language of President Barroso became less charismatic in the periods of manifest exacerbation of the Eurozone crises. This finding is even more significant if read together with the study of Tortola and Pansardi (2018), which, for the same period of time, attests an increase in the charismatic language of another central player in the dealing of the Eurozone crisis, namely the President of the European Central Bank (at the time, Jean Claude Trichet).

2.1 Methods and research design

While the manual coding of the SOTEU speeches allows for the investigation of the discursive legitimation strategies used by the two Presidents, the study of the overall degree of charisma of the Presidents' communication relies on a computer-assisted analysis of all speeches delivered between 2010 and 2017. Accordingly, I conducted an analysis of the entire corpus of speeches from the inception the second Barroso Commission on 9th February 2010 to 31 December 2017.[218] The corpus consists of 783 speeches, of which 709 delivered by President Barroso, and 74 by President Juncker. Considering that the time spans under investigation for the two Presidents are not extremely dissimilar - around four and half years for President Barroso, and a little more than three

218 Speeches were downloaded from the European Commission Press Release Database: http://europa.eu/rapid/search.htm

years for President Juncker -, the difference in the number of speeches is quite surprising (please note that a consistent number of speeches by Juncker were excluded from this investigation - around 60 - because they were delivered in a language different from English, mostly in French or in a mix of French, German and English; yet, this exclusion does not account for this extreme difference in number).

To analyze the texts I have relied on the use of the DICTION 7 software (Hart 2001). Created specifically to analyze the tone of political discourse, in speeches and other types of texts, DICTION codes text on 31 pre-defined variables using in-built dictionaries and assigning scores reflecting the presence and weight of dictionary terms.

Relying on a well-established method (Bligh et al. 2004; Bligh & Robinson 2010; Davis & Gardner 2012; Bastardoz et al. 2015; Olsson & Hammargård 2016; Tortola and Pansardi 2018), I have analyzed the corpus of speeches by combining DICTION variables into seven composite constructs, building on the linguistic characteristics of charisma listed in the previous section. Table 2 summarizes the seven constructs and the corresponding formulas of DICTION variables, along with sample words for each variable.

Table 2. The seven charismatic constructs and operationalization in DICTION 7 (Tortola and Pansardi 2018)

Construct	DICTION 7 variables	Sample terms
Collective focus: charismatic leaders show a collective orientation and describe their actions and goals as directed towards common achievements and interests.	Collectives	Assembly, cabinet, humanity, mankind, nation.
	+ People references	Crowd, residents, constituencies, majority, citizenry, population
	- Self-reference	I, I'd, I'll, I'm, I've, me, mine, my, myself, race, union
Temporal orientation: charismatic leaders use more temporal references and tend to highlight continuity between the past and the present.	Present concern	Become, care, desire, make, need, request, take
	+ Past concern	Became, cared, desired, made, needed, requested, took, wanted want
Follower's worth: charismatic leaders highlight the positive aspects of the followers and reinforce their sense of awareness vis-à-vis the achievement of collective goals (collective self-efficacy).	Praise	Admirable, brave, delightful, intelligent, kind, lovely, respected
	+ Inspiration	Ambition, devotion, ideals, leadership, merit, optimism, promise, reassurance
	+ Satisfaction	Comfort, cherish, delight, fascinate, gratify, laugh, love, pleasure, rejoice
Similarity to followers: charismatic leaders highlight their own similarity to followers by describing themselves as "one of them".	Levelling	Anybody, everybody, fully, obvious, permanent, totally, unquestionably
	+ Familiarity	About, between, for, on, past, than, who, with
	+ Human interest	Children, family, friends, parents, relatives, widows, yours, charity, blessing, eternal, faith, hope, mercy
Tangibility: charismatic leaders devote less attention to concrete and short terms goals, and are more prone to discuss their expectations and goals in abstract and general terms.	Concreteness	Animal, baseball, cancer, factory, household, movie, school, silk, sugar
	+ Insistence	Score calculated on the basis of repetition of key terms.
	- Variety	Score calculated by dividing the number of different words in a passage by the total words

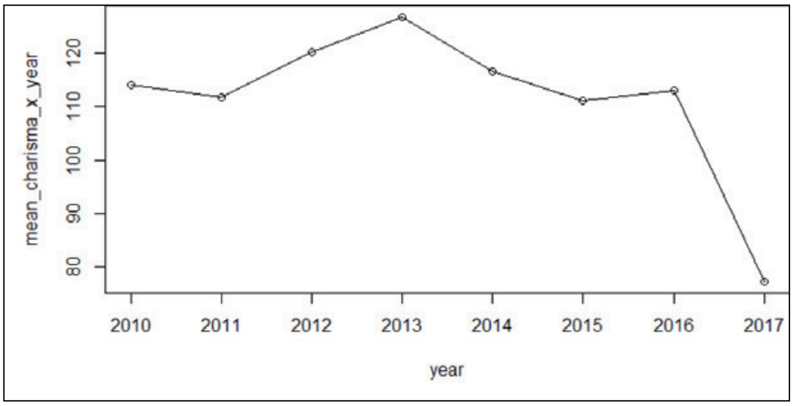
Action; charismatic leaders use an action-oriented language in order to mobilize followers and describe themselves as "proactive".	Aggression	Attack, challenge, combat, dominate, furious, hurt, kill, oppose, preempt
	+ Accomplishment	Achieve, aspire, create, finish, motivate, pursuit, resolution, succeed
	- Passivity	Accept, acquiesce, complacent, disinterested, hesitate, lackadaisical
	- Ambivalence	Blur, confound, hesitate, puzzle, quandary, vacillate, wonder
Adversity: charismatic leaders describe the situation as intolerable with the aim of supporting the proposed alternative "visionary future" and moving to action.	Blame	Contemptible, desperate, guilty, incompetent, mediocre, rash, senile
	+ Hardship	Conflict, crisis, death, fear, insecurity, loss, outrage, sorrow, tension
	+ Denial	Didn't, hadn't, never, wasn't, wouldn't

2.2 Findings

The next step in answering the research question about an increase in the ‚politicization' of Juncker's communication in comparison to Barroso's is to analyze the results obtained after running DICTION 7 on the whole corpus of the Presidents of the Commission speeches between 2010 and 2017. The charismatic constructs presented in Table 2 are aggregated in a single indicator of charismatic rhetoric, by subtracting the value of *tangibility* from the sum of the six remaining constructs.[219] Figure 2 presents a first overview of the charismatic content of the corpus under exam by plotting the year-by-year mean value of the speeches' aggregate indicator of charisma. A first visual inspection is not very telling: while two peaks can be immediately detected (a high peak in 2013 and a low peak in 2017), the remaining years under investigation present a degree of charisma of the Presidents' speeches that seems overall constant, and accordingly not affected by the change in the occupant of the presidency. Overall, however, this first investigation does not seem to depict the increase in charismatic rhetoric with the passage from Barroso to Juncker that we were expecting in light of Juncker's own assumption of a ‚more political' interpretation of his role as President of the Commission, nor to replicate the findings of the qualitative analysis of the SOTEU speeches.

219 The aggregation formula follows Bligh et al. (2004: 225).

Figure 2. Charisma indicator mean per year



To assess the statistical significance of a change in charismatic rhetoric, so as to establish whether an actual variation occur between the rhetorical styles of the two Presidents, I follow the literature on charismatic rhetoric (e.g. Bligh et al. 2004; Bligh et al. 2010; Davis & Gardner 2012; Schroedel et al. 2013; Olsson & Hammargård 2016, Tortola and Pansardi 2018), and rely on a multivariate analyses of co-variance (MANCOVA), a technique for testing the significance of mean differences in a dependent variable of interest (in our case charismatic language) across samples, while also controlling for a number of factors (covariates) that might be related to that variable. In the absence of statistical significance, the null hypothesis that the underlying populations are the same, and that any increase is due to sheer chance, cannot be safely discarded.

I accordingly run a one-way multivariate analysis of covariance (MANCOVA) comparing the measure of the speeches seven charismatic constructs taken individually (the dependent variables) for the two Presidents (the independent variable), including the total number of words in each speech as a covariate, to control for speech length. The multivariate test shows a significant difference between the two Presidents' overall charismatic rhetoric: Wilks's Lambda = 0.941, F (7, 774) = 6.976, p < 0.001. However, the direction of the difference - namely, which President scores the best in terms of overall charisma - is more difficult to assess. As Table 3 shows, the test determined that four out of the seven constructs present statistically significant differences for the two Presidents: *Followers' worth*, *Similarity to followers, Action* and *Adversity.* However, while President Barroso scores higher on the first three variables, Juncker scores higher on the last one, namely *Adversity*. Moreover, if we look at the other variables that do not show a statistically significant variation, we see that Juncker scores higher (and lower, in the case of *Tangibility*, which is expected to decrease to attest charismatic rhetoric) in two out of three.

Table 3. The charismatic rhetoric of the two Presidents. Results by single construct

	Barroso MEAN	Standard error	Juncker MEAN	Standard error	Univariate F (1, 780)	Sign.	Partial eta squared
Collective Focus	1.015	.223	1.484	.835	.245ns	.621	.000
Temporal Orientation	13.614	.181	12.540	.532	3.224ns	.073	.004
Follower's Worth	22.759	.322	17.571	1.076	19.708***	.000	.025
Similarity to Followers	163.626	.763	157.291	1.871	7.324**	.007	.009
Tangibility	95.145	2.133	89.455	6.745	.215	.643	.000
Action	5.126	.330	0.705	1.391	13.522***	.000	.017
Adversity	6.690	.167	8.461	.616	5.950*	.015	.008

*Notes: Barroso N = 709; Juncker N = 74. *p < 0.05; **p < 0.01; ***p < 0.001; ns = non-signficant value.*

The multivariate test, as a result, does not allow us to obtain straightforward answer to the question of which of the two Presidents make use of a more charismatic rhetoric. Nonetheless, if we take into account only the statistically significant results, we should consider that, in contrasts to our expectations, the tone of Juncker's speeches appear to be less charismatic than the one found in the speeches by Barroso, leaving us with a finding that goes against the results obtained by performing the qualitative analysis of the SOTEU speeches.

3. Discussion and conclusion

By relying on the qualitative analysis of the SOTEU speeches reported in the first part of this paper, we can highlight a radical change in the two Presidents' interpretation of their role as key actors in the promotion and support of the project of European integration. On the specific occasion of the delivery of the SOTEU speech, the two Presidents did not only rely on extremely different strategies for top-down legitimation, but also adopted different vision of the nature of the legitimacy of the EU. The growing attention reserved by the European community to the SOTEU speeches may have the result of rendering these speeches the paramount opportunity for expressing rhetorical strategy, charisma, and vision, and accordingly, to concentrate the rhetorical efforts of the President in that particular event.

A possible explanation of the differences between Barroso's and Juncker's SOTEU speeches may come from taking seriously into account the role of the *Spitzencadidaten* system in changing the President's perspective about the legitimacy and nature of his/her own mandate. If, on the one hand, the content and the discursive strategies employed in the speeches highlight the role of agency in attesting Juncker's willingness to present himself and communicate as a 'more political' President than Barroso – the latter being often criticized for a lack of political assertiveness (Dinan 2016: 102) – on the other hand, the differences in the communication style of the two Presidents may be interpreted as also related to changes in the political and institutional context. While agency is certainly central in the selection of the discursive strategies, Pansardi and Battegazzorre (2018) highlight how the introduction of the *Spitzencandidaten* system has been fundamental in providing the two Presidents with a different discursive opportunity structure.

Firstly, the different procedure of appointment has undoubtedly endowed the two Presidents with a different symbolic repertoire. As suggested by Christiansen, the introduction of the *Spitzencandidaten* procedure "provided a powerful symbolic change" (2016: 993) – that may also be interpreted, following Gronau and Schmidke (2016), as an institutional strategy for legitimation – in the nature of the Presidency. While the appointment of Barroso and his predecessors was the result of intergovernmental negotiations and merely 'approved' by the European Parliament, the new appointment procedure allows Juncker to claim a sort of *electoral* mandate, and, as a consequence, offers him the opportunity to resort more directly to the symbolic repertoire of democratic legitimacy. Secondly, the nature itself of the *Spitzencandidaten* system has allowed Juncker to claim a sort *personal* mandate (Kassim 2017; see also Dinan 2016), offering him the opportunity to claim more legitimacy for his role and enabling a stronger leadership. As Christiansen points out: "The President of the Commission, less encumbered than his predecessor by the need for support and approval from the majority of member states, has been able to assume a leadership role unseen since the days of Jacques Delors" (2016: 1007).

Accordingly, the new opportunity structure created by the introduction of the *Spitzencandidaten* system has allowed Juncker to shape his discursive strategies in a way just precluded to his predecessor. 'Building' (Dinan 2016: 103) on his new appointment procedure, Juncker has been able to include in his speeches discursive strategies directed at the legitimation of his own role and of the EU's policy proposals in terms of democratic authorization, thus offering an overall interpretation of the EU's legitimacy in terms of input. Moreover, in light of his stronger leadership, Juncker has been able to reinforce his legitimacy claims by including discursive strategies of top-down legitimation through moral evaluation and mythopoesis, overall contributing to an interpretation of the EU as a 'community of values' in terms of a substantial, Weberian, conception of the legitimacy of the EU (Pansardi and Battegazzorre 2018).

However, the quantitative analysis of the tone of the language of the two Presidents depicts a quite different picture. Not only the tone of Juncker's speeches is not more charismatic then the one found in Barroso, but can - with a few precautions - be described as overall less charismatic. This accounts for two possible explanations. A first explanation may assume the peculiar nature of the State of the Union Addresses as the reason why Juncker concentrates his efforts - in terms of rhetorical language and top-down discursive legitimation - on these specific speeches. To support this explanation, there is also the great and unexpected difference in the overall number of speeches of the two Presidents in the period under scrutiny. Overall, it may appear that Juncker prefers to contract the number of occasions in which he openly speaks to the public, and - with the exclusion of the SOTEU - to reserve his open communication to more ‚coordinative' and less ‚communicative' speeches. A second, not alternative explanation, refers to the new opportunity structure offered by the institution of the *Spitzencaditaten* system: differently from Barroso, Junckers' may not see the need to negotiate the legitimacy of its own role in each single occasion, and accordingly, not only ‚speaks less', but when he does, he goes to the heart of the matter in a more ‚direct' and less ‚emotional' language.

With regard to the overall research question guiding this analysis, we have to conclude that, at least in terms of the analysis of language and communication, we cannot describe Juncker as ‚more political' than Barroso. Rather, we should see their use of language as strongly affected by the institutional changes introduced with the *Spitzencaditaten* system which also affects the way in which language is politicized.

References

Antonakis, J., N. Bastardoz, P. Jacquart & B. Shamir (2016). Charisma: An ill-defined and ill-measured gift. *Annual Review of Organizational Psychology and Organizational Behavior* 3: 293-319.

Bauer, M.W. and Becker, S. 2016. Absolute Gains are Still Gains: Why the European Commission is a Winner of the Crisis, and Unexpectedly So. A rejoinder to Eugénia da Conceição-Heldt. *Journal of European Integration*, 38(1): 101–6.

Bligh, M. C., J.C. Kohles & J.R. Meindl (2004). Charisma under crisis: Presidential leadership, rhetoric, and media responses before and after the September 11th terrorist attacks. *The Leadership Quarterly* 15(2): 211-39.

Bligh, M. C. & G. D. Hess (2007). The power of leading subtly: Alan Greenspan, rhetorical leadership, and monetary policy. *The Leadership Quarterly* 18(2): 87-104.

Bligh, M., J. Merolla, J.R. Schroedel, and R. Gonzalez (2010). Finding her voice: Hillary Clinton's rhetoric in the 2008 presidential campaign. *Women's Studies* 39(8): 823–50.

Bligh, M. C. & J. L. Robinson (2010). Was Gandhi "charismatic"? Exploring the rhetorical leadership of Mahatma Gandhi. *The Leadership Quarterly* 21(5): 844-55.

Börzel T. 2016. From EU Governance of Crisis to Crisis in EU Governance. Regulatory Failure, Redistributive Conflict, and Eurosceptic Publics. *Journal of Common Market Studies.* 54 (S1): 8-23.

Cerutti F. 2008. Why political identity and legitimacy matter in the European Union. In Cerutti F. and S. Lucarelli (eds), *The Search for a European Identity: Values, Policies and Legitimacy of the European Union*. London: Routledge.

Christiansen, T. (2016). After the Spitzenkandidaten - Fundamental Change in the EU's Political System? *West European Politics*, *39*(5), 992-1010.

Della Sala, V. 2010. Political Myth, Mythology and the European Union. *Journal of Common Market Studies* 48(1): 1-19.

Dinan, D. 2016. Governance and Institutions: A More Political Commission. *Journal of Common Market Studies* 54 (Annual Review): 101–116.

Fabbrini S. 2015. *Which European Union? Europe after the Euro Crisis.* Cambridge: Cambridge University Press.

Gronau J., Schmidtke H. 2016. The quest for legitimacy in world politics – international institutions' legitimation strategies. *Review of International Studies* 42 (3): 535-557.

Hansen, L., Williams, M.C.. 1999. The Myths of Europe: Legitimacy, Community and the "Crisis" of the EU. *Journal of Common Market Studies* 37(2): 233–249.

Hart, R. P. (2001). Redeveloping DICTION: Theoretical Considerations. In M. West (ed.) *Theory, Method and Practice of Computer Content Analysis.* New York: Ablex.

Hurrelman A. 2016. Empirical legitimation analysis in International Relations: How to learn from the insights – and avoid the mistakes – of research in EU Studies. *Contemporary Politics* (forthcoming).

Kassim H. 2017. What's new? A first appraisal of the Juncker Commission. *European Political Science* 16 (1): 14–33.

Kassim, H., Connolly, S., Dehousse, R., Rozenberg, O., Benjaballah, S. 2017. Managing the house: The Presidency, agenda control and policy activism in the European Commission. *Journal of European Public Policy* 24 (5): 653-674.

Mayring, P. (2014) *Qualitative content analysis. Theoretical foundation, basic procedures and software solution.* Social Science Open Access Repository SSOAR, URN: http://nbn-resolving.de/urn:nbn:de:0168-ssoar-395173 .

Oakes G. 2003. Max Weber on Value Rationality and Value Spheres. *Journal of Classical Sociology* 3(1): 27–45.

Olsson E., Hammargård K. 2016. The Rethoric of the President of the European Commission: charismatic leader of neutral mediator?. *Journal of European Public Policy* 23(4): 550-570.

Pansardi P., Battegazzorre F. 2018. The discursive legitimation strategies of the President of the Commission: a qualitative content analysis of the State of the Union Addresses (SOTEU), *Journal of European Integration* (First published online: doi.org/10.1080/07036337.2018.1482286).

Reyes, A. 2011. Strategies of legitimation in political discourse: From words to action. *Discourse and Society* 22(6): 781-807.

Shamir, B., M. B. Arthur & R. J. House (1994). The rhetoric of charismatic leadership: A theoretical extension, a case study, and implications for research. *The Leadership Quarterly* 5(1): 25-42.

Shamir, B., R. J. House & M. B. Arthur (1993). The motivational effects of charismatic leadership: A self-concept based theory. *Organization Science* 4(4): 577-94.

Schmidt, V.A. 2013. Democracy and Legitimacy in the European Union Revisited: Input, Output and "Throughput". *Political Studies* 61(1): 2–22.

Theiler, T. 2005. *Political Symbolism and European Integration*. Manchester: Manchester University Press.

Tortola P.D., Pansardi P. 2018. The charismatic leadership of the European Central Bank presidency. A language-based analysis, *European Journal of Political Research* (First published online: doi/10.1111/1475-6765.12272).

Tucker, R. C. 1968. The theory of charismatic leadership. *Daedalus*: 731-56.

Verdun, A. 2017. Political leadership of the European Central Bank. *Journal of European Integration* 39(2): 207-21.

Vaara, E. 2014. Struggles over legitimacy in the Eurozone crisis: Discursive legitimation strategies and their ideological underpinnings. *Discourse & Society* 25(4) 500–518.

Van Leeuwen, T. 2007. Legitimation in discourse and communication. *Discourse and Communication* 1(1): 83-118.

Weber, M. 1949a. "Objectivity" in Social Science and Social Policy. In Shils E.A. and Finch H.A. (eds). *The Methodology of the Social Sciences*. New York: Free Press.

E THE DEMISE OF LAW

THE EU AS "HONEST BROKER"? GERMAN AND ITALIAN PERSPECTIVES ON AN ADMINSTRATIVE BODY

Anna Katharina Mangold[220*]

Goethe University, Frankfurt am Main

From its very beginning in the European Community of Coal and Steel (ECSC), the leading organ of European integration, that was later to become the EU Commission, was designed as a merely bureaucratic, a-political agency, and an "honest broker" between the Member States. From these early days, this has been a blunt lie about the nature and inner workings of the then High Authority of the ECSC and later the European Commission. In this paper, I argue, that nothing has changed very much over time. In fact, I argue that we need to get rid of the understanding that there is such a thing as a "neutral", "merely bureaucratic", European Commission.

Two recent scandals surrounding the Juncker Commission may shed some light on the current state of affairs in the EU Commission: the promotion of Martin Selmayr as Secretary-General of the Commission, and the interview of Commissioner Günter Oettinger on the Italian elections. Drawing on these two recent scandals within the EU Commission, I try to show how a more political understanding of the role of the EU Commission could help to bring about a more nuanced and politicised vision of European integration. Such a vision is necessary to make room for political debates about alternatives – as the bureaucratic and technocratic conception of the EU Commission still inhibits debate about political alternatives.

1. Historical origins of the Commission

When the British considered joining the European Community of Coal and Steel (ECSC) that French Foreign Minister Robert Schumann had suggested be built among European nation states, Prime Minister Clement Attlee explained on the 27 June 1950 in the House of Commons:

> "We on this side are not prepared to accept the principle that the most vital economic forces of this country should be handed over to an authority that is *utterly undemocratic* and is *responsible to nobody*."[221]

a. The High Authority of the ECSC

It is surely true that the High Authority of the ECSC can be considered the truly supranational element of the first Treaty on European Integration – the very term "supranational" was introduced to describe both the functioning of the High Authority and the competences of its

220* This paper is part of an ongoing project trying to trace the origins of current understandings and theoretical conceptualisations of the organs and institutions of the European Union. In a previous paper, I looked into the exclusive right to initiate legislation conferred upon the EU Commission which the European Court of Justice has turned into a veritable veto position in the informal Trilogue legislative mechanism. I now want to trace the historical origins of the Commission as an institution of the EU and its theoretical conception in the Treaties, in political life, and in European Studies. I am very grateful for all suggestions and hints (mangold@jur.uni-frankfurt.de).

221 Prime Minister Clement Attlee replying to MP Winston Churchill in a debate about the Schumann plan, Hansard, 27 June 1950, p. 2169 (Italics added), available at: https://api.parliament.uk/historic-hansard/commons/1950/jun/27/schuman-plan-1 . The British had intentionally been left out of this plan from the very beginning, as can be gathered from the fact that the British Foreign Minister, Ernest Bevin, was only informed about Schumann's proposition on the morning of the very same day that Schumann anounced his plan; see, with further references, A.K Mangold, *Gemeinschaftsrecht und deutsches Recht*, (Tübingen: Mohr Siebeck, 2011), p. 35 fn. 14.

members.[222] Jean Monnet famously envisaged the High Authority as a technocratic administration free from parliamentary and political oversight, and, indeed, any control whatsoever.[223] Thus, Attlee was certainly right in stating that the High Authority was not in any traditional understanding of the term "democratically" elected or responsible.

b. The Commission of the EEC

The Commission of the European Economic Community (EEC) partly was less powerful than the High Authority of the ECSC in that the Treaty of Rome was much broader in its wording and conferred less precisely defined competences to the newly established Commission. Partly, however, the Commission became much more powerful because the Treaty of Rome comprised everything "economic". Over time, the Commission interpreted the term "economic" in a very broad sense so that it came to encompass literally everything from cultural performances to the disposal of waste, from radio broadcasting to the protection of the environment. This approach was to some extent foreseen and envisaged in the Treaty itself.[224] The progressive narrative was bound to lead to a teleological understanding of the competences. Historical research has again and again shown how especially the legal service of the Commission was the driving force behind the ECJ's seminal decisions of the 1960s[225] and also the 1970s.[226] The ECJ could only perform its activist role in European integration because it could rely on the Commission to provide well prepared cases, and in fact test cases that were laboriously drafted to bring about jurisprudence that would allow for enhancing the competences of the Commission.[227]

Despite Attlee's complaints about the ECSC High Authority, no major changes took place in the conception of the Commission in the EEC. The Commission's composition[228] and accountability[229] were not very convincing when pitched against the powers of this institution. The worries deepened over time as the Commission took an activist and teleological approach to interpreting its own competences, which the ECJ backed in nearly all cases.[230]

In the case of the Commission, the "law in the books" and the "law in action"[231] never added

222 Art. 9 paras. 5 and 6 TECSC (1951): "(5) The members of the High Authority shall exercise their functions in complete independence, in the *general interest of the Community*. In the performance of their duties, they shall neither seek nor take instructions from any Government or from any other body. They shall refrain from any action incompatible with the *supranational character* of their functions.
(6) Each Member State undertakes to respect this *supranational character* and not to seek to influence the members of the High Authority in the performance of their tasks." (Italics added.)

223 A. Boerger-de Smedt, "La Cour de Justice dans les négociations du traité de Paris instituant le CECA", (2008) 12 *Journal of European Integration History*, pp. 7-33 (passim, expressly p. 12).

224 Art. 2 TEEC (1957): "It shall be the aim of the Community, by *establishing a Common Market* and *progressively approximating the economic policies of Member States*, to promote throughout the Community a harmonious development of economic activities, a continuous and balanced expansion, an increased stability, an accelerated raising of the standard of living and closer relations between its Member States." (Italics added.)

225 A. Boerger-de Smedt and M. Rasmussen, "The Making of European Law: Exploring the Life and Work of Michel Gaudet", (2017) 57 *American Journal of Legal History*, pp. 51-82.

226 Unpublished paper by Bill Davies and Walter Much presented at the conference of the Max-Planck-Institute for Legal History Frankfurt/Main "Key Biographies in the Legal History of European Union, 1950-1993", 21-22 June 2018 (on file with the author).

227 1960s: It has been argued that *van Gend en Loos* was in fact a test case. 1970s/1980s: The *Defrenne* litigation both gave Art. 157 TEEC (equal pay for men and women) a new and much broader meaning, thus bringing this dorment Treaty provision to life, and provided a new policy field to the Commission, namely establishing non-discrimination in labour relations which in eventually would lead to the far reaching antidiscrimination directives of the early 2000s.

228 Art. 158 TEEC: appointment by the Member States.

229 Art. 160 TEEC: removal of Commissioners from office.

230 The notorious exception was the Tobacco advertisement directive which, in its first version, was not upheld by the ECJ, C-376/98, 5 October 2000, and was accepted only in the second attempt by the Court, ECJ, C-380/03, 12 December 2006.

231 R. Pound, "Law in Books and Law in Action", (1910) 44 *American Law Review*, pp. 12-36.

up. Room for charismatic leadership existed, and it was filled in a memorable way by the famous "Delors Commission" in the 1980s.[232]

c. The Commission of the EU

The same is still true for the Commission of the Lisbon Treaty. Article 17 TEU is a lengthy article which tells law students little about the actual workings of the EU Commission. The number of Commissioners has not been decreased as foreseen in Article 17 para. 4 TEU because the Member States decided to maintain their respective "national" Commissioner.[233] The composition in itself seems paradoxical: according to Article 17 para. 3 TEU, the Commission's term of office is five years and has, thereby, adjusted to the legislative term of the European Parliament (EP). Nonetheless, it is not the EP which has the decisive say in the composition of the Commission, but the European Council, even though Article 17 para. 7 TEU requires that it take "into account the elections to the European Parliament".

The ensuing "*Spitzenkandidaten*" or "Lead/Top Candidates" process was hotly debated in 2014[234] and is far from established as the guiding political principle for the selection of the President of the Commission following the elections to the European Parliament next year (2019).

232 See, e.g., White Paper "Completing the Internal Market", COM(85)310, Brussels, June 1985.

233 European Council Decision 2013/272/EU of 22 May 2013 concerning the number of members of the European Commission, OJ L 165, 18.6.2013, p. 98.

234 See, for example, the debate on Verfassungsblog in April 2014, available at: https://verfassungsblog.de/category/debates/spitzenkandidaten-fuer-die-europawahl, and later in June 2014 between Matthias Kumm (https://verfassungsblog.de/der-europaeische-rat-ist-verpflichtet-juncker-vorzuschlagen) and Kenneth Armstrong (https://verfassungsblog.de/european-council-legal-duty-appoint-jean-claude-juncker).

2. The Promotion of Martin Selmayr as Secretary-General of the EU Commission: Independence from Parliamentary Oversight

The first scandal surrounds the promotion of Martin Selmayr from Chief of Staff to the President of the European Commission, Jean-Claude Juncker, to the position of Secretary-General of the European Commission, the most senior civil servant position in the Commission, and, basically, the right hand of the President of the Commission.[235]

As is well known by now, in a meeting of the EU Commission in early February 2018, Martin Selmayr was first promoted to the position of Vice Secretary-General of the Commission. In the same meeting, the then Secretary-General resigned, to the surprise of everybody except Juncker, who had known that he wanted to resign for some time. Selmayr was appointed Secretary-General. A *pro forma* alternative candidate, later to become Juncker's Chief of Cabinet, withdrew her candidature. Hence, Selmayr was promoted twice within just nine minutes.[236]

Criticism followed suit. Juncker remained adamant and even threatened high-ranking members of his own party, the conservative EPP, with his resignation if Selmayr was forced to step down.[237] Criticism was directed both at the opaque procedure and at the fact that yet another German is now holding a top position in the EU bureaucracy.

235 The history of this position shows that the relationsship between Commission Presidents and secretary-generals was always politically important. Émile Noël and Walter Hallstein had a very trusting relationship. Noël served as secretary-general from 1957 until 1987. Jacques Delors replaced him with the British David Williamson and in doing so tried to involve a possible antagonist in his far reaching project for the Commission.

236 http://www.deutschlandfunk.de/europaparlament-milde-resolution-zum-fall-selmayr.1773.de.html?dram:article_id=415846.

237 https://www.politico.eu/article/martin-selmayr-juncker-goes-i-go/.

There are many questions to be asked about this particular promotion, and indeed the EP asked several, 134 to be precise.[238] However, in the end, the EP could only mildly admonish the Commission for the intransparency of the whole procedure.[239] This partly has to do with the still flawed wording of the Treaty on the European Union. Article 17 para. 8 TEU only enables the EP to ask for the resignation of the Commission "as a body".

The EU Ombuds"man", Emily O'Reilly, re-elected for five years in December 2014, will look further into the affair.[240] Franklin Dehousse, former Justice at the CJEU, predicts that this scandal will haunt both the Commission and the EU as a whole for months, and possibly years, to come.[241]

If we were to consider the position of Secretary-General just as an ordinary civil servant position, then, of course, the procedure employed in promoting Martin Selmayr warrants heavy criticism: for the lack of transparency, the missing advertisement of the position, and the ensuing low number of (alleged) candidates. However, if we think of the Secretary-General as a clearly political position, it becomes self-evident why Juncker would want a loyal follower in this key position.

However, the appointment procedures put Member State interests centre stage, not the political allegiances of the College of Commissioners, which is not a government cabinet in the traditional sense of a national government organisation; rather, Commissioners are chosen according to Member State preferences.

The same is true for positions in the Commission bureaucracy, even – and maybe especially – for high-ranking positions. National quotas still play a decisive role in the promotion of civil servants, albeit informally.[242]

Implicitly, the idea of national belonging apparently has a strong foothold in the conception of both parts of the Commission, the College of Commissioners and the Commission bureaucracy. If Jürgen Habermas argues, for the democratic setting, that the EU bridges Union citizenship, on the one hand, and Member State citizenship, on the other,[243] this may well be criticised for being overly optimistic and in need of being legal implementation.[244] For the organisation of the EU Commission, Member State citizenship is, apparently, still the decisive factor. As long as this remains the case, the Commission will not become a politically independent "government of the EU".

3. The Interview of Commissioner Oettinger on the Italian elections: Italy as Periphery?

In an interview on the 29 May 2018 with *Deutsche Welle*, Budget Commissioner Günter Oettinger was asked about the outcome of the Italian elections of March 2018. The Interview took place at a time, in May, when Italy was still without a government because of the outcome of the election. Oettinger said the following:[245]

> "It is my worry and expectation that the next weeks will show that the markets, that the government bonds, that the economic development of Italy could be so radical that this possibly turns into a signal for voters not to vote for left and right populists.

238 https://www.tagesschau.de/ausland/selmayr-eu-parlament-101.html.

239 http://www.europarl.europa.eu/committees/en/cont/subject-files.html?id=20180326CDT02181.

240 https://www.politico.eu/article/eu-watchdog-ombudsman-emily-oreilly-confirms-martin-selmayr-promotion-probe/.

241 https://verfassungsblog.de/european-council-legal-duty-appoint-jean-claude-juncker/.

242 U. Haltern, *Europarecht I*, 3rd ed. 2017, p. 222 marg. no.479.

243 J. Habermas, *Zur Verfassung Europas: Ein Essay*, (Berlin: Suhrkamp Verlag, 2011), pp. 86 et seq.

244 A.K. Mangold, "Democratic Legitimacy of EU Law. Two Proposals to Strengthen Democracy in the European Union", in: Johan van der Walt and Jeffrey Ellsworth (eds), *Constitutional Sovereignty and Social Solidarity in Europe*, (Baden-Baden-London: Nomos-Bloomsbury, 2015), pp. 165-192.

245 In my account of the events, I follow a report of *Tagesschau*, available at: https://www.tagesschau.de/ausland/oettinger-italien-wirbel-101.html.

… Even now, developments on bond market, the market value of banks, and Italy's economy in general have darkened noticeably and negatively. This has to do with the possible government formation. I can only hope that this will play a role in the election campaign and send a signal not to hand populists on the right and left any responsibility in government."[246]

The interviewing journalist of *Deutsche Welle*, Bernd Riegert, captured this in a short Tweet, which read:

"The markets will teach the Italians to vote for the right thing", #EU commissioner #Oettinger told me [….]."[247]

The now Italian Minister of Economic Development and Labour, Luigi Di Maio, responded on Twitter that Oettinger's allegations were "absurd" and continued:

"These people treat Italy as a summer camp where they can spend their holidays."[248]

Swiftly, on the very same day, the President of the EU Commission, Jean-Claude Juncker, issued a statement implicitly castigating Oettinger for his interview remarks:

"The President of the European Commission, Jean-Claude Juncker, wishes to put on record his conviction that *Italy's fate does not lie in the hands of the financial markets*. Regardless of which political party may be in power, Italy is a founding member of the European Union that has contributed immensely to European integration. President Juncker is convinced that Italy will continue on its European path. The Commission is ready to work with Italy with responsibility and mutual respect. *Italy deserves respect*."[249]

Interestingly and maybe surprisingly, later that same week, in a Q & A Session in Brussels on 31 May 2018, Juncker was cited by the *Guardian*:

"Italians have to take care of the poor regions of Italy. That means more work; less corruption; seriousness."[250]

These events, I argue, show that, even though Italy and Germany were founding members of the ECSC, they are no longer on equal footing when it comes to their current position both in the EU and *vis-à-vis* the EU Commission. Rather, these events highlight a perception in the Commission of the relationship between Germany and Italy as one of "centre and periphery" where Germany is a centre state and Italy a mere peripheral state. It is, I hold, not coincidental that the German Commissioner Oettinger was the one to state bluntly what can be taken to be a general sentiment in the Commission when it comes to Italy.[251] In the Commission, there seems to be an understanding that there are more important and less important Member States. This calls into question whether the Commission can really play the role of an "honest broker" between competing Member States among themselves, and between Member States and the EU. Again, a truly political institution could take political positions openly if the Commission were to be democratically elected and accountable.

246 English translation at https://en.wikipedia.org/wiki/Günther_Oettinger#Intervention_in_Italian_politics. In the original German: "Meine Sorge und meine Erwartung ist, dass die nächsten Wochen zeigen, dass die Märkte, dass die Staatsanleihen, dass die wirtschaftliche Entwicklung Italiens so einschneidend sein könnten, dass dies für die Wähler doch ein mögliches Signal ist, nicht Populisten von links und rechts zu wählen. … Schon jetzt ist die Entwicklung bei den Staatsanleihen, bei dem Marktwert der Banken, beim wirtschaftlichen Verlauf Italiens generell deutlich eingetrübt, negativ. Dies hat mit der möglichen Regierungsbildung zu tun. Ich kann nur hoffen, dass dies im Wahlkampf eine Rolle spielt, im Sinne eines Signals, Populisten von links und rechts nicht in die Regierungsverantwortung zu bringen."

247 The tweet of 29 May 2018 has since been deleted. However, it is still depicted as a screen shot in several tweets, most notably in one of the now Italian Interior Minister Matteo Salvini: https://twitter.com/matteosalvinimi/status/1001437881880272896.

248 My translation. In the original Italian: "Questa gente tratta l'Italia come una colonia estiva dove venire a passare le vacanze", available at: https://twitter.com/luigidimaio/status/1001474208269045760.

249 http://europa.eu/rapid/press-release_STATEMENT-18-3982_en.htm.

250 https://www.theguardian.com/world/2018/may/31/italy-cancelled-league-rallies-signal-political-impasse-may-soon-end.

251 The former Justice at the CJEU rather cruelly characterised Oettinger thus: "Oettinger's explanations are generally dumb and contradictory, but occasionally honest." https://verfassungsblog.de/selmayrs-appointment-why-this-juncker-crisis-is-much-more-dangerous-for-the-eu-commission-than-the-santer-crisis-in-1999.

INTEGRATION-THROUGH-CRISIS AS A DISTINCT INTEGRATIVE MODE: PLACING EXPEDIENCY AHEAD OF DEMOCRACY?

Nicole Scicluna
The University of Hong Kong

Abstract

Integration-through-crisis has affected EMU governance in myriad ways. This paper focuses on two trends, both of which have negative implications for democratic legitimacy in the EU and its member states. Firstly, the crisis has led to an increased reliance on non-majoritarian modes of policy-making, at the expense of democratically accountable institutions and processes. Secondly, the crisis has led to a new emphasis on coercive enforcement in EMU, at the expense of the voluntary cooperation that previously characterised (and sustained) the EU as a community of law.

The ECB is implicated in both of these trends. In relation to the first, while the ECB was already unusually independent - even by the standards of central banks - this could be justified, prior to the crisis, by the specificity, technicality and low salience of its monetary policy mandate. However, the crisis has resulted in both the politicisation of the Bank's mandate and its *de facto* expansion, in ways that render its insulation from democratic politics highly problematic. Indeed, it is made all the more problematic by the ECB's involvement in the second trend; the coercive turn in EMU governance. In this connection, the ECB, in its role as provider of liquidity to eurozone banks, has been instrumental in pushing debtor states towards acceptance of harsh austerity policies.

Thus, the ECB's (over-)empowerment may be viewed as a synecdoche of a wider problem: The EU's tendency to resort to technocratic governance in the face of challenges that require political contestation mediated by democratically accountable institutions. In the absence of opportunities for open contestation, EU emergency governance oscillates between moments of heightened politicisation, in which *ad hoc* decisions are justified as necessary, and the (sometimes coercive) appeal to the depoliticised rule of rules.

Introduction

One of the many consequences of the euro crisis, which began in 2010, has been the politicisation of policy areas and decision making processes in which most Europeans previously had little interest - including the decisions and policies of the European Central Bank (ECB). However, it has not lead to any meaningful democratisation of monetary policy making, nor of any other aspect of the crisis response. On the contrary, the regulatory space in which the ECB operates has expanded during the crisis years. This expansion was driven by the Bank itself, which, for a variety of reasons, seized the initiative at the height of the crisis, including by taking decisions that have redefined what constitutes a monetary policy measure.

Moreover, the euro crisis has revealed deficiencies and pathologies in EU governance that go far beyond the intricacies of monetary policy making. In short, I argue that the EU has moved from a mode of governance centred on law as agent and object (integration-through-law, ITL), to one predicated on expediency (integration-through-crisis, ITC). I use the ECB as a point of departure to illustrate that transformation. How and why did a highly independent, deliberately-insulated and narrowly-mandated body become such a powerful political actor? The answers reveal shortcomings in the EU's institutional architecture and political culture. The former include the difficulty of formally amending the EU's treaties, and the incomplete construction of EMU as a monetary union without a fiscal counterpart. These, in turn, hint at the latter: National and EU leaders are reluctant to attempt treaty reform because doing so would require referendums in at least some member states, the outcomes of which would be highly uncertain. Similarly, there are major disagreements among national governments about how best to proceed - e.g. on whether the eurozone ought to have its own budgetary resources, or on the creation of a eurozone finance minister.

The paper is organised as follows. The first section discusses ITC as a distinct integrative mode, contrasting it with ITL. In the second section, I continue the elaboration of ITC via a focus on the role of the ECB as a regulatory body that is both very powerful and highly insulated from majoritarian democracy. In particular, the ECB has come to symbolise two key characteristics of ITC: Firstly, the exacerbation of the EU's pre-existing tendency to concentrate power in the hands of executives and non-majoritarian bodies. Secondly, the belated and misguided turn to coercive enforcement of EMU's rules. These tendencies are discussed in the third and fourth sections, respectively.

Again, what makes the crisis-driven empowerment of the ECB so significant is what it tells us about more serious deficiencies of EU governance, which leaves insufficient space for the kind of open political contestation that is necessary for democratically legitimate policy-making. It is telling, for example, that the ECB's bold redefinition of its own mandate was legally ratified by the Court of Justice of the European Union (CJEU), rather than through any legislative process. Herein lies the connection between ITL and ITC: Both prioritise non-majoritarian modes of policy making in the advancement European integration, but with an emphasis on different types of 'experts' (e.g. judges as opposed to bankers). Thus, the concluding remarks reflect on the implications of ITC for the EU's democratic legitimacy.

From integration-through-law to integration-through-crisis

ITL describes the dynamic whereby courts drive the integration process forward through their dissemination of EC/EU legal norms. The Court of Justice created the legal framework for this dissemination through its groundbreaking articulation of the principles of direct effect and EC legal supremacy in the 1960s. Combined with the preliminary reference procedure, direct effect and legal supremacy enabled the CJEU to issue binding treaty interpretations, the normative force of which was amplified by the fact that they were incorporated into the judgements of national courts in cases brought directly by member state nationals. It is in this way that the EU's founding treaties were constitutionalised (Weiler 1994).

ITL's crucial insight concerned the dual nature of law in the then-EC: Law was both object and agent of integration (Cappelletti et al. 1986). In other words, ITL conceptualised a project of integration *by* law (court-driven constitutionalisation of the treaties) and *towards* law (a closely integrated and legally bound union of people and peoples).

EMU, as framed by the Maastricht Treaty, *adapted* the logic of ITL, but did not adopt it completely. Like the single market, EMU was to be a 'community of law', with fiscal discipline guaranteed by formally binding rules. However, EMU norms do not have direct effect, and are not subject to the kind of judicial dissemination that so effectively constitutionalised the single market. Instead, implementation of EMU norms required the kind of concerted legislative and administrative action that, prior to the crisis, was often lacking. In sum, EMU was a political project, framed by formal rules, but without giving law the kind of agency it had enjoyed in relation to the single market.

The financial crisis became a European crisis in 2010. Initially framed as a problem caused by excessive and unsustainable sovereign debt (a narrative that has since been shown to have been inaccurate, but which continues to colour the response), the crisis manifested most urgently in relation to Greece. In May 2010, Greece received the first in what was to become a series of bailouts, the initial one taking the form of bilateral loans from European partners (Louis 2010). I will not recapitulate the story of the euro crisis and its evolution here. The important point, for our purposes, is that the crisis precipitated a transition to a new mode of integration, which I term Integration through Crisis (ITC) (Scicluna 2017). The key characteristics of ITC may be summarised as follows:

- It is ends-driven; the end being the preservation of EMU, with its current membership, and without turning it into a transfer union,
- It is extra-constitutional, in the sense of avoiding treaty reform by going outside the treaty framework,
- It exacerbates pre-existing tendencies in the EU to avoid political contestation by concentrating power in the hands of executives and non-majoritarian bodies,
- It places more emphasis on the coercive enforcement of EMU's rules (including those adopted through *ad hoc* and extra-constitutional processes) on debtor states,
- And, finally, it is justified through emergency rhetoric.

Thus, ITC does not *abandon* law. On the contrary, the 'rhetoric of rules' (i.e. the emphasis on the importance of following the rules) has been pervasive throughout the crisis response. In fact, this rhetoric mirrors the dominant, though inaccurate, narrative of Northern 'saints' and Southern 'sinners' - the latter got themselves into trouble precisely because they did not follow 'the rules'.

ITC might provide short term fixes, but it does not provide long term solutions to the EU's myriad crises because it is an integration mode that specifically relies on avoiding the kind of major institutional and legal reform that EMU needs. Moreover, the highpoint of ITC may already have passed. ITC relies on there being an elite consensus, or something close to an elite consensus, in order to circumvent the popular constraining dissensus. But that elite consensus is breaking down, as may be evidenced, for example, by the formation of a new governing coalition in Italy between the populist Five Star Movement and the eurosceptic *Lega*, or by fractures within the German governing coalition.

The ECB as an agent of integration-through-crisis

It is in the context of the transition from ITL to ITC that the ECB took centre stage. Since its creation in 1998, the ECB has been an important component of the EU's regulatory state. It is an independent agency, insulated from direct majoritarian pressure, which has been mandated by member states to set monetary policy for the eurozone. As is common with regulatory bodies, the ECB's mandate (constitutionalised in the Maastricht Treaty) is explicitly circumscribed in some areas, but vague, or 'incomplete' in others.

In the case of the ECB, two key aspects of its mandate are made explicit. Firstly, the Bank is confined to monetary policy making and excluded from the realm of economic policy making, which is left to individual national governments. Secondly, the Bank is given an explicit hierarchy of objectives to pursue - price stability is its primary goal, though it may also act to support the general economic policies of the Union so long as such actions do not conflict with the objective of price stability. Yet, there are other, equally important aspects, in which the principal-agent contract is incomplete. 'Price stability' is not defined, and neither are the policy instruments by which the ECB may pursue its mandated objectives.

The crisis offered an opportunity to fill in some of those gaps. Faced with possible collapse of the eurozone in 2010-2012, the ECB began to adopt a number of unconventional policy instruments, including the Outright Monetary Transactions (OMT) programme, and to take a bigger role in providing much-needed finance to euro area banks via the Emergency Liquidity Assistance (ELA) programme. The Bank's actions over the crisis years have often been described as 'necessary' (though cf. Sinn 2014: 280-293). But how are we to understand and evaluate necessity under these circumstances, and how does it relate to legitimacy? Indeed, notwithstanding the rhetoric of necessity, the policy problems addressed by the ECB are very much distributional in their effects and, therefore, not suitable for technocratic resolution. Consequently, the ECB's empowerment has contributed to the crisis-hit EU's 'politicisation without democratisation' (Scicluna 2014), as may be illustrated by reference to the *Gauweiler* litigation over the OMT programme.

The *Gauweiler* litigation: Constitutionalisation of regulatory overreach

The *Gauweiler* litigation marked, perhaps, the most significant test of the constitutionality of the euro crisis response (Fabbrini 2016: 3). The case concerned the compatibility with EU law of the OMT programme, an initiative announced by the ECB in September 2012, according to which the Bank would purchase the debt instruments of eurozone member states on secondary markets, in exchange for the affected state entering into a programme of financial assistance with the European Stability Mechanism (ESM), the eurozone's permanent bailout fund. The OMT programme was, thus, the policy manifestation of Mario Draghi's famous pledge, made in July 2012, that the ECB would do 'whatever it takes' to guarantee the eurozone's survival. Measured against its aim of calming markets so as to ensure the smooth transmission of ECB monetary policy, the OMT programme was highly successful. So successful, in fact, that it was never used. Its mere announcement had the desired effect.

Nevertheless, the fact that it was never used did not allay concerns over the programme's alleged illegality. This was especially so in Germany, where most steps in the crisis response have elicited fears that, notwithstanding the provisions put in place in the Maastricht Treaty, EMU is becoming a transfer union. The complaint brought by the Christian Social Union (CSU) politician, Peter Gauweiler, and others was couched in constitutional terms. It centred on the claim that the ECB had acted *ultra vires* in announcing OMT, since this was an *economic* policy, outside of the Bank's monetary policy remit, and, furthermore, that the programme breached Article 123 TFEU's prohibition of monetary financing of government debts.

The case came first to the German Federal Constitutional Court (FCC), which referred certain questions to the CJEU - the first time in its history that the FCC had used the preliminary reference procedure. In this respect, the constitutional significance of the case extended beyond its particular subject matter to take in the relationship between national courts and the CJEU in the EU's informally constitutionalised judicial order (Scicluna 2015). For, although the FCC's utilisation of the preliminary reference procedure could be regarded as indicating acceptance of the CJEU's exclusive competence to interpret EU law, the text of the referral made it clear that the situation was not so settled (Fabbrini 2016: 4).

Indeed, the potential for direct conflict between the two courts was flagged by the German Court's invocation of its own previously established test of whether an EU institution has exceeded its competences.[252] That is, the FCC suggested that the OMT programme constituted a 'manifest violation' of the ECB's powers that caused a 'structurally significant shift' in the allocation of competences between the national and supranational levels.[253] The FCC's very ability to articulate such a test is not accepted by the CJEU, which claims for itself sole competence to find the act of an EU institution *ultra vires*. Hence, the *Gauweiler* case was an opportunity to test not only the legality of the euro crisis response - particularly its expansion of the space available for technocratic decision making at the expense of democratically-accountable policy

252 BVerfG, 2 BvR 2661/06 vom 6.7.2010, Absatz-Nr. (1 – 116), available at www. bverfg.de/entscheidungen/rs20100706_2bvr266106en.html (*Honeywell* case).

253 BVerfG, 2 BvR 2728/13 vom 14.1.2014, Absatz-Nr. (1 – 105) available at www.bverfg.de/entscheidungen/rs20140114_2bvr272813en.html (*OMT referral*), paras. 36-43.

modes - but also either to reaffirm or reconfigure core features of the EU's constitutional settlement.

The CJEU announced its decision in the *Gauweiler* case on 16 June 2015.[254] The Court affirmed the legality of the OMT programme, applying an *objectives*-based, rather than *effects*-based, test. This allowed OMT to be qualified as a monetary policy measure, owing to the ECB's overarching price stability objective, notwithstanding the programme's potentially significant economic policy effects, including its requirement that a beneficiary state undertake a macroeconomic adjustment programme (Louis 2016: 60-1).

What are the consequences of the *Gauweiler* verdict? Formally, the ECB's mandate has not changed. It retains its exclusive monetary policy competence, while eurozone member governments retain their economic policy competences. Yet, *de facto*, the ECB has expanded the scope of its powers considerably - an expansion that the CJEU has gone some way towards constitutionalising. In particular, the objectives-based test takes the ECB at its own word. OMTs must be a monetary policy measure because the Bank's stated aim in announcing the policy was to safeguard the 'singleness' of eurozone monetary policy, itself a prerequisite of the Bank's effective pursuit of its core goal of price stability.

The CJEU's deferral to the ECB's expertise on the question of what constitutes monetary policy is neither surprising nor without justification (see e.g. Zilioli 2016). As the Court itself pointed out, since preparation and implementation of a programme such as OMT requires the ECB 'to make choices of a technical nature and to undertake forecasts and complex assessments', the Bank 'must be allowed, in that context, a broad discretion'.[255] Certainly, it would not make sense for the Court to attempt to substitute its own judgement on the highly technical questions involved in the case for that of the ECB. Yet, deferral to expertise cannot be limitless, and the *Gauweiler* case was surely an opportunity for the Court to make clear that while the EU treaties may interpreted flexibly, their letter and spirit cannot be blatantly disregarded (see e.g. Joerges 2016).

As it is, the *Gauweiler* decision has left the ECB's discretion to interpret its own mandate effectively unchecked. Now that the CJEU has endorsed the Bank's unorthodox policy manoeuvres, only treaty reform - with all of its prohibitively high barriers - could reintroduce constraints. Thus, while the ECB's unprecedented empowerment was driven by the circumstances of the euro crisis, it will long outlast the 'state of emergency' (White 2015: 593–9). Meanwhile, the FCC declined to follow up on its implied threat to overrule a binding interpretation issued by the CJEU. In its final ruling on the *Gauweiler* case, delivered in June 2016, the German Court cast doubt upon the CJEU's reasoning, including its uncritical acceptance of the ECB's interpretation of the purposes and nature of the OMT programme, but it nevertheless accepted the Court of Justice's conclusion.[256]

Thus, a clash between two of Europe's most powerful courts, which could have threatened the basic tenets on which the EU as a community of law was founded, was avoided. Despite its occasionally strong rhetoric, the FCC continues to willingly endorse the supremacy of EU law, embodied in the CJEU's extensive and exclusive power to determine the outer limits of the competence of EU institutions.

However, at the same time, the *Gauweiler* litigation, by constitutionalising the ECB's regulatory overreach, contributes to a deeper and much more serious crisis of EU constitutionalism: That is, the EU's shift from a *Europäische Rechtsgemeinschaft* (European community of law), premised on *voluntary* cooperation, to a *Zwangsgemeinschaft* (community under duress), which places more emphasis on coercive forms of integration (Bogdandy 2017). This idea is explored further below.

254 Case C-62/14, *Peter Gauweiler et al. v Deutscher Bundestag* (*Gauweiler* case)

255 Case C-62/14 *Gauweiler*, para. 68.

256 BVerfG, 2 BvR 2728/13, 2 BvR 2729/13, 2 BvR 2730/13, 2 BvR 2731/13, 2 BvE 13/13 decision from 21.06.2016.

The ECB and the coercive turn in EMU governance

The second characteristic of ITC on which this paper focuses is its tendency to emphasise coercive enforcement of 'the rules', however those rules may have come into existence. As Christian Kreuder-Sonnen (2018: 452-4) has noted, the crisis years have produced an 'authoritarian turn' in European politics that afflicts both EU-level and national-level governance. At the EU level, 'traits of authoritarianism' manifest in an emergency politics that privileges non-democratically accountable discretion in policy making. Again, the ECB is heavily implicated in this 'authoritarian turn', as three examples shall suffice to illustrate.

We may firstly point to the ECB's decision, in mid-2015, not to increase the level of ELA to Greek banks to a level that would be necessary to counter the capital flight that the country's banking system was experiencing. This decision was taken in the midst of fierce contestation between Greece and its creditors over whether it would receive further financial assistance and under what conditions. In fact, the ECB made its decision on 28 June 2015 - the day following Greek Prime Minister Alexis Tsipras's announcement of a referendum on the bailout terms offered by the creditors. It resulted in a three-week closure of Greek banks, which began days before the referendum was held.

It is debatable whether the ECB was simply applying the ELA eligibility rules in a technical manner (with unfortunate timing), or whether it was deliberately signalling to Greeks the consequences of voting to reject austerity. In some ways, it does not matter. A decision that shuts down a country's banking system days before a major vote in that country is a political decision. The ECB simply lacks the legitimacy resources to take such a consequential action.

The second example concerns the ECB's intervention in Cyprus two years prior to the Greek ELA decision. On 19 March 2013, the Cypriot parliament rejected a ten-billion euro bailout negotiated between the government and the 'Troika' of creditors (comprising the European Commission, the IMF and the ECB itself), which controversially required the imposition of a tax on all Cypriot bank deposits over 20,000 euros. The ECB responded by issuing an ultimatum on 21 March that Cyprus either secure a new bailout before 25 March, or lose its ELA funding (Wearden and Amos 2013). The amended bailout package was duly adopted a few days later, in a form that did not require parliamentary approval (Smith 2013). Thus, the ECB was able to use the ELA programme to pressure the Cypriot government into accepting an austerity-linked bailout that the Bank itself, as part of the Troika, had helped to design and would help to oversee. It contributed to the undermining of democratic oversight in Cyprus by encouraging the Cypriot government to adopt policy in a way that bypassed the parliament.

The final example concerns the infamous Trichet-Draghi letter that was sent to the Italian government of Silvio Berlusconi on 5 August 2011. In the letter, which was intended to be confidential but was later published by an Italian newspaper, Jean-Claude Trichet, then ECB president, and Draghi, his heir, outlined a number of reform measures, which they urged the Italian government to undertake with the utmost speed.[257] The ECB had, and has, no legal basis make such a request, which called for comprehensive and detailed legal reform in areas including the labour market, public administration and pensions - all areas of national competence. It was, rather, a coercive form of 'implicit conditionality', enabled by the ECB's leverage over national banking systems and justified by the prevailing atmosphere of emergency (Sacchi 2015).

What all three examples have in common is that they involve the technocratic, non-democratically accountable ECB playing the role of teacher and disciplinarian in order to 'discipline and punish' the eurozone's delinquent member states (Kund-

257 The letter is available at https://www.corriere.it/economia/11_settembre_29/trichet_draghi_inglese_304a5f1e-ea59-11e0-ae06-4da866778017.shtml?fr=correlati.

nani 2018). Such attempts at coercive enforcement betray the EU's purposes and values, and contribute significantly to the degradation of democracy in Europe, particularly in the countries of the eurozone's periphery.

As noted above, there is a tendency among scholars and observers of the EU to allow the ECB considerable room to manoeuvre on the grounds of 'necessity'. However, even if the Bank's actions *are* deemed necessary, it is worth asking *why* this is so. The fact that no other EU institution could act so decisively exposes the EU's lack of actorness; its weakness as a political construct. It also exposes the anti-democratic, market-beholden logic that has driven the crisis response: The need to placate 'the markets' (explicitly invoked, e.g., in the Trichet-Draghi letter) is treated as considerably more important than the need to placate disaffected voters.

A recent illustration of this phenomenon occurred in May 2018, when it looked like Italians would have to return to the polls for the second time in a matter of months to resolve a government formation deadlock. In an interview with *Deutsche Welle*, Günther Oettinger, the European Commissioner for Budget and Human Resources, suggested that the markets would teach Italians not to vote for populists. Such sentiments, however carelessly expressed, reflect the underlying teleological assumptions that many practitioners, as well as scholars, continue to hold about the purpose and end point of European integration. These assumptions may be summarised in the idea that more integration is the solution to any and all of Europe's problems. Deviations from the path towards ever closer union are exactly that - deviations; mistakes in need of correction.

It is in this context that regulators take on ever-expanding political roles. If national publics, and even national governments, are fickle and short-sighted, then it is for regulators - dispassionate, objective, far-sighted - to keep the process of European integration on the right track. However, these attitudes are very much part of the problem. They impoverish democracy and fuel the turn to populism within member states, and they undermine the legitimacy on which the EU rests.

More broadly, the idea that the EU could regulate itself out of crisis; that restoring confidence and stability to the eurozone was primarily a matter of putting the right policy settings in place; was misplaced and misguided. The regulatory approach to the euro crisis - of which the ECB has been at the forefront - overestimated fidelity to the rules and to the idea of the 'rule of rules' amongst member states. It underestimated the extent to which acceptance of, and adherence to, rules was contingent on there being a virtuous circle of cumulatively causal integration (Jones 2018). In short, the regulatory approach to crisis was based on a misunderstanding of the nature of the EU as a community of law. The EC/EU worked relatively well as a voluntary community of law - eliciting compliance through powerful instrumental and normative logics without the need for hard enforcement. However, the euro crisis has severely disrupted the economic benefits-driven virtuous circle that powered European integration. EMU's 'coercive turn' has only made the integration project's problems worse.

Concluding remarks

The euro crisis has created a 'postfunctionalist dilemma' for European elites. Functional pressures continue to push national executives towards integrative steps - bailout mechanisms, banking union, fiscal surveillance, etc. However, growing popular resistance to 'more Europe' has made it impossible to adopt and embed crisis initiatives into the existing framework of EU constitutionalism via treaty change. Consequently, emergency politics in the EU has taken on a distinctly extra-legal character (Hooghe and Marks 2017: 8-9).

To put it differently, over the last several years, extraordinary policies have been adopted via extraordinary means. These policies are then embedded via a ritualistic insistence (usually made by EU institutions and creditor states towards debtor states) on the need to follow the rules - an insistence which ignores the dubious ways in which the 'rules' that make up the EU's emergency politics came into existence. Both ITL and ITC are problematic from a democratic standpoint – the former empowered courts to decide on fundamentally political questions, while the latter empowers executives and technocratic experts. Combined with politicisation and disregard for maintaining the coherence of EU constitutionalism, ITC further damages the EU's legitimacy.

As I have argued in this paper, the case of the ECB is particularly illustrative. Without any formal change to its narrow, monetary policy-focused mandate, its role has been significantly expanded and politicised. The ECB is guarantor of the euro's continued existence. It is lender of last resort for the eurozone's troubled banks and sovereigns. And it is teacher and disciplinarian to those governments and publics that attempt to escape the dictates of austerity.

Perhaps national executives and EU leaders judged the regulatory approach to the euro crisis to be the 'path of least political resistance' (Hooghe and Marks 2017: 9). However, this judgement is likely to prove incorrect over the longer term. Just as European integration is cumulatively causal, so too is disintegration (Jones 2018). As domestic-level political resistance - expressed, for example, via the election of eurosceptic populists - accumulates, the constraining dissensus that operates at the European level is strengthened. As European elites continue to push against the constraining dissensus, so national-level democracy is undermined, and EU-level legitimacy weakened.

Bibliography

Cappelletti, M., Seccombe, M. and Weiler, J.H.H. (1986), *Integration Through Law*, Berlin: De Gruyter.

Fabbrini, F. (2016) 'The European Court of Justice, the European Central Bank, and the Supremacy of EU Law', *Maastricht Journal of European and Comparative Law* 23(1): 3-16.

Hooghe, L. and Marks, G. (2017) 'Cleavage theory meets Europe's crises: Lipset, Rokkan, and the transnational cleavage', *Journal of European Public Policy,* DOI: 10.1080/13501763.2017.1310279.

Joerges, C. (2016) '*Pereat Iustitia, Fiat Mundus*: What is Left of the European Economic Constitution after the *Gauweiler* Litigation?' *Maastricht Journal of European and Comparative Law* 23(1): 99-118.

Jones, E. (2018) 'Towards a theory of disintegration', *Journal of European Public Policy* 25(3): 440-51.

Kreuder-Sonnen, C. (2018) 'An authoritarian turn in Europe and European Studies?', *Journal of European Public Policy* 25(3): 452-64.

Kundnani, H. (2018) 'Discipline and Punish', *Berlin Policy Journal*, 27 April 2018.

Louis, J.-V. (2010) 'The No-Bailout Clause and Rescue Packages', *Common Market Law Review* 47(4): 971–86.

Louis, J.-V. (2016) 'The EMU after the Gauweiler Judgment and the Juncker Report', *Maastricht Journal of European and Comparative Law* 23(1): 55-78.

Sacchi, S. (2015) 'Conditionality by other means: EU involvement in Italy's structural reforms in the sovereign debt crisis', *Comparative European Politics* 13(1): 77-92. Scicluna, N. (2014) 'Politicization without democratization: How the Eurozone crisis is transforming EU law and politics', *International Journal of Constitutional Law* 12(3): 545–71.

Scicluna, N. (2015) *European Union Constitutionalism in Crisis*, London: Routledge.

Scicluna, N. (2017) 'Integration through the disintegration of law? The ECB and EU constitutionalism in the crisis', *Journal of European Public Policy,* DOI: 10.1080/13501763.2017.1362026.

Sinn, H.-W. (2014) *The Euro Trap: On Bursting Bubbles, Budgets, and Beliefs*, Oxford: Oxford University Press.

Von Bogdandy, A. (2017) 'Von der technokratischen Rechtsgemeinschaft zum politisierten Rechtsraum', *MPIL Research Paper Series* No. 2017-12.

Wearden, G. and Amos, H. (2013) 'Cyprus Crisis: Politicians Race to Agree Details of "Plan B"', *The Guardian*, 22 March 2013.

Weiler, J.H.H. (1994) 'A quiet revolution: The European court of justice and its interlocutors', *Comparative Political Studies* 26(4): 510–34.

White, J. (2015) 'Authority after emergency rule', *The Modern Law Review* 78(4): 585–610.

Zilioli, C. (2016) 'The ECB's Powers and Institutional Role in the Financial Crisis: A Confirmation from the Court of Justice of the European Union', *Maastricht Journal of European and Comparative Law* 23(1): 171-84.

SHOULD THE SPECIFICS OF NATIONAL POLITICAL CULTURES BE CHARACTERISED AS "DEMOCRATIC ACQUIS" AND CAN THEY BE DEFENDED BY LAW? BEYOND THE NOSTALGIA-CONTROVERSY BETWEEN JÜRGEN HABERMAS AND WOLFGANG STREECK

Christian Joerges

Berlin / Bremen

Two Introductory Remarks

These introductory remarks will define the objectives of my intervention. They are ambitious but this may not be so readily apparent and may hence require some explanations. The difficulty is twofold: My disciplinary focus is on law but my type of argument does not comply with the rules prevailing in legal studies. On the other hand, the announcement of a discussion of a *legal* problem tends to disappoint non-legal quarters from the very outset. I hope to explain why my legal queries mirror conceptual and theoretical issues of general importance, namely the mainstream understanding of the functions of law and the judiciary in the integration process. The critique which I submit is related to the big names in my subtitle and the fierce controversy over the relationship between the nation state and the Union (Section I.). The follow-up section will turn to the implications of my critique. My argument will be as immodest as the announcement in the conference agenda. We have to abandon, so I will submit, the "ever more Europe" mantra, take instead the fortunate motto of the ill-fated Draft Constitutional Treaty of 2004 seriously, and explore what it might entail for Europe to be "united in diversity ("*in Vielfalt geeint*") (Section II.).

1. The Failures of the "Integration through Law" Orthodoxy

As late as 1990, the former President of the EUI, Joseph Weiler, and his successor to the presidency, Renaud Dehousse, co-authored an article on the "legal dimension" of the integration project in a prestigious collection of essays edited by William Wallace.[1] The law, so the most famous and much cited sentence of the article reads, is both "the object and the agent" of integration.[2] Nearly everything that went wrong in the integration project is summarised in this perplexing pronouncement.

The famous motto was coined at the height of the American law and society movement, which promoted the sociological study of law and all sorts of interdisciplinary "law and …" explorations. How could European law scholarship defend views and visions on the potential of "law as such" which had long since been discredited? These methodological irritations coincide with substantive concerns. On what grounds could the unity of law in the (then) Community be understood as an end in itself? To be sure, the implicit assumption of the unity doctrine that "one size would fit all" and "be best for all" was not as implausible in the foundational period as it has now become. However, even in the relatively homogenous orders of the former EEC, any unification at European level had disintegrative effects within national legal orders. The reference procedure of the EEC Treaty cannot accomplish anything beyond some pointillist "harmonisation" here and there. The integration-through-law agenda is therefore deficient where "positive integration", *i.e.*, the replacement of national legislation by a comprehensive Euro-

1 Renaud Dehousse and Joseph H.H. Weiler, "The legal dimension", in: William Wallace (ed.), *The Dynamics of European Integration*, (London: Pinter, 1990), 242-260, at 243.

2 Ibid., 243.

pean scheme is envisaged.[3] To be sure, such piecemeal steps have been undertaken from early on, in particular in the field of consumer protection, but they could not transform the pointillist modes of legal integration. The reasons should have been obvious. Back in 1982, the America scholar and judge Guido Calabresi had examined the tensions between the common law system and problem-specific legislative corrections.[4] It is obvious that what is difficult to accommodate within the common legal culture of the US is more problematical in a Community of six or more Member States with diverse legal traditions. And last, but not least, on what grounds can one argue that an ever more uniform legal order deserves the same degree of recognition throughout the entire Community?

The "Integration through law" agenda tends to cause the disintegration of national legal systems without establishing a European substitute because "the logic of integration" (as practised through "negative integration") is at odds with the "logic of post-classical private law".[5] In a seminal essay, entitled "Legal Irritants: Good Faith in British Law, Or How Unifying Law Ends up in New Differences",[6] Gunther Teubner has made comparative lawyers aware of this phenomenon, which is both unsurprising and unavoidable, as Karl-Heinz Ladeur has added, because European law cannot reach the sphere of social norms within which the law operates and upon which its functioning depends.[7]

Gunther Teubner has re-published his essay in the legendary Hall and Soskice volume on the *Varieties of Capitalism*.[8] This is indeed, in my view, the background for the disintegrative effects of integration through law. What seems so irritating to the community of European lawyers hardly requires any explanatory exercises in the present context. If there is a kernel of truth in the message about the varieties of the socio-economic systems of the Member States of the EU, it is simply inconceivable that their integration can be brought about "through law". It is totally unsurprising that the orchestrators of Europe's crisis politics argue that they have to impose a convergence of the economies and policies of the Member States in order to ensure the functioning of the "new modes of economic governance". This is, of course, not to suggest that these efforts will overcome the difficulties of the integration-through-law agenda. Teubner's "irritants" make themselves felt in the resistance of legal and economic cultures.[9]

Our conference has explored these issues more

3 *Locus classicus*: Friedrich A. von Hayek, "The Economic Conditions of Interstate Federalism", in: Friedrich A. Hayek, *Individualism and Economic Order*, (Chicago IL: University of Chicago Press, 1949), 255-272 (reprinted from the *New Commonwealth Quarterly* V. 2 (September 1939), 131-149.

4 Guido Calabresi. *A Common Law for the Age of Statutes*, (Cambridge, MA/London: Harvard UP 1982).

5 See Christian Joerges, "The Impact of European Integration on Private Law. Reductionist Perceptions, True Conflicts and a New Constitutional Perspective", (1997) 3 *European Law Journal*, 378-406. Gert Brüggemeier and Christian Joerges, "Europäisierung des Vertrags- und Haftungsrechts", in: Peter-Christian Müller-Graff (ed.), *Gemeinsames Privatrecht in der Europäischen Gemeinschaft* (Baden-Baden: Nomos 1993, 2nd. ed. 1999), 301-360.; Christoph Schmid, *Die Instrumentalisierung des Privatrechts durch die Europäische Union. Privatrecht und Privatrechtskonzeptionen in der Entwicklung der Europäischen Integrationsverfassung* (Baden-Baden: Nomos, 2010), *passim*.

6 *Modern Law Review* 61 (1998), 11-32.

7 Karl-Heinz Ladeur, "'Conflicts Law as Europe'sConstitutional Form' … and the Conflict of Social Norms as its Infrastructure", in: Christian Joerges and Carole Glinski (eds), *The European Crisis and the Transformation of Transnational Governance: Authoritarian Managerialism versus Democratic Governance*, (Oxford-Portland OR: Hart Publishing, 2014), 383-396.

8 "How Unifying Law Ends up in New Differences", in: Peter Hall and David Soskice (eds), *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage.*, (Oxford: Oxford UP, 2001), 417- 441.

9 See Gunther Teubner, "Eigensinnige Produktionsregimes: Zur Ko-evolution von Wirtschaft und Recht in den varieties of capitalism", (1999) 5 *Soziale Systeme*, 7-26 [Idiosyncratic Production Regimes: Co-evolution of Economic and Legal Institutions in the Varieties of Capitalism, in: John Ziman (ed.), *The Evolution of Cultural Entities: Proceedings of the British Academy 112.* (Oxford: Oxford UP, 2002), 161-182], and the works of Werner Abelshauser, e.g., "Europa in Vielfalt einigen. Eine Denkschrift", in: A.B. Atkinson, P.M. Huber, H. James and F.W. Scharpf (eds), *Nationalstaat und Europäische Union. Eine Bestandsaufnahme*, (Baden-Baden: Nomos, 2016), 275-294; W. Abelshauser, D. Gilgen and A. Leutzsch, "Kultur, Wirtschaft, Kulturen der Weltwirtschaft", in: Wener Abelshauser, David Gilgen and Andreas Leutzsch (eds), *Kulturen der Weltwirtschaft*, (Göttingen: Vandenhoek und Ruprecht, 2013), 9-29.

thoroughly. My objective as a lawyer, however, is distinct. I am primarily concerned with the normative – legal and constitutional – implications of Europe's diversity. It is this concern which the debate between Habermas and Streeck, to which my subtitle refers, illustrates quite instructively.

Their exchange[10] builds on well-known arguments and is somewhat repetitive.[11] There is a strong legal dimension in their controversy, which fits well into the agenda of our conference. Streeck questions the potential of Europe to establish, at a transnational level, an equivalent to the national *Sozialstaat*. In Streeck's understanding, which is informed by the constitutional theory of Hermann Heller,[12] *Sozialstaatlichkeit*, as it has been endorsed by the eternity clause of the Basic Law, is a democratic essential.[13] Because of the ongoing erosion of social protection provisions in the integration process, he opts for a defence of the nation state and its institutions against a deepening of economic integration.[14] Habermas shares a commitment to Hermann Heller – small wonder, as Wolfgang Abendroth, with whom he wrote his habilitation thesis, wrote a famous defence of Heller's in the first great post-war *Verfassungsstreit*.[15]

10 Jürgen Habermas, "Demokratie oder Kapitalismus? Vom Elend der nationalstaatlichen Fragmentierung in einer kapitalistisch integrierten Weltgesellschaft", (2013) 5 *Blätter für deutsche und internationale Politik*, 59-70; Wolfgang Streeck, "*Small-State Nostalgia*? The Currency Union, Germany, and Europe: A Reply to Jürgen Habermas", (2014) 21 *Constellations*, 213-221.

11 The earliest encounter of which I am aware is Streeck's – unpublished -- reaction to Habermas' plea for a European constitution in his "Hamburg Lecture" of 26 June 2001 on "Warum braucht Europa eine Verfassung?", published in DIE ZEIT and still available at: http://www.zeit.de/2001/27/200127_verfassung.xml/seite-7. "Voluntarism" is the core objection in Streeck's paper ("Das 'soziale Europa' und seine Verfassung: Fragen zu einem politischen Projekt", on file with author).

12 See, e.g., his recent "Heller, Schmitt and the Euro", (2017) 21 *European Law Journal*, 361-370.

13 Art. 79 III GG.

14 Wolfgang Streeck, "Small-State Nostalgia? The Currency Union, Germany, and Europe: A Reply to Jürgen Habermas", (2014) 21 *Constellations*, 213-221.

15 See Christian Joerges, "The *Rechtsstaat* and Social Europe: How a Classical Tension Resurfaces in the European Integration Process", (2010) 9 *Comparative Sociology*, 65-85..

"The social" became more deeply engrained in the discourse theory of law and democracy.

The nation state and its welfare accomplishments, Habermas submits, is merely a nostalgic option, a hideaway in the sovereign powerlessness of the overrun nation (*eine "nostalgische Option für eine Einigelung in der souveränen Ohnmacht der überrollten Nation*").[16] There is some unity in the diversity of the two opponents. Both invoke the interdependence of facticity and validity. They share the premise that economic liberalism is far too insensitive to the quests for social justice and should therefore be subjected to political corrections. They disagree about "the level of governance" at which such corrections can be realised. This, however, is anything but a trivial disagreement. It is one which reveals a deep *lacunae* in extensive legal debates on what has been characterised in ever more intensity as "Europe's Justice Deficit".[17] This notion is of a revealing vagueness. What exactly is Europe supposed to do? Should it compensate justice failures with the Member States, for example, by imposing a uniform "European Social Model"? Should it, instead, supervise the inter-state relations and ensure "justice between" its Members?

Streeck's political and normative conclusion builds coherently on his sociological analysis – including his extensive discussion of the varieties of capitalism.[18] His logic is both sociologically and legally compelling: under European rule, the social state cannot survive. We have hence to replace the supremacy of European law by a primacy of the nation state. His argument is also richer than the usual rejection of European claims to supremacy:

16 Jürgen Habermas, "Demokratie oder Kapitalismus. Vom Elend der nationalstaatlichen Fragmentierung in einer kapitalistisch integrierten Weltgesellschaft", *Blätter für deutsche und internationale Politik* 5/2013, 59-70 ("Nostalgische Kleinstaaterei", 62).

17 *Europe's Justice Deficit?*, co-edited by Dimitry Kochenov, Gráinne de Búrca and Andrew Williams, (Oxford: Hart Publishing, 2015).

18 Streeck, MPIfG Discussion Paper 10/ 12; Blätter 2013: Was nun, Europa? Kapitalismus ohne Demokratie oder Demokratie ohne Kapitalismus.

> "[W]hat I would suggest to call the *acquises démocratiques* of the national *demoi* in Europe … importantly comprises a wide range of political-economic institutions that provide for democratic corrections of market outcomes – for democracy as *social* democracy."[19]

This is one of the very few suggestions to take the insights of the studies of the varieties of capitalism both normatively and seriously. I am aware of only three German jurists – there will be more! -- who have submitted like arguments, namely, Anna Beckers,[20] Ulrich K. Preuß.[21]and Gunther Teubner[22] They have all understood the legal implications of the varieties studies. Legal rules and institutions do not operate in splendid insulation, but constitute interdependencies. The deeper level of the gist of the matter can be explained with the help of a famous dictum of the German constitutional scholar and judge Ernst-Wolfgang Böckenförde: secularised democracies, he held, live on normative resources, which they cannot generate themselves.[23] In the European context, the integration project lives on cultural and normative resources, which cannot be produced wilfully or by some political or legislative fiat. In a more mundane version, democratic legitimacy in the EU lives on the quality of the democracies in the Member States, their historical experiences, ideational traditions, and political preferences. Europe can promote and protect these accomplishments. To replace national endeavours by the prescription of some uniform political rule risks their destruction.

19 Wolfgang Streeck, *How Will Capitalism End?*, (London: Verso Books, 2016), 198, n. 20.

20 Anna Beckers, Enforcing *Corporate* Social Responsibility *Codes*. On Global Self-Regulation and National Private Law, Oxford, Hart Publishing, 2015, 50 ff.

21 Claus Offe and Ulrich K. Preuß, "The Union's Course: Between a Supranational Welfare State and Creeping Decay", in id. and Claus Offe, *Citizens in Europe*. Essays on Democracy, Constitutionalism and *European* Integration, Colchester: ECPR Press, 2015, 15 ff.

22 Teubner above, n. 8.

23 Ernst-Wolfgang Böckenförde, "Die Entstehung des Staates als Vorgang der Säkularisation", in id. *Staat, Gesellschaft, Freiheit. Studien zur Staatstheorie und zum Verfassungsrecht*, Frankfurt a.M.: Suhrkamp 1975, 42-64.

2. Institutionalising the United in Diversity Vision

The observations just submitted are somewhat emphatic and abstract. I should not proceed with their defence without mentioning Habermas' objections. His three main points are (I reproduce only the substance of his messages; his German is impressive and would get hurt by a translation of mine):

> There is a concession to the diversity vision: "In keinem demokratischen Gemeinwesen darf das historisch gewachsene politisch-kulturelle Selbstverständnis nationaler Minderheiten der Assimilation an die Mehrheitskultur geopfert werden."
>
> However, we should not equate cultural identities with economic cultures: "Aber können wir den wohlbegründeten Rechtsschutz für kulturelle Identitäten umstandslos auf Wirtschaftskulturen, auf die, wie Wolfgang Streeck sagt, 'parochialen' Formen des Kapitalismus, z.B. auf Systeme von Arbeitsbeziehungen oder auf sozialpolitische Regime ausdehnen? "Ich sehe nicht, wie sich ein kultureller Naturschutz für ein jeweils bestehendes Ensemble von sozioökonomischer Praktiken begründen ließe."
>
> We should instead trust that a postnational identity and solidarity will emerge: "Es ist nicht unrealistisch anzunehmen, dass sich die, im Laufe der Nationalstaatsbildng sehr allmählich etablierte staatbürgerliche Solidarität in dem Maße über die Grenzen des Nationalstaates hinaus erweitert, wie die Bürger von supranationalen Entscheidungen nicht nur betroffen, sondern daran nach demokratischen Verfahren auch beteiligt werden."

Never take Habermas lightly. Fortunately enough, however, I can invoke the authority of another classic, namely, the founding father of economic sociology, Karl Polanyi, for my critique of his argument.

Karl Polanyi's *Great Transformation* is concerned with the emergence of "market societies", where "instead of the economy embedded in social relations, social relations are embedded in the economy".[24] Writing at the end of the Great War, Polanyi had witnessed the destruction of liberal economic ordering by Fascism and Nazism. However, by now, at the end of the Second World War, the rebirth of alternative counter-movements was in sight and nurtured hopes in a better national and international future: alternatives to the Fascist transformation, namely, social counter-movements which would undermine the working of the market system ("the tension between a constant push towards self-regulating markets and spontaneous resistance to the subordination of society to market forces", Dorothee Bohle). His somewhat enigmatic views are difficult to decipher. "*The Great Transformation* can legitimately be read either as an anti-capitalist manifesto or as a social democratic bedtime story."[25] Be that as it may, my shortcut is a passage in which Polanyi considers that:

> "… with the disappearance of the automatic mechanism of the gold standard, governments will find it possible to […] tolerate willingly that other nations shape their domestic institutions according to their inclinations, thus transcending the pernicious nineteenth century dogma of the necessary uniformity of domestic regimes within the orbit of world economy. Out of the ruins of the Old World, cornerstones of the New can be seen to emerge: economic collaboration of governments and the liberty to organize national life at will."[26]

Was this just wishful thinking? The passage was written at a time when Keynes and the like-minded American economist and politician Harry Dexter White were working towards the post-war settlement of Bretton Woods. There were reasons to envisage a better future. Polanyi's considerations deserve attention for three additional and interrelated reasons. For one, he re-states his foundational argument that the capitalist market economy is not an evolutionary given, but a political product – "*laissez-faire* was planned"[27] – which requires institutional backing and continuous political management. To put it slightly differently, "the political" is inherent in "the economic"; market economies "are polities".[28] A second insight of topical importance follows from this: capitalist market economies will exhibit varieties which mirror a variety of political preferences, historical experiences, and socio-economic configurations. This is what we can expect, and, so I conclude, *should respect*, *once our societies have gained the "liberty to organise national life at will"*. The third point is only alluded to in half a sentence. It is an implication of the new freedom. Polanyi predicts and advocates "collaboration"; diversity, we can assume, is there to stay.

Three follow-up queries have to be addressed:

> Even if we concede that the diversity of the institutional infrastructures of the European economies deserves, in principle, recognition, we have to concede that these infrastructures are not written in stone. Endogenous democratic change must remain possible, and insulation against the impact of Europeanisation and globalisation is inconceivable. What precisely distinguishes a variety of an economic culture from a Habermasian "*Schrebergarten*"?
>
> Query (1) assumes implicitly that both Streeck's defence of the nation state and Habermas' defence of European rule are going a step too far. What we need instead is a channelling of change. It is

24 Polanyi, *The Great* Transformation, 57.

25 Gareth Dale, *Karl Polanyi. A Life on the Left,* New York: Columbia UP, 2016, 286.

26 Polanyi, 253-254.

27 "… planning was not", Polanyi, at 147.

28 For a very dense re-construction, see Fred Block, "Towards a New Understanding of Economic Modernity", in: Bo Stråth, Peter Wagner, Christian/Joerges (eds), *The Economy as Polity: The Political Constitution of Contemporary Capitalism*, London: UCL Press 2005,, 3-16.

precisely this which is the objective of the conflicts-law approach which promises to institutionalise the united-in-diversity vision, thereby offering an alternative to both Streeck's nation state nostalgia and Habermas' European utopia.

The normative credentials of this alternative deserve special attention. It seems noteworthy that the conflicts-law approach is by no means as idiosyncratic as my terminology may insinuate.

Ad (1) The first query is the easiest to cope with. It seems obvious that Habermas reproduces his famous dual of "system and lifeworld", that is, his "two-level theory of society, which distinguishes the lifeworld reproduced through communicative action from the functional integration of the administrative and economic subsystems, narrows the capitalist economy to exchange mediated by money". The economy is not "a polity", but a purely functional machinery?! I restrict myself to citing an essay by the Tilburg legal theorist Hans Lindahl, who reminded European lawyers of the enduring currency of Hannah Arendt's concept of "spatiality" as:

> "[N]ot merely a geographical term. It relates not so much, and not primarily, to a piece of land as to the space between individuals in a group whose members are bound to, and at the same time separated and protected from each other by all kinds of relationships, based on a common language, religion, a common history, customs, and laws."[29]

As Michelle Everson commented:

> "For lawyers, the complex of sociological and cultural artefacts that are called upon to instantiate spatial community may appear opaque, but they translate not simply into jurisdictional notions, or territorial instruments of nationality law and security policy, but rather into far more fundamental constitutional structures of political representation and democracy, as well as regulatory frameworks of national economic steering and social re-distribution. And it is here, in the unravelling of the nationally-bounded, majoritarian politics and policies of economic and social integration through intensified globalisation that political populism has found its niche, and that academic thought struggles to identify the new paradigms of political, social and economic organisation,30 which might bridge the gap between a traditional, spatially-delineated world and a post-war globe of universalising aspirations and complex interdependencies."[31]

Ad (2) The second is by no means more demanding, but, due to the technicalities of its structure, more difficult to restate. A very brief summary must suffice here.

Back in 1997, Jürgen Neyer and I submitted the core ideas of the conflicts-law approach ("deliberative" as opposed to orthodox supranationalism) in an essay on European comitology.[32] Our basic premise and intuition was very simple: it is a core premise of theories of democracy, most notably of Habermas' discourse theory of law and democracy, that we, the citizens, must be able to understand ourselves as the authors of the legal provisions with which we are expected to comply. Under conditions of Europeanisation and globalisation and ever more growing interdependences,

29 Hans Lindahl, "Finding a Place for Freedom, Security and Justice: The European Union's Claim to Territorial Unity", (2004) 29 *European Law Review*, 461-484, at 466.

30 Christian Joerges, "Brother, can you Paradigm?", Review Essay of Kaarlo Tuori and Klaus Tuori, *The Eurozone Crisis: A Constitutional Analysis*, (Cambridge: Cambridge UP, 2014), (2014) 12 *International Journal of Constitutional Law*, 769-785.

31 "A Very Cosmopolitan Citizenship: But Who Pays the Price?", in: Michael Dougan, Niamh Nic Shuibhne, Eleanor Spaventa, *About Empowerment and Disempowerment of the European Citizen*, (Oxford: Hart Publishing, 2012), Chapter 6..

32 Christian Joerges and Jürgen Neyer, "From Intergovernmental Bargaining to Deliberative Political Processes: The Constitutionalisation of Comitology", (1997) 3 *European Law Journal*, 273-299.

this is no longer conceivable. To cite Habermas himself:

> "Nation-states … encumber each other with the external effects of decisions that impinge on third parties who had no say in the decision-making process. Hence, states cannot escape the need for regulation and coordination in the expanding horizon of a world society that is increasingly self-programming, even at the cultural level …"[33]

It is difficult to reject these insights. The implications are, of course, controversial. Among the three just-named alternatives – state-building, down-scaling of integration, and co-operation - I opt for the third. In the European case, we can build on European law's potential to compensate for the legitimacy deficits of national rule. European law can derive its own legitimacy from this function: its mandate is to implement the commitments of the Member States towards each other by two legal claims, namely, the requirement to take the interests and concerns of their neighbours into account when designing national policies, and by imposing a duty to co-operate. The very notion of co-operation indicates that this kind of rule cannot be some "command and control" exercise, but must rely on the deliberative quality of co-operative interactions. Two important implications should be underlined. The first: there is no in-built-guarantee that such co-operative efforts will, in the end, be successful; but such limitations need not be damaging *per se*; quite to the contrary, they may document mutual respect of essential, yet distinct, values and commitments of the other (the *ordre public* in the parlance of conflict of laws and private international law). The second implication is more drastic: socio-economic, institutional, political and cultural diversity is particularly strong and difficult to overcome. This, however, is by no means a plea for inactivity; it is, instead, a reminder that we have to distinguish "justice within" consolidated polities, on the one hand, and "justice between" them, on the other - and that we have to work in both spheres.[34] Last, but not least, it should be underlined that the conflicts approach seeks to defend the idea of the law-mediated legitimacy of public rule. A lot more on the conflicts-law approach can be said and has been said.[35] We focus here on the third query.

Ad (3) Again, my terminology is only seemingly idiosyncratic. As long as there is diversity in the EU, the law will have to cope with differences. Conflicts law is simply the name of the discipline doing this. Europe can, in the foreseeable future, not live without it. It can only consider design, its principles and methodology. The normative intuitions which my version of conflicts-law seeks to institutionalise are certainly outside the mainstream of European studies. But I can point to similar approaches. Among them is Daniel Innerarity's concept of "inter-democracy".[36] Two of his insights are particularly important for my argument. The first concerns Europe's heterogeneity, which excludes all "one-size-fits-all" recipes. Instead, "If the EU is going to be more democratic, it will be so in the style of complex democracies. And that complexity is not only related to the diversity of its citizens but to the variety of issues about which it needs to decide, some of which may require proximity, but others that demand a certain distance".[37] "Inter-democracy" is his key concept: the democratisation of interdependencies must replace state-like or federal hierarchical models, he argues forcefully. And,

> "The states are increasingly more incapable of democratic action because they cannot

33 Jürgen Habermas, "Hat die Konstitutionalisierung des Völkerrechts noch eine Chance?", in *id.*, *Der gespaltene Westen,* Frankfurt a.M.: Suhrkamp, 2004, 113-193, at 175.

34 Christian Joerges, "Social Justice in an Ever More Diverse Union", in: Frank Vandenbroucke, Catherine Barnard and Geert De Baere (eds), *A European Social Union after the Crisis*, (Cambridge UP 2017), 92-119; available at: SSRN: http://ssrn.com/abstract=2697440.

35 References to FS Petersmann and TLT Special Issue.

36 Daniel Innerarity, *Democracy in Europe. A Political Philosophy of the EU*, (London: Palgrave Macmillan, 2018).

37 See the Introduction "Understanding European Complexity", at 7.

> include everyone affected by their decisions in the electoral process and, on the flip side, citizens cannot influence the behaviour of those who are making decisions in their name. This is the principal democratic deficit that the European Union should rectify. Extraterritorial effects and the burdens that one state imposes on others cannot be justified by recourse to domestic democratic procedures and require another type of legitimacy. That is why we can affirm that the fact that national actors keep outside interests in mind may improve the representation of true domestic interests, since they are no longer circumscribed by the state arena either. In this sense, we might think that the EU helps strengthen the democratic authority of the member states, to the extent to which it can serve as a measure to manage externalities in an efficient fashion."[38]

A second one, so it seems to me, is Damian Chalmers' still unpublished essay on the "Democratic Authority and the Resettlement of EU Law".[39] This quest for a resettlement is ground-breaking and much more elaborated than my own: "*EU law allows* [Chalmers departs from Article 2 TEU] … *for another approach in which the European Union's mission become resettled around the promotion of democratic authority within Europe. The central question would be whether a measure has sufficient democratic credentials to warrant obedience over its alternatives, with EU law only justified where it would promote the quality of democracy within a Member State. EU law would, thereby, become an instrument for the cultivation of politics and the values of political community rather than something which suppresses these to secure a policy.*"[40]

The third is a contribution to this conference, namely, Florian Rödl's suggestion to re-orient the jurisprudence of the CJEU from its promotion of the primacy of the economic liberties over the democratic *Rechtsstaat* ("economic constitutionalism" in my parlance) towards a principle of restraint, namely, to respect the limits of European competences" which requires that "the law of the Union does not limit welfare state options at the national level too severely".[41] We will hear more from Florian directly.

Instead of an Epilogue

It may not be so readily apparent how all this is related to the agenda of this conference and to the search for a new future. It *is*, in fact, although certainly not in perspectives which would be shared by everybody. "United in Diversity" is an anti-centralist, con-federal, rather than federal vision, a defence of political autonomy against imposed convergence, combined, however, with duties to co-operative problem-solving. How much realism is in this "united in diversity" vision? It is to be conceded that the *praxis* which this vision envisages certainly depends, to invoke Böckenförde's famous dictum again,[42] on cultural and normative resources, which cannot be produced wilfully or by some political or legislative fiat. European integration research used to be aware of such dependencies and has sought to identify them.

38 See Chapter 3 ("What Should Be Democratized? The Peculiarity of Democracy in Europe", at 73.

39 Ms. Singapore 2018 (on file with author)

40 Ibid., 1 (italics in the original).

41 The "European Pact for Social Progress" Program", at 2.

42 Böckenförde, "Die Entstehung des Staates", .n. 23 above.

THE END OF THE UNIVERSALITY OF NORMS AS A MODEL FOR EUROPE: THE ERROR OF "SEEING LIKE A STATE" (J.S. SCOTT) IN THE POSTMODERN CONDITION

Karl-Heinz Ladeur

Hamburg

1. Universality of Norms and the Emergence of More Complex Markets

The financial crisis of 2008 has exacerbated the differences within the economic systems of the Member States. As one of the less visible consequences of this crisis, there is no longer a paradigmatic market that can serve as model for a European policy of an economic dynamic. This, in my view, is due to the fact that the new market for information services, in particular, is much more complex than the telecommunications market. The difficulties consist in the fact that these new emerging markets do not follow a stable universalising trajectory. *Universality* - as an order building principle - may have had its time in general. The new markets follow a more network-like experimental path of trial and error upon the basis of complex knowledge that is difficult both to access and to use in regulatory strategies. In such a constellation, there is no single trajectory of development that is carved out by a central regulatory agent upon the basis of technology and market observation. The difficulty is exacerbated by the fact that Europe is weak in the development of new computer technologies and software. The "Lisbon Process" which should have brought Europe to the top of technological development has been a complete failure. This drawback finds its repercussions in the missing knowledge base that can only be generated and understood in permanent co-operation with the relevant industries. There is a new tendency towards hybrid public-private interconnected systems or platform markets that undermine the difference between public and private, between customer and wholesale services. In my view, this is not only relevant for the specific markets to which I refer but this also demonstrates for Europe that *universality as a constitutional principle* that extends its effects beyond the economic system has lost at least some of its integrative power. More and more, we are challenged by the rise of "modular technologies" for complex information services that are difficult to assess beforehand and no longer lend themselves to the construction of steady state markets, and, as a consequence, the rather stable regulatory strategies of the past begin to move on slippery ground. At the same time, the interests of Member States are becoming much more heterogeneous. This development requires a more open network-like model of regulation. Technologies develop more within "ecosystems" of different networks that allow for experimentation and do not follow established paradigms of organisation. The focus of the European project should no longer be the super-state, but a more focal model that is meant to push the technological processes of the future, *i.e.*, nano-technology, smart energy technologies, but also the ecological transformation of agriculture, the future of ageing populations, ideas for rural development, *etc.* I think that the ongoing economic and technological transformation of postmodern societies is crucial for the conception of a European constitutional order, as well: universality is no longer a guiding principle for the organisation of regulatory strategies at the level of the nation state, nor for the management of difficult economic questions. Regulation can only follow a trend towards differentiated "network governance". And, more generally, one might take the view that a model of a "consociational governance" is necessary. That is to say, the organisation model can no longer be conceived as uniform and stable for *every* kind of market, but should get involved in regulatory strategies that rely more on a mixture of principles ("*métissage*") and for different types of governance according to the technology or the issue that is at stake. We need more project-like regulatory strategies that are to be formulated by a limited number of Member States according to their interests with differentiated models of action involving private interest groups. Uniformity should not be imposed on Member States that do not consent to potential common strategies.

We need organisational strategies that experiment with the eclecticist "*métissage*" of components of different, even contradictory, political repertories and the management of conflict of norms as a response to the emergence of ill-structured social and economic problems. A paradigm for the latter is the Euro crisis.

Apart from creating worrying problems and the almost unmanageable complexity of an emergency regime (Joerges 2016) that has given enormous power to the ECB, the Monetary Union has also opened the Pandora's box of a transfer union which, to a certain extent, has to be accepted by the northern states. At the same time, the southern states should be more aware of the errors that they themselves have committed in the past: The northern states (not just Germany) are more advanced because of the technological reform of their production and organisation – it is not the myth of the (relative) social dumping of salaries.

The limits to the conception of a universality of rules and principles can also be observed in the field of regulation of other data-driven technologies. Such a regulatory strategy can itself only follow a model of "evolutive networks" (M. Amstutz). Under conditions of uncertainty, stable goals for the regulatory process can only be formulated to a limited extent. Such a strategy is useful in so far as certain risks can be analysed and described beforehand – and these are the risks of the past. This is why, first of all, the internal risk management of firms (financial services in particular) should be strengthened.

2. The Change of Political Causalities within an Incomplete Federal System

All this demonstrates that the idea of a universal order for Europe - or even the world - that is modelled on the example the traditional nation state is outdated. A system like the EU that still follows the "one size fits all" rule is doomed to fail. Universality may work on paper, but, in reality, it deepens the cleavages within the EU. It even creates a perverse expectation of a universal rule that should guarantee equal outcome of different sovereign strategic action. One cannot take the view that it is the construction of the EU that is fine and that the problems are to be attributed to the bad policies of Member States. Once a "union" has been established, a logic that distributes responsibility in a haphazard and irrational way is unavoidable. Despite the different political options left to the Member States, one can, of course, demand a re-distribution of the profits that have been collected unevenly by the Member States. And this is what happens in the European debate. However, this will, of course, meet with the opposition of the richer Member States that will claim that their advantage is due to more intelligent sovereign policy. The incomplete model of the "union" changes the political causalities, which leaves the hitherto established rationality of the nation state behind without having the power to develop a new consistent pattern of the attribution of responsibilities that is characteristic for a federal state with its strong position of the federation. The state of the "union" instead allows for a perverse combination of sovereignty and the claim for a federalist responsibility for the negative consequences of sovereign decision-making. Under the present legal conditions, Member States cannot impose claims for a transfer union on opposing Member States, although they can threaten to "communitise" a factual risk by overburdening the common monetary system even if they themselves will suffer from such a strategy more than other Member States ("raise your neighbours costs"). In my view, the change of political causalities is the most devastating consequence of uniform law that touches Member States in increasingly divergent modes. The implementation of norms needs, first of all, a common idea of its social and technical pre-conditions, and, secondly, a common idea of its implementation, one that is - at least in part - generated in "real time" *ex post*. This approach demands a common knowledge base and an idea of shared political causalities. Causality in politics does not mean an objective factual relationship between input and output. Causalities are more or less social constructions that allow for variation and contestation, but they pre-suppose some form of consensus – which apparently does not exist in many fields of European law. Uniform laws or uniform strategies may even deepen the inequality among the Member States. This is also true beyond economic policy: the German push for a (temporary) "refugees welcome" option probably gave the Brexit votes the one or two per cent that they needed for their victory. The victory of the Polish national-conservative party is also attributed to Angela Merkel's refugee policy.

3. The Role of Social Norms as Opposed to Legal Rules Becomes more Visible

The role of the social norms, the rules of action, the patterns of "how things are done" (Charles Taylor 2004: 55), have all, from the outset, been very different in the Member States, but, for a rather long time, the market regimes have had the power to function as a kind of liberal constitutionalism that has been able to impose a certain level of uniformity and consensus on fragile processes of compromise-finding (cf., generally, Joerges 2016). The rise of economic heterogeneity among the Member States and the deepening of the differences of interests, for example, in the "refugee crisis", while the markets themselves are increasingly fragmenting at the same time; the market regime and the universality of rules in general have undermined the established modes of finding "arrangements" in late-night bargaining processes. This development should not just be reduced to a momentary difficulty. This is a symptom of a transformation that will not pass away within a short lapse of time. It asks for a new *strategy* of a management of diversity also with the EU. Moral appeals will not work.

4. The "Instituted" and the "Constituted Society" (V. Descombes)

Rather, the tenacity of "Seeing like a state" (J.S. Scott) – as opposed to indulging in the observation of the fragmented realities of different *societies* with their own multiple histories that are full of specific hidden intricacies of implicit social norms, patterns of behaviour, forms of life, memories, *etc*., seems to determine the rationale of the EU. The facticity of social norms is characteristic for the "*instituted society*", as opposed to the "*constituted society*" which is based upon explicit (legal) norms. This seems to be a productive distinction that has been introduced by the French philosopher Vincent Descombes.

The idea of progress leads to a superimposition of the forward looking "horizon of expectation" ("*Erwartungshorizont*") on the backward looking "space of experience" (Reinhart Koselleck 2004)). Many of the conflicts over European "constitutionalism" can be explained with a view to the dominance of the "*Erwartungshorizont*" of a new political constitution and the establishment of a new "constituted society": the "*Erwartungshorizont*" can be broadened: it is already less certain that one can give up the "*Erfahrungsraum*" of the nation state and, as a consequence, the nation-based society. However, the nation state cannot be reduced to a nationalist ideology and state-based constitution that can be given up or just fade away. Pierre Manent (2008) has opposed "*la raison des nations*" to the illusionary assumption that we have just to expand the territorial base of the democratic state in order to regain its historical role as rule giving rational power. One might call this the "*acquis étatique*" that, according to observers such as Jürgen Habermas, can be and should be re-established in conditions of globalisation which undercut the state's authority because of the split between its territorial limitation and the unlimited economic networks of transactions. Clearly, Habermas (2011; and others) have a point, but it is only *one* point (for critique cf. Grimm 2016).

"*La raison des nations*", in the sense of Pierre Manent (2008), is not to be interpreted as a nationalist idea that is focused on the nation as an "imagined community" (Benedict Anderson) – a concept that is based upon the constructivist idea that societal imagination is mainly the product of an intersubjective construction. Instead, it refers to a deeper "social imaginary" that consists in the mainly practical "repertory" of decision models, patterns of action, *etc*., in a society (Charles Taylor 2004) – the "instituted society", as one may put it according to V. Descombes (2004). In the market related field of law, co-ordination is, to a certain extent, mainly managed by economic actors themselves, be it spontaneously or via the mediation brought about by the *lex mercatoria* or other self-organised private institutions. However, this looks completely different in fields where co-ordination has to absorb and mitigate much more conflicts such as in industrial relations, administrative action, budgetary discipline, welfare practices, *etc*. In these domains, law - to a large extent - plays a secondary role, as compared to societal norms and patterns of action.

The "instituted society" is, in many respects, regarded by progressive political scientists as based upon power relations – which is true. However, this is not the whole story: it is also a network of societal rules, life forms, patterns of action, which even left-wing political scientist should acknowledge as being characterised by *different* power relations according to "varieties of capitalism" (Peter A. Hall & David Soskice 2001). Clearly, variety matters! Astonishingly, in the controversy over the EU, this matters only for (political) economists. In the "Eurocrats" book, this finds an expression in (political scientist) Fritz W. Scharpf's analysis (2016: 29 et seq.). The economic heterogeneity of Europe is undeniable, but the normative idea of the Eurocrats (including the majority of specialists of European law) pre-supposes a smooth adaptation of weaker states to a more rational form of economic behaviour – naturally, with the benevolent help of the different "programmes" of the EU – this is their "*Erwartungshorizont*".

5. The Unavoidable Difference of European Law in Member States

One of the illusions of the "Eurocrats" – in this case, the term is legitimate – and of the specialists of European law is the assumption that European law is the same in all countries: equal law leads to equal conditions of life, at least in the long run. The possibility that equal law imposed under unequal conditions of life can even deepen differences is discarded. Countries such as Germany and other "northerners" have reacted to the "uniform internal market" by modernising their formal *and* informal institutional rules (e.g., of industrial relations). Countries such as France and Greece have reacted to pressure by expanding their civil service – financed by public debt. This has deepened the heterogeneity between the Member States, as we can now observe. This would be an example for the different "repertories" of political and economic action in Member States.

At the same time, the EU tries to impose a uniform rule of free movement of workers on all Member States in spite of the fact that the social and economic situation is completely different in every Member State: just take the UK with its long history of different waves of immigration, or Bulgaria, whose health system will be confronted with a catastrophe in the near future if the emigration of medical doctors and other qualified people continues at the present rate. One rule fits all? The same is true for immigration. Can and should the "Eurocrats" just force citizens to accept immigration according to the rules? Is "free movement of workers" a dogma that can only be called into question by "exit"? Some Member States might be willing to follow the British example in the future. At present, the situation in the UK is difficult to handle – much more so than the Brexiteers could ever have imagined. Immigration is different in all Member States, in spite of uniform laws. Shouldn't we think about just adapting the law to different social constellations? We should think about more heterogeneity!

6. The Exhaustion of the Simple Market Regime and the Need for New Ideas for the EU

One may criticise the early market orientation ("*Ordnungspolitik*") or the rise of diverse regulatory approaches as being too technocratic and not open to democratic deliberation. However, there was still room for deliberation at a meta-level about alternatives. At the same time, the market regime has at least worked satisfactorily to bring about a certain level of uniformity, and it has, in a way, established some kind of political integration as a side-effect. It has limited the effects of the divergence of the European law at Member State level. It has always been an illusion that the EU suffers from a "democratic deficit". It has been the strength of the EU that it was not supposed to be a super-state. Deliberation alone, that is, without a common "political grammar" (de Ligio 2018), without a common cause, will not compensate for the lack of a common project, and, at the same time, a sense of shared practical life-forms. The emergence of more heterogeneity by the new technological and economic dynamic and other ill-structured problems of postmodernity such as the immigration problems, clearly do not lend themselves to solutions based upon uniform, universal rules. The introduction of EMU, in particular, has completely changed the game: the EU is just stuck in a stalemate, it cannot go on forwards towards more integration (it would be a complete illusion that the treaties can be changed in this respect – and although this could work as an institutional solution), and it cannot stay where it stands. The only possibility that might open a new perspective is, as a consequence, *to take a step back*.

Bibliography:

Amstutz, Marc (2001), *Evolutorisches Wirtschaftsrecht: Vorstudien zum Recht und seiner Methode in den Diskurskollisionen der Marktgesellschaft*, Baden-Baden: Nomos.

Descombes, Vincent (2004), *Le complément de sujet*, Paris: Gallimard.

Grimm, Dieter (2016), *Europa ja, aber welches? Zur Verfassung der europäischen Demokratie*, Munich: Beck.

Habermas, Jürgen (2011), *Zur Verfassung Europas: Ein Essay*, Berlin: Suhrkamp.

Hall, Peter A., and David Soskice (2001), *Varieties of Capitalism: The Institutional Foundation of Comparative Advantage*, Oxford: Oxford University Press.

Joerges, Christian (2016): "Integration Through Law and the Crisis of Law in Europe's Emergency", in: Markus Jachtenfuchs, Damian Chalmers and Christian Joerges (eds), *The End of the Eurocrats' Dream: Adjusting to European Diversity*, Cambridge: Cambridge University Press, pp. 299-338.

Koselleck, Reinhart (2004), *Futures Past: On the Semantics of Historical Time*, New York: Columbia University Press.

Ligio, Giulio de (2018), "Indétermination et stérilité dans la démocratie post-totalitaire", *Le Philosophoire* 2018, Nr. 49, 261-291.

Manent, Pierre (2008), *La raison des nations. Enquête sur la souveraineté nationale et les fondements de la démocratie*, Paris: Gallimard.

Möllers, Christoph (2015), "Krisenzurechnung und Legitimationsproblematik in der Europäischen Union", *Leviathan* 43, 339-364.

Reiling, Katharina (2016), *Der Hybride. Administrative Wissensorganisation im privaten Bereich*, Tübingen: Mohr.

Scharpf, Fritz W. (2016), "The Costs of (Non-) Disintegration: The Case of the European Monetary Union", in: Markus Jachtenfuchs, Damian Chalmers and Christian Joerges (eds.), *The End of the Eurocrats' Dream: Adjusting to European Diversity*, Cambridge: Cambridge University Press, pp. 29-49.

Taylor, Charles (2004), *Modern Social Imaginaries*, Durham NC: Duke Univerity Press.

F JUSTICE DEFICITS AND SOLIDARITY

IS THE EU UNJUST?

Glyn Morgan

(Collegio Carlo Alberto, Torino, and Maxwell School, Syracuse University)

Fans of the EU often forget that the single market is basically just Thatcherism on a continental scale …. It was built by business, for business.

The best trick the Commission ever played was to convince the easily led that the EU is an avatar for diversity, multiculturalism, inclusion and all those fluffy things that appeal to „progressives."

In fact the Commission … realised that those same „progressives" are almost all middle class, and therefore neatly aligned with the interests of big business (being as they are far bigger beneficiaries of it than the working class).

The real losers every single time are the worst off, and of course the countries who lose all of their young (Poland, Romania, Portugal etc). It's a genuine disgrace, and every EUphile on here abusing Brexiters as racists, bigoted etc are a big part of the problem.

"CodeIs4500" [Random anti-EU leftist Guardian Commentator]

In recent years, Eurosceptics have voiced a new type of argument against the EU: it's unjust. The project of European Integration benefits the wealthy at the expense of the poor, business at the expense of labour, liberal cosmopolitans at the expense of conservative nationalists, the Northern European countries at the expense of the South, and the Western European countries to the detriment of the East. The angry post above (from somebody called CodeIs4500) contains the essence of this criticism.

The claim that the EU is unjust – a claim that could be heard throughout the Eurozone Crisis, the Brexit debate, and the recent Italian elections—marks a shift in the focus of Eurosceptics. The traditional complaint of such people was either that the EU was incompatible with national sovereignty or that the EU was insufficiently democratic. The argument that the EU is fundamentally unjust is quite new.

Any adequate response to claims about the EU's alleged injustice requires, I think, a two-fold strategy. First, it is necessary to provide some justification for the project of European integration (Why bother? Why not get rid of it in favour of a Europe of sovereign nation states, as Brexiters and Italian populists demand?) Second, it is necessary to justify a conception of justice within the EU. In an earlier work, I tried to justify the project of European integration in terms of a conception of security (Morgan 2005). The point or purpose of the EU, so I argued, is to make its members more secure, less exposed to domestic and international threats to the basic liberal values that define the European way of life. In that work, I didn't have much to say about the distributive consequences of the project of European integration. Nor did I have anything to say about the duties owed to people who might be wrongfully harmed (if indeed there are such people) in the course of the European project. To address these issues, a conception of justice that includes both distributive and rectificatory components is needed. In this paper, I want to summarize part of an argument that addresses the "justice deficit," as it has been called, of my earlier argument (de Burca, 2015).

My paper proceeds in two sections. Section One restates and updates my earlier argument that the principal justification of the project of European integration is to deliver security for its members. The EU, I argue, is first and foremost a security project; the effort to construct a Single Market regulated by an overarching legal and regulatory system is secondary — a means -- to that end. In order to realize this security project, the EU needs greater state capacity. Section Two examines one argument—that of John Rawls—in support of the claim that a Federal Europe (the very type of Europe needed, I think, to deliver for its members security) is incompatible with justice.

I

The modern history of Europe is a history of violent conflict and war. Wars of plunder and military glory; wars of dynastic succession; religious wars; imperial wars; vastly destructive industrial wars; genocidal wars; wars that lasted one hundred years: Europe has seen them all. And then war stopped--at least on a large scale. One reason, although certainly not the only one, is European integration. The EU was initially envisaged by its Founding Fathers as a Peace Project in the tradition of Abbe de Saint Pierre and others (Bideleux, 2012). The very structure of the EU – Council, Commission, Court, etc.— was taken over from the League of Nations, which Jean Monnet served in the inter-war period as Deputy Secretary General. Even the decision in the post-war era to focus the initial steps of European integration on a Coal and Steel agreement were done with a view to controlling the raw materials that might fuel a military arms race. It's certainly true that after the failure of the Pleven Plan and the European Defence Community in 1952, the history of European integration set in motion by the Schuman Plan (ratified in 1957 in the Treaty of Rome) has been primarily a history of economic integration. But it is important not to lose sight of this alternative track—call it the peace or security track—which, even if it has played a secondary role, has never wholly disappeared and resurfaces in such institutions and policies as the European External Action Service, the Common Foreign and Security Policy, and even the Galileo Project.

From an analytical point of view, it is helpful to have available some categories that allow us to approach the EU as a contested project. People disagree about the importance—both historically and normatively—of the economic and peace or security tracks. Likewise, they disagree—again both historically and normatively—about the process by and through which the post-war project of European integration has (and can) come about. Some maintain that the point and purpose of the EU is and ought to be to produce a market-conforming regulatory system.[258] Others think that the point and purpose of the EU is and ought to be to rescue the European welfare state. It is impossible to draw a normatively compelling justification of the European project out of this contested history. Not only did different states--and political actors within those states--have different goals in mind (Lacroix and Nicolaides 2012). But these goals changed over time. It's a social scientific fallacy to think that the factors decisive in the formation of a phenomenon in one period must be decisive in another.

Notwithstanding the contested nature of the European project, we have to recognize the salient role played by economic processes in driving this project forward. But again merely because the EU relied upon the spill-overs from different forms of economic integration, we should still leave open a space for a normative argument that challenges the salience of this way of making Europe. Perhaps the process of European integration—i.e. the mechanism of European Union formation—ought to be turned over to Europe's citizens, organized as a bottom-up, grass-roots movement. One of the dangers the EU currently faces is that it is so closely tied to the Euro and to the laws governing the Single Market that any threat to the latter endangers the former. In short, we can disagree both about *the project of European integration* (what is its telos?) and *the process of European integration* (how much should we rely upon economic processes?)

So far as the *telos* of the European project is concerned, it is certainly possible to view European integration as a peace project. But peace as a normative value has some significant drawbacks. The trouble with peace is that it can be achieved at the price of independence and influence. Liechtenstein is small, peaceful and without any influence in the wider world. Europe (whether measured in terms of the EU or the Council of Europe) has a

258 The Single European Act of 1986 was primarily the creation of Mrs Thatcher's neo-liberal trade expert, Arthur Cockfield, who was Vice President of the European Commission from 1985-1989.

population and GDP larger than the United States. For Europe to go the same way as Liechtenstein would be a betrayal of, what Max Weber had in mind, when he spoke of the responsibility of a great power (Weber 1994 [1916]).[259]

Embedded in the public culture and shared history of Europe—embedded in the lifeworld, as it were--is a conception of itself as one of the great world Civilizations, a repository of unmatched culture and learning, a distinctive and most pleasing way of being in the world. At the core of the European way of life lies a set of fundamental and universal values, which are nicely captured by Article 2 of the Treaty of European Union:

The Union is founded on the values of respect for human dignity, freedom, democracy, equality, the rule of law, and respect for human rights, including the rights of persons belonging to minorities.

I mention the idea of Europe as a Civilizational power that possesses a distinctive way of life not because I think that this settles anything normatively, but because it provides the ideational framework that any justification for the project of European integration must incorporate—at least if it is to have any persuasive purchase. Partly for this reason, I think it is better to conceptualize the project of European integration less in terms of peace than in terms of security, which envisages an altogether more active role in the creation and maintenance of peaceful global relations.

Security is, as John Stuart Mill noted, the most fundamental and universal of all individual human interests. Without security, individuals can't enjoy any other pleasure (Mill 1860). Mill's claim about security is perfectly sensible so far as it goes. But it doesn't tell us enough about the form of security worth possessing. Here I can do no more than stipulate a position that draws upon the type of security that people today enjoy in Europe. European security has, I think, five dimensions. We are only full secure when all five dimensions are present.

1. An individual is secure when he or she enjoys an adequate range of personal and political rights necessary for liberal democratic citizenship;

2. An individual is secure when he or she has the opportunity to acquire wealth (which I understand in the Smithian sense of "the necessaries and conveniences of life") through the sale of his or her labour, skills, property, and/or products in a well-ordered market economy;

3. An individual is secure, when he or she is guaranteed an adequate level of social welfare (including access to health care, housing, and pensions), which can be relied upon to compensate for the uncertain rewards of the market economy;

4. An individual is secure when he or she has adequate safeguards against violence, whether from individuals, criminal gangs, terrorists, officers of his or her own state, and foreign powers;

5. An individual is secure, only when he or she is not dependent on an arbitrary public or private power.

This barebones account of security begs a lot of questions, including what counts as adequate in (1.), (2.), (3.), and (4.). But probably the most controversial of these five dimensions is the last one. (5.) In some respects, this injunction against arbitrary power is merely a corollary of the first one (1). But (5.) goes a lot further than (1) in recognizing that an adequate range of domestic rights might itself prove insufficient protection against threats to security arising from internati-

259 Weber was, of course, especially in this period, a German nationalist. It is, however, possible to reject the nationalist reasons Weber himself relied upon to justify Germany's world historical role, while accepting that "good states" with the potential to become great powers ought to become so—especially if the alternative is for "bad states" to be the only great powers in the international system. For a discussion of this point, see (Morgan 2018b).

onal society (including foreign powers, whether enemies or allies.) In other words, we need, as neo-Republicans like Philip Pettit argue, "a certain independence in relation to the state; … control of its doings in such a way that [we] are not unprotected in relation to *imperium* or public power" (Pettit 2014, p.77). Yet, as Pettit and other neo-republicans neglect to mention, it's not just our own state that we need a certain independence from; we also need to avoid dependence upon foreign states—including our nominal allies who have very different agendas from our own, whose reliability is questionable, leadership erratic, and prone to swing wildly between isolationism and adventurism.

Notwithstanding the underspecified account given here of security, I want to argue—or, so far as the present paper goes, stipulate—that a European polity (whether a Europe of nation-states, an Intergovernmental Europe, a more centralized Federal Europe) that provides security for its members thereby constitutes "a Good Polity;" conversely "a Bad Polity" fails to provide security for its members. By the same token, I want to argue that members of a Good Polity have duties to each other to support and sustain the conditions of security.

One of the great weaknesses of the EU in its current form is that it lacks any capacity to play anything other than a subaltern role in international affairs. European states depend for their security on an asymmetrical military alliance funded largely by an increasingly reluctant United States. It is widely accepted that the European states need to spend a lot more on their defense capabilities. It is less widely noted that no matter how much money European states devote to this task, the EU is unlikely to be able to play much of an independent role in global affairs without centralizing its foreign, security, and defense policy. The European level of government is in charge of Europe's Agricultural Policy, its Foreign External Trade Policy, and (at least for Eurozone countries) its Monetary Policy. Foreign and defense policy is largely decentralized to 27 member states. This is roughly equivalent to a US Constitution that would allow the 50 state governors the right to veto US foreign and defence policy.

If the EU is to provide Europeans with an adequate level of security, the EU needs to acquire greater state capacity. This is no easy task. I conclude this section with a couple of remarks about state capacity.

The modern state—first conceptualized in the seventeenth century by Thomas Hobbes, albeit a long time before it actually existed in modern Europe—has two components that together constitute a form of impersonal public power: (i) a system of representation; and (ii) a system of administrative infrastructure.

> (i) The system of representation allows the modern state to legitimate itself by way of a myth that the people (the represented) are themselves the authors of everything the state does—it acts in their name. If a state cannot successfully deploy this myth, then it is in trouble. State capacity is thus partly a function of the ability to deploy the myth of popular representation.
>
> (ii) The system of administrative infrastructure allows the state to structure the lives of the people that fall within its boundaries. An administrative infrastructure includes *inter alia* a public bureaucracy capable of extracting revenue, a system of laws and regulations, and some enforcement agencies.

Whether we are referring to (i) or (ii), the EU in its present form is weak—indeed, it is so weak that no one could sensibly describe the EU as a modern state (Morgan 2018a). The EU's system of representation allows only for a mediated form of citizenship. The EU Constitution recognizes as the EU's component entities member states and individuals. We are members of the European Union, only insofar as we are citizens of a Member State. This point is further confirmed by the nature of civic identification within the EU. Most people in most member states think of themselves first and foremost as nationals (French, German, Italian etc.) and only secondarily as Europeans. A lot could be said about the conditions conducive for greater form EU civic identification. But clearly one condition *not* conducive is a widespread belief that the EU in its present form is unjust.

II

One of John Rawls's most distinctive contributions to political theory is the argument that different principles of justice apply to different social and institutional arrangements (Ronzoni, 2009, Sangiovanni 2013). As Rawls put is, "the correct regulative principle for a thing depends on the nature of that thing (Rawls 1999, 25)." This basic idea forms one of the grounds of Rawls's controversial approach to global justice. We owe a lot more to our fellow citizens--indeed, we owe them duties of distributive justice—than we do to foreigners (no matter how poor they might be). Our thing is not, as it were, their thing. This position also helps explain Rawls's surprisingly Eurosceptic position on the European Union. In a passage that CodeIs4500 might well have been proud to have authored himself, Rawls writes (in a letter to Philippe Van Parijs)

One question the Europeans should ask themselves, if I may hazard a suggestion, is how far–reaching they want their union to be. It seems to me that much would be lost if the European union became a federal union like the United States. Here there is a common language of political discourse and a ready willingness to move from one state to another. Isn't there a conflict between a large free and open market comprising all of Europe and the individual nation-states, each with its separate political and social institutions, historical memories, and forms and traditions of social policy. Surely these are great value to the citizens of these countries and give meaning to their life. The large open market including all of Europe is [the] aim of the large banks and the capitalist business class whose main goal is simply larger profit. The idea of economic growth, onwards and upwards, with no specific end in sight, fits this class perfectly. If they speak about distribution, it is [al]most always in terms of trickle down. The long–term result of this — which we already have in the United States — is a civil society awash in a meaningless consumerism of some kind. I can't believe that that is what you want. (Van Parijs, 2003; Morgan 2008).

Although expressed in a personal exchange of letters rather than as a considered philosophical position, Rawls's judgement is fully compatible with the basic idea that the European Union—a Union of different nation-states—is one thing; the United States, a Federal Union, is another. The sting in this observation is the suggestion that if the EU were to move in a Federal direction—to become, in short, a Federal Union--it would acquire the deficiencies, the forms of injustice, that we see in the United States. Rawls's claim here certainly does not exhaust the repertoire of those who allege EU's injustice, whether actual or potential. But it's an important argument—echoed in some respects by Wolfgang Streeck (Streeck 2015) and other Eurosceptics--and deserves a response.

Viewed more closely, Rawls's argument about the EU seems to have not two things in mind-- the nation-state and the Federal Union--but four or even five different things:

- (i) the European nation-state as it now is;
- (ii) the EU as it now is (call it an Intergovernmental Europe);
- (iii) the EU as Rawls fears it might become (call it a Bad Federal Europe);
- (iv) the US as a Federal Union (also Bad);

And lurking in the background—although not specifically mentioned by Rawls--there is:

- (v) A Good Federal Europe

The position that Rawls wishes to defend with respect to the EU might be elaborated as follows:

- (a) We owe duties of distributive justice only (or primarily) to fellow citizens (i.e. members of our nation-state);

- (b) The European nation-state is good insofar as it sustains duties of justice;

And either

- (c) The current Intergovernmental Europe is good, because it supports and sustains the good European nation-state (b);

Or

- (d) A reformed Intergovernmental Europe is good, insofar as it can support and sustain the good European nation-state (b);[260]
- (e) An Intergovernmental Europe—whether (c) or (d) -- is durable in the face of shifting global power relations;
- (f) Any attempt to turn an Intergovernmental Europe into a fully-fledged Federal Europe will lead to a Bad Federal Europe (i.e. a Europe where neither the nation-state nor the Federal level of government will be able to sustain duties of distributive justice).
- (g) There is no realistic possibility of a Good Federal Europe (i.e. a Europe whose members sustain duties of justice).

If this argument were to go through, then Rawls would have a convincing argument against the project of European integration.

There are, I think, four different (although not mutually exclusive) ways of responding to an argument of this type.

> <u>Counterargument One</u>—reject (a). This is the move of liberal cosmopolitans (Caney 2001, 2005). I do not discuss this move here. Instead I will assume that (a) is, for one reason or another, valid. I will also, for the sake of argument, accept (b)
>
> <u>Counterargument Two</u>—reject (c) and (d). Against the claim that the EU in its present form either currently constitutes (or can be reformed to produce) a desirable balance between the nation-state and the European level of governance, it might be argued that an Intergovernmental Europe is inherently flawed and beyond reform.

Streeck (2014, 2015, 2016) comes close to holding this position. Many Brexiters draw the same conclusion. Yet rather than drawing the conclusion that the flaws of an Intergovernmental Europe justify a regression to a Europe of independent sovereign nation-states, it would be possible to accept the premise but draw the conclusion that an Intergovernmental Europe must be replaced by a Federal Europe—ideally a Good Federal Europe (g). In other words, Eurosceptics and Federalists could find common cause in their misgivings about Intergovernmental Europe (whether actual or reformed), but hold very different views of the type of polity that ought to replace it. Federalists must then then find some way of denying (f) and (g). Of course, the Federalist argument raises various difficult questions about feasibility. But there is no obvious reason why Rawls must reject the very idea of a long-term progression towards a European level of government with the kinds of social interaction and cultural similarity sufficient to sustain duties of justice. Indeed, Rawls himself allows that "relations of affinity are not a fixed thing, but may continually grow stronger over time as people come to work together in cooperative institutions" (Rawls, 1999, 112).[261]

260 This is the position, I think, that Sangiovanni (2013) defends. For him, the central task of a normative theory of the EU is to justify a fair distribution among member states of the collective goods that an Intergovernmental Europe produces.

261 Although I can't pursue the argument here in the length that it needs, a similar type of counterargument might be made against Sangiovanni's rich and nuanced argument concerning the status of the current institutional arrangements of Europe (Sangiovanni 2013). Yes, it might be said, the EU in its present form sustains different kinds of social interactions. Yes, they are *at present* denser, richer, and so forth at the national rather than the European level. But there is no obvious reason why this current arrangement cannot (and ought not) change. If I am right about the non-sustainability of this current arrangement; if, in other words, I am right to think that even a reformed Intergovernmental Europe is incompatible with security (as I have defined it), then it would be better to replace this type of Europe with (what I have called) a Good Federal Europe.

Counterargument Three—reject (e). An alternative route to the same conclusion reached in Counterargument Two is to focus attention on (e), the more or less unstated assumption that an Intergovernmental Europe is sustainable in the face of shifting global power relations. This assumption is highly debateable, not least because of some of the problems that Rawls's own argument against European integration mentions. The US is, in his account, a Bad Federal Union, which lacks a fair distribution of goods and is awash in "meaningless consumerism." If those terms exhausted its predicates, then Europe could ignore the United States. The trouble for Europe is that the United States is a hegemon, the bulwark of the global liberal order, and an asymmetrical supplier of Europe's security. More than this, the US variety of capitalism has deeply penetrated European societies, whose individual governments are relatively powerless whether in conflicts with the largest US tech. companies or the US state.[262] The notion that individual European states can gain leverage against this concentrated form of power is a fallacy--call it the Brexiters' fallacy. It is only by acting as a unitary actor--as happens when the EU's Trade Commission acts--that Europeans have any leverage at all.

The difficulty for an Intergovernmental Europe comes when the United States, its protector, becomes unwilling to supply the collective good of European security, a good for which the United States pays a disproportionate amount of the cost. I argued earlier that the EU could only fill this gap by assuming greater state capacity. This will likely entail a transition towards a more Federal Union. If my argument here is correct then we must reject the idea of an Intergovernmental Europe as a stable and secure place. We must by extension reject (c) and (d).

Counterargument Four -- reject (f) and (g). In rejecting (e), we are left with the dystopian possibility that an Intergovernmental Europe (whether actual or reformed) is unstable in the face of shifting global power relations *and* its alternative—some form of a Federal Union—is incapable of sustaining the duties of distributive justice to qualify it as a Good Federal Europe. Are there any grounds to reject (f) and (g)?

This brings me to my (unfortunately rather inconclusive) concluding point.

A Federal European Union will mark a fundamentally different type of polity from the modern democratic nation-state. It will probably be as different from the nation-state as was the nation-state from the early modern dynastic kingdom. If we accept the Rawlsian argument that different types of political association have different regulatory principles, then we can infer that a Federal European Union will have different regulatory principles than the nation-state. I have argued in this paper that in order for a Federal European Union to account as a good polity is must guarantee its members security. Members of such a polity owe each other the duty to guarantee the conditions of security. This duty will have distributive implications, but different distributive implications than within a nation-state.

In the long transition to a Federal Europe—in all likelihood, a multigenerational project—Europe will experience many different challenges to the changes underway. From the point of normative political theory, I doubt that any grand theory can be of much help here, not least because normative arguments need to be pitched at a level of comple-

262 One can gain some sense of the scale of Europe's problem here, when one realizes that the market cap of the top four US internet companies (Google, Apple, Amazon, and Facebook) are roughly 3 trillion dollars—larger than every European member state other than Germany and 60 times greater than the combined value of Europe's top four internet companies (Spotify, Adyen, Zalando, Asos).

xity not too far above the grasp of ordinary citizens. Among the different challenges that will likely need to be addressed are the following.

1. Some people contend that the European project embodies a distinctively liberal way of life hostile to traditional forms of religion and ethnic conceptions of belonging.

2. The challenge from people who seek to secede from a European member state or seek a form of representation within Federal Europe commensurate with that of a member state. We are already seeing demands of this sort, first in Scotland in 2014 and more recently in Catalonia.

3. The challenge from people demanding restrictions on freedom of movement, both within Europe and from outside. This challenge raises the broader question of how far a Federal Europe based on the primary good of security must involve itself in the internal affairs of neighbouring countries in, say, Northern Africa and the Middle East.

4. The challenge from people who contend that the EU's current economic architecture is unfair. In recent years, the central complaint of this nature has arisen in the context of the Eurozone Crisis.

5. A final challenge to consider concerns the range of acceptable ways that a Federal Europe might deploy its trade regulations. In the context of the Brexit debate, a common argument made by Brexiters is that the EU has "bullied" the UK and in its Withdrawal Agreement is imposing a range of so-called Level Playing Field Conditions that will reduce the UK to "a vassal state" (Morgan 2018b).

Bibliography

Bideleux, Robert. 2012. "European Integration: The Rescue of the Nation-State," Dan Stone ed., *The Oxford Handbook of Postwar European History*. Oxford: Oxford University Press.

Caney Simon. 2005. *Justice Beyond Borders: A Global Political Theory*. Oxford: Oxford University Press.

Caney, Simon. 2001. "International Distributive Justice" *Political Studies*. 49: 974-997.

De Burca, Grainne, et al eds. (2013), *Europe's Justice Deficit*, Oxford: Hart

Habermas, Jurgen. 2013. "Democracy, Solidarity, and the European Crisis," *Social Europe* 7 May.

Mill, John Stuart 1861, "Utilitarianism," *Collected Works of John Stuart Mill Volume 10* Toronto: University of Toronto Press.

Morgan, Glyn. 2005. *The Idea of a European Superstate: Public Justification and European Integration*. Princeton: Princeton University Press.

Morgan, Glyn. 2008. "John Rawls: Euro-sceptic? European Integration as a Realistic Utopia" http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1113223

Morgan, Glyn. 2018a. "Alexis de Tocqueville, The Modern Democratic Nation State, and Its Competitors." *The Tocqueville Review*

https://www.academia.edu/36790198/Alexis_de_Tocqueville_the_Modern_Democratic_Nation-State_and_Its_Competitors

Morgan, Glyn. 2018b. "On Brexit, Citizenship and Vassal States."

https://www.academia.edu/37316827/On_Brexit_Citizenship_and_Vassal_States

Pettit, Philip. 2014. *Just Freedom*. New York: W. W. Norton and Co.

Rawls, John. 1971. *A Theory of Justice*. Cambridge: Harvard University Press.

Rawls, John. 1993. *Political Liberalism*. New York: Columbia University Press.

Rawls, John. 1999. *The Law of Peoples*. Cambridge, Mass.: Harvard University Press.

Ronzoni, Miriam, 2009. "The Global Order: A Case of Background Injustice," *Philosophy and Public Affairs* 37: 229-256.

Sangiovanni, Andrea. 2013. "Solidarity in the European Union," *Oxford Journal of Legal Studies* 33. 213-241.

Streeck, W. (2013) 'Vom DM-Nationalismus zum Euro-Patriotismus? Eine Replik auf Jürgen Habermas's', *Blätter für deutsche und internationale Politik* 58(9): 75–92.

Streeck, W. (2014) "'Small-state nostalgia? The currency union, Germany, and Europe: A reply to Jürgen Habermas," *Constellations* 21(2): 213–221.

Streeck, W. (2015) 'Why the Euro divides Europe', *New Left Review* 95 (September/October 2015): 5–26.

Streeck W. (2017). "What about Capitalism? Jürgen Habermas's Project of a European Democracy," *european political science*: 16

Van Parijs, Phillipe (and John Rawls). 2003. "Three Letters on "Law of Peoples" and the European Union," https://cdn.uclouvain.be/public/Exports%20reddot/etes/documents/Rawls-VanParijs1.Rev.phil.Econ.pdf

Weber, Max. 1994 [1916]. "Between Two Laws," in Peter Lassman ed., *Max Weber: Political Writings*, Cambridge: Cambridge University Press.

A EUROPEAN MINISTER OF ECONOMY AND FINANCE: ASSESSING THE COMMISSION'S PROPOSAL AND COMPARING THE POSITIONS OF GERMANY AND ITALY

Tiziano Zgaga

Luiss, Rome

Introduction

The following paper deals with the proposal to provide the EU with a European Minister for the Economy and Finance (EMEF). The EMEF is part of the long debate on granting the EU more powers on fiscal policy,[263] thus aligning integration to the level that has been reached in monetary policy. To complete the economic side of the Economic and Monetary Union (EMU) raises the issue on which institution(s) should be involved in this process. The paper focuses on the proposal, put forward by the European Commission in December 2017, to create an EMEF.

The paper aims to answer two research questions: 1) How to assess the Commission's proposal for an EMEF?; and 2) What is the position of Germany and Italy on this proposal? The paper is divided as follows. The first section re-constructs when the discussion about an EMEF was first launched, which actors pushed it ahead, and how the 2017 European Commission's proposal finally came out. The second section presents the Commission's proposal and the third section evaluates it. The fourth section analyses Germany's position, while the fifth section does the same for Italy. The sixth section assesses the position of the two countries. The last section concludes.

There are at least three reasons why these research questions are important. Firstly, the debate on how to provide the euro area with more fiscal policy competences cannot be separated from the questions of which institution(s) should exercise them. Secondly, the position of two large Member States (MS) – Germany and Italy – that are founding members of the EU and have followed all the steps of integration taken to date, is key to any attempt to reform the euro area. When dealing with EU reform proposals, the literature tends to focus on the contraposition between Germany and France. Thirdly, Germany and Italy are of particular interest because they developed a different reading of the euro crisis. The timeframe of the analysis goes from when the idea of an EMEF first emerged to the positions of the current German and Italian governments.

1. The Proposal for a European Minister of Economy and Finance

The EMU launched in the Maastricht Treaty (MT, 1992) foresaw full delegation of monetary policy to the European Central Bank (ECB). No corresponding supranational institution was established for fiscal policy, which was kept in the hands of the MS. The new policy regime was thus born incomplete, because the euro area had – and still has – one single monetary policy and 19 different fiscal policies. The EU has only a small budget with comparatively few resources (De Feo 2017). Because of this, it is prevented from adopting counter-cyclical policies during times of crisis and, more generally, from fostering public goods that benefit all the MS. European institutions do not have the power or the means to exert a stabilisation function (De Grauwe 2014).

This is why it has repeatedly been argued that the EU needs to become a fiscal union.[264] Fiscal unions can vary according to the tools and competences that are assigned to the centre. They can display different kinds of fiscal capacity. The fiscal power

263 For the sake of brevity, in the paper, I often use the expression "fiscal policy" to refer to "fiscal and budgetary policy".

264 The term "union" refers to a certain relationship that territorial entities (usually states) establish among themselves on the basis of an agreement. Unions have a centre and some constitutive units (states).

of the centre may consist in regulating the fiscal policy of the units (as is the case of the EU) or in managing a budget made up of own resources.

Here is where the debate on the EMEF comes in. The rationale is to create an institution that could manage the EU budget in a more efficient way. The proposal for an EMEF goes hand in hand with the reform of the EU budget. The debate on an EMEF gained momentum with the so-called "Five President's Report" in 2015, in which the Commission called for a stronger president of the Eurogroup, taking into account the possibility of making him or her a full-time president with a clear mandate, *inter alia* representing the euro area on the global stage (European Commission 2015).

In May 2017, the Commission published a "Reflection Paper on the Deepening of the Economic and Monetary Union". It discussed the possibility of a "full-time permanent chair" (European Commission 2017a: 27) of the Eurogroup and of merging it with the Commissioner for Economic and Monetary Affairs and the euro. The paper then deals with a euro area Treasury that "could be placed under the responsibility of an EU Finance Minister, who would also be Chair of the Eurogroup/ECOFIN" (ibid., p. 28).

The debate around the EMEF intensified in 2017, and in December the Commission put its first proposal into concrete terms.

2. The Commission's Proposal for an EMEF

On 6 December 2017, the Commission outlined the rationale, the appointment and the tasks of the EMEF (European Commission 2017b). First and foremost, it specified that the creation of the EMEF would not require amendments to the European treaties. The treaties already allow the Eurogroup to elect a president.[265] The EMEF would be both a member of the Commission (one of its Vice-presidents) and the President of the Eurogroup. Moreover, he or she would have a second intergovernmental role as chair of the Board of Governors of the European Stability Mechanism (ESM).[266]

The Commission stressed that political accountability would be established between the EMEF and the European Parliament (EP). The EMEF would be subject to the same provisions foreseen for the Commission. Regarding appointment, starting with the 2014 EP elections, the *Spitzenkandidaten*[267] system applies. The EP has to grant a vote of consent to the President of the Commission, to the High Representative of the Union for Foreign Affairs and Security Policy (HR)[268] and to the other commissioners. After obtaining the consent, the European Council appoints the Commission by qualified majority (TEU, Art. 17.7). As for dismissal, the EP can also approve[269] a motion of censure that forces the Commission as a whole, including the HR, to resign. The duty to resign also occurs by request of the Commission's President (*ibid.*, Art. 17.6c).

Accountability of the EMEF towards the EP would take place through so-called economic dialogues envisaged by EU legislation,[270] which may also involve hearings in front of the EP. In addition to this, "national Parliaments could request the

265 See Art. 2 of the Protocol Nr. 14 on the Eurogroup. This has been interpreted as if the president should be elected among its members, i.e. should be a national minister of finance. However, according to the Commission, this is part of the informally agreed working methods of the institution and could be changed by simple majority.

266 The ESM is an intergovernmental institution that grants financial assistance to MS in crisis provided they "implement tough reform programmes" (ESM.eu). Currently, the President of the Eurogroup chairs the ESM.

267 When proposing a candidate to the EP, the European Council must take into account the results of the EP elections. Every party presents its candidate for the role of President of the Commission. The European Council must then propose to the EP the candidate of the party that got most votes (seats).

268 The HR is Vice-President of the Commission.

269 In order to be approved, the motion of censure needs "a two-thirds of the votes cast, representing a majority of the component members of the European Parliament" (TFEU, Art. 234).

270 The Six Pack (five regulations and one directive), approved in 2011, states that the EP can start an economic dialogue with other EU institutions (i.e. including single commissioners) on the prevention (Reg. 1174/2011), the surveillance (Reg. 1175/2011) and the correction (Reg. 1176/2011) of excessive macroeconomic imbalances. The EMEF would interact on a regular basis not only with the EP but also with national Parliaments.

Minister to present the Commission opinion on the respective Draft Budgetary Plan to them" (European Commission 2017b: 7).

As the EMEF would be part of both a supranational and an intergovernmental institution, he or she would have a number of tasks. The first would be to represent the common interests of the EU and the euro area. Secondly, the EMEF could support economic policy co-ordination between the MS and the EU institutions, particularly the Commission. It could oversee the implementation of the existing economic, fiscal and financial rules. This entails close co-operation with national authorities and the EP, with the view to promote reforms in the MS. Thirdly, the EMEF could lay down fiscal policy decisions to support and complement monetary policy by the ECB, working to "find a balance between the fiscal interests of the Member States and the best solution for the euro area as a whole" (ibid., p. 4). This also includes co-ordinating the "surveillance of Member States' fiscal policies, ensuring fiscal sustainability and applying the Stability and Growth Pact […]" (ibid., p. 4). Finally, he or she could oversee the EU and euro area budgetary instruments (European Commission 2017b: 7).

3. Assessing the Commission's Proposal

This section assesses the Commission's proposal with the aim of identifying potential drawbacks. Fromage (2018) argues that the three different roles of the EMEF (Vice-President of the Commission, President of the Eurogroup, and chair of the ESM Board of Governors) would limit his or her accountability towards the EP. According to Xanthoulis (2018), the powers of the EMEF are not clearly specified. Most importantly, "the Minister appears not to have authority to adopt decisions, formulate policy or enforce rules" (ibid., p. 10). Concerning external representation, the EMEF would probably have to divide this task with the existing actors that already exert it, *i.e.*, the Commission and the European Council.

The merger between the figure of Vice-President of the Commission and President of the Eurogroup is meant to assure the organic representation of the euro area and the EU (European Commission 2017b). But are the interests of euro and non-euro area countries always coinciding? Not necessarily. If there is a conflict of interest, it might not be easy for the EMEF to mediate. To this, one has to add his or her role as chair of the board of Governors of the EMF, which is to say that he or she has to reconcile differences between the MS on crucial decisions regarding financial assistance programmes.

As Xanthoulis (2018) underlines, the EMEF is not accompanied by an extension of EU competences nor does it transfer of new ones from national to EU level. Hence, from a legal point of view, the European treaties seems not to stand in the way of the Commission's proposal. The fact that the Commission's proposal passed the legal test does not mean that it will also stand the political one. The person elected as Vice-President of the Commission might not be the same that is elected as President of the Eurogroup. Each electing institution might have a veto power depending on who first completes the selection/election process: in the former case, it is the Council, in agreement with the President-elect of the Commission regarding the appointment, the EP regarding approval; in the latter case, the national finance ministers sitting in the Eurogroup.

The Commission proposed the EMEF as a step towards deepening integration after the euro crisis. But what this crisis has proved is that the MS have different perspectives on what they want from the EU. Some are willing to go further into the process of integration. Others want to participate only in the single market (Fabbrini 2015). The way the EMEF is designed does not consider the different perspectives. It follows a one-size-fits-all approach. Although it differentiates between the euro area and the EU as a whole, this distinction is not adequately reflected in the tasks assigned to the EMEF. It is not clear how the EMEF will be able to identify a general interest that fits both the euro area and the non-euro area Member States.

On the one hand, the EMEF might be under political pressure by national finance ministers in the Eurogroup. This is true particularly with regard to the stronger (creditor) MS. On the other hand, the President of the Commission could force the EMEF to resign individually, while the EP could dismiss him or her together with the whole College of Commissioners. Formally, the Eurogroup does not have this power. It could exert it only through political pressure. However, in this case, the President of the Commission and the EP might not agree. As for the appointment, also for the dismissal there will always need to be consensus between the intergovernmental and the supranational side. But this cannot be taken for granted.

The role of the EMEF in assuring compliance with the SGP would be crucial, in particular within the framework of the excessive deficit procedure (EDP). How the function of overseeing and co-ordinating this procedure could be carried out by the EMEP is not clear. Since he or she has a linkage to both institutions involved, but the final decision in the EDP is political, he or she might end up aligning with the relevant actors and find it difficult to bring in his or her own position. In sum, it is unclear how the EMEF will be able to move between different countries and different institutions.

The proposal for an EMEF is not able to enhance the EMU's fiscal capacity towards a complete (i.e. political) union significantly. It must be accompanied by an increase in the EU's own resources. However, it seems unlikely that this process will happen soon, considering the strong resistance in some of the MS. A transfer of more resources to EU level also opens the door to a transfer of further competences. In the light of the different preferences that the MS have on the integration process, only some countries, if any, might agree. But this would show the limitations of an EMEF that should represent both the euro area and the non-euro area countries.

The EMEF would have a sufficient degree of legitimacy for playing a role in budgetary decisions. But the Commission's proposal assigns him or her the task of co-ordinating "the use of relevant EU and euro area budgetary instruments and maximis[ing] their impact in support of shared priorities" (European Commission 2017b: 5). This sentence is quite vague and does not seem to imply real budgetary decision-making powers of the EMEF. In sum, the EMEF does not prove able to solve the situation of "representation without taxation" that currently applies to the EU.

4. Germany's Position on the EMEF

The following section re-constructs the German position on the EMEF. Since the beginning of the euro crisis, Germany has showed "fear of provoking moral hazard and lowering incentives for reforms" (Schwarzer 2018: 50). It has managed to make sure that financial assistance is conditional on domestic structural reforms.

The German position on the EMEF emerged only recently, when the issue entered the debate. In order to infer this position, it is useful to look at the traditional stances of the country towards the EMU. The 2013 coalition agreement states that the allocation of competences in the EMU must follow the principle that the level (EU or national) that takes decisions must also bear the responsibility for them (Koalitionsvertrag 2013). The document is clear in stating that "national budgetary responsibility and supranational, shared liability are irreconcilable" (Konrad-Adenauer-Stiftung 2014: 103).

The then Finance Minister, Wolfgang Schäuble, and the President of the German Bundesbank, Jens Weidmann, argued that establishing a fiscal union was a viable integration process because it would mean that decisions in and responsibility for fiscal policy rests at EU level. However, this implies national transfer of this competence to the EU. The EU could then intervene in national fiscal policy and the MS would ultimately have to comply with European decisions. The alternative would be to maintain national responsibility for fiscal policy and strengthen the existing set of rules (*Der Spiegel* 2012 and Weidmann 2015).

Germany's stance in the first years of the euro crisis was marked by doubts and uncertainty. Actually, the country "did not, for instance, provide any answer or devise an ensuing initiative to the Four Presidents' Report of 2012 […] or the Five Presidents' Report of 2015" (Schwarzer 2018: 51). Angela Merkel is not against an EMEF. She underlined that the question is which competences he or she would have, how he or she would be appointed, how his or her relationship with the other institutions and the MS would be regulated, *etc*. (Bundeskanzlerin 2017).

The 2018 coalition agreement again takes up the traditional view of the country. EMU should (continue to) work through a linkage between risk (in the sense of control over competences) and liability (*Haftungsverantwortung*, Coalition agreement 2018: 9). The document suggests that Germany will also apply its rule-based approach to EMU with regard to the EMEF. It is in favour of an EMEF that controls and supervises MS compliance with the rules of the SGP (Schwarzer 2018). In particular, it wants him or her to have an apolitical role, focusing on the enforcement of the existing regulatory framework.[271] The government is not likely to support the part of the Commission's proposal that foresees the EMEF's use of budgetary resources for countering asymmetrical shocks. The concern that EMU could move from a stability union (*Stabilitätsunion*) to a transfer union (*Transferunion*) is deeply rooted in the Germane élite (see, for instance, Fuest 2018, and König 2018). Both before and during the euro crisis, this concern has been shared by the national central bank[272] and the Federal Constitutional Court.[273]

5. Italy's position on the EMEF

The following section re-constructs the Italian position on the EMEF. As for Germany, Italy's position on the EMEF can be inferred from the country's more general position on the reform of the euro area governance. In turn, this position is also influenced by the country's reading of the euro crisis. Italy has interpreted the crisis as a being caused by abrupt speculative attacks of financial markets. This is why the key aspects of its stance are greater solidarity and risk-sharing at EU level. Increasing the EU budget to promote investments, to support domestic reforms and to absorb asymmetric shocks would probably find the support of any Italian government (right-wing, left-wing, technocratic or populist) (Jones 2018).

In the 2016 document "A Shared European Policy Strategy for Growth, Jobs, and Stability", the Italian government called for a finance minister for the euro area, who should adopt an aggregate fiscal policy and manage the European budget (IAI 2016). Managing the budget would primarily mean creating public goods.[274] The budget should result in a "fiscal capacity based on specific revenue sources as well as a mutualized funding mechanism which could entail issuance of common bonds"[275] (MEF 2016b: 6). The Italian proposal does not assign the role of supervising European fiscal rules to the EMEF.

The EMEF should have a political mandate and should be accountable to EU citizens. He or she

271 Germany criticises the EDP as being too political because, although the process starts following a Commission's recommendation, it is the Council that takes the final decision (Schwarzer 2018). During the euro crisis, attempts to depoliticise the EDP led to the adoption of so-called "reverse qualified majority voting" (RQMV): If, within 10 days, the Council does not reject or amend the Commission's recommendation by RQMV, the latter is "deemed to be adopted" (Reg. 1173/2011, Art. 4.2).

272 See, for instance, Weidmann (2014) and Weidmann (2018).

273 See, for instance, the Lisbon Treaty judgement (2009) and the ESM/Fiscal Compact judgement (2012).

274 Reference is made to "borders, security, large scale investments, defence" (MEF 2016b).

275 This is considered the most "visible and constraining commitment that can convince the markets that member countries are serious about the future of the euro" (De Grauwe 2014: 224).

should be a member of the Commission and have "a strong link with both the European Parliament and Council" (MEF 2016b: 3). The proposal sees the EMEF as chair of the Eurogroup. Institutionally, it would be similar to the High Representative for Foreign Affairs and Security Policy, even though no reference is made to an administrative structure as is the case of the EEAS for the HR. The Italian Minister of Finance and Economy, Pier Carlo Padoan, endorsed the EMEF because the EU needs institutional improvement (*Il Sole 24 Ore* 2017).

As for Germany, the position in Italy of the national central bank (*Banca d'Italia*) was also in line with the government: its governor, Ignazio Visco, argued that an EMEF would have to manage common resources and tools that would differentiate him or her from the Commission. The EMEF should not only vouch for the rules, but also politically interpret them. He or she should manage a common budget, acting as counterparty to the monetary policy of the ECB (*Economia.rai.it* 2016).

After political elections held on 4 March 2018, the Five Star Movement and the League signed a coalition agreement. As in the German coalition agreement, there is no explicit mention of the EMEF. As far as the EU budget is concerned, the parties state that it has to be renegotiated in order to make it compatible with the coalition agreement. The most important part is where Five Star Movement and League affirm that European economic governance has to be changed, together with the other MS. In particular, amendments should be introduced to monetary policy, the SGP, the Fiscal Compact, the ESM and the EDP (Contract for a Government of Change 2018).

6. Germany's and Italy's Position on the EMEF Compared: An Assessment

The last section compares the position of the two countries on the EMEF and tries to see whether at least a common denominator can be identified between them.

With regard to Germany, the analysis has outlined that its stance towards the EMEF is connected with the country's traditional attitude towards EMU. Emphasis is placed on risk reduction, crisis prevention, and solidarity through conditionality (*i.e.*, in exchange for structural reform). In Germany, the debate is centred on the competences that the EMEF should have. In Italy, it is centred on the policies that he or /she could adopt, particularly with regard to the provision of public goods.

Germany would support the EMEF if he or she were to supervise and enforce fiscal rules. The aim is to depoliticise the surveillance of national fiscal policies. The EMEF should primarily be accountable to the German Parliament. The centrality of the *Bundestag* in fiscal and budgetary policies has repeatedly been stated by the German Constitutional Court. The stress on fiscal regulation and supervision (EDP) also implies that Germany would prefer to reform the economic governance of the EU as a whole, rather than deal separately with the euro area.

In contrast to Germany, Italy has different priorities: risk sharing, crisis mitigation, and solidarity in the face of financial turmoil, with less or no emphasis on conditionality. The Italian proposals for the EMEF are referred to the euro area. The idea is that this group of states would be willing to accept institutional reforms because they have already reached a certain degree of integration.

The proposal is centred on the policies that the EMEF could contribute to adopt. Italy wants the EMEF to have some discretionary power in deciding how to spend EU resources. The aim is to politicise this figure with regard to spending decisions. No reference is made to his or her role of supervisor of fiscal rules. The EMEF should relate to national parliaments but its main accountability should be to the EP.

Interestingly, neither of the two strictly opposes further delegation of competences on economic and fiscal policy to the EU. Germany calls for what has been defined a "surveillance model" (Hinarejos 2013: 1634). The Member States hold fiscal policy competence while the EU has regulatory power (Genschel and Jachtenfuchs 2015): it enforces a number of legal rules aimed at constraining the fiscal policy discretion of the MS. Italy calls for a "classic fiscal federalism model" (Hinarejos 2013: 1635). Here, both the EU and the MS retain fiscal policy competence with taxing and spending powers, but in different realms. The EU would retain this competence for the creation of public goods, which is precisely what the Italian proposal states. The MS would keep fiscal competence on those policies/goods that they can better deliver themselves.

The dividing line between the two countries is clearly visible in Schäuble's "Non-paper for paving the way towards a Stability Union": "we must keep fiscal responsibility and control together, to avoid moral hazard" (Schäuble 2017: 1). In the German view, this is the position that applies to any transfer of competences to the European level. If the actor that takes decisions is not the same person who is liable for those decisions, the risk of moral hazard emerges. Why is this position so deeply rooted in Germany? Because it belongs to the German ordoliberal tradition.[276]

The above-mentioned models – surveillance and fiscal federalism – do not fully take account of Germany's approach to the EMEF. More precisely, what the country follows is a model that one could define competence-liability. Germany would agree to an EMEF equipped with regulatory *and* spending budgetary powers only if the MS accepted to transfer fiscal sovereignty completely to the EU *beforehand*.[277] If this were not the case, granting the EMEF the power to make use of resources from the EU budget would mean transferring to him or her liability for decisions taken at national level. For example, he or she could decide to spend EU money to make up for the effects of (profligate) national fiscal policies. This would be equal to a decoupling of control and liability. In the German view, it entails the risk that the EMEF would use common EU resources to compensate for fiscally irresponsible decisions of the MS.

This is why, for Germany, the EMEF should only perform supervisory tasks. The Italian proposal, which is focused on public goods, does not take this "either/or" position between the levels to which a certain competence is assigned. By dividing fiscal policy competence according to the type of goods to be produced, the proposal also implies that part of this competence continues to be exercised at national level. Currently, the MS are not ready to transfer fiscal policy competences fully to the EU. Hence, in the German view, as long as they maintain control of their fiscal policy, they have to be liable for it. If competences and political discretion moved to the EU level, this would imply that the MS have given them up.

Clearly, the German ordoliberal attitude is missing in Italy. The debate over decoupling liability and control does not play the same role in that country.

Conclusions

This paper has analysed the proposal for an EMEF presented by the Commission on 6 December 2017.

The EMEF would be President of the Eurogroup and Vice President of the Commission. He or she would have four main tasks: 1) external economic representation (euro area/EU); 2) policy co-ordination and supervision of fiscal rules (euro area/EU); 3) fiscal policy decisions (euro area); and 4) the overseeing of budgetary instruments (euro area/EU). The EMEF would be accountable to the EP.

While this would not raise legal problems, from a political point of view, there are some critical aspects. To perform three different roles (President

276 The basic idea can be found in Walther Eucken's book *The Principles of Economic Policy* (1952/04). According to the so-called liability principle (Eucken 1952/04), who takes advantage of something, must also bear the costs (*Wer den Nutzen hat, muß auch den Schaden tragen*, Eucken 2004: 279). From this stems that who is responsible for an action, is also liable for it. The rationale is that this should foster prudent decisions. Ordoliberalism is against any decoupling of control from liability. In the EMU control and liability are at national level for economic and fiscal policy and at European level for monetary policy. The no-bailout clause makes sure that this situation remains unchanged.

277 This would also imply that the EU could intervene in national budgets.

of the Eurogroup, Vice-President of the Commission, and also chair of the Board of Governors of the EMF) would not be easy to combine. One the one hand, the EMEF might be subject to pressure from the supranational or, more probably, from the intergovernmental side of his or her role. On the other hand, the fact that his or her tasks are not clearly specified further complicates this point. By making the EMEF the representative of the euro area and the EU as a whole, the proposal does not take clearly into consideration the different perspectives that have emerged on the integration process. Last, but not least, it is doubtful whether it could really contribute to complete the EMU. In the absence of a larger EU budget that he or she can somehow control, an EMEF with no clear defined powers risks undermining the potential of the reform.

Germany's position on the EMEF is in line with its traditional approach to EMU. The EMEF is seen as an institution that should primarily supervise and enforce fiscal rules, with the aim of (further) depoliticising the SGP and the EDP. The country supports a surveillance model. In contrast, Italy sees the EMEF as an institution that should manage a (larger) EU budget in order to face EU-wide asymmetric shocks. The focus is not primarily on the EMEF as the watchdog of the regulatory framework. The country supports a classical fiscal federalism model.

Although, in principle, both Germany and Italy would accept further transfers of economic and fiscal competence to the EU, the real discrepancy between them seems to be the relationship between the level (national or European) that takes decisions and the level (again national or European) that bears responsibility for these decisions. The relationship between control and liability, which is part of the German ordoliberal tradition, is a red line for the country, whereas it does not have the same importance in Italy.

Germany would support an EMEF responsible for European fiscal policy only if competence on this policy were entirely transferred to EU level beforehand. As long as the MS want to retain competence, they must continue to be liable for the consequences of their decisions. If the EMEF were allowed to use political discretion with regard to the EU budget, he or she would be liable for what MS have done at national level. The model that the country supports can more properly be defined as competence-liability.

The German attitude represents a hindrance to the establishment of the EMEF. Completing the EMU can and will not happen overnight. Particular attention has to be given to the composition of the EU budget. The EMEF and the reform of the EU budget must go hand in hand. Because of this, it should also not be faced through an all-or-nothing approach. The focus should be on those parts of fiscal policy where the MS might be willing to give up competences.

That would be as easy as the process would serve the creation of European public goods. Following a step-by-step approach would perhaps make it possible also to preserve the link between the level (EU or MS) that takes decisions and the level (EU or MS) that is responsible for the consequences of those decisions. By doing so, Germany and Italy would overcome what is currently the deepest discrepancy in their positions towards the EMEF.

Selected Bibliography

Bundeskanzlerin (2017). "Strategische Zusammenarbeit vertiefen", available at https://www.bundeskanzlerin.de/Content/DE/Artikel/2017/09/2017-09-15-merkel-empfaengt-philippe.html, last accessed 4 September 2018.

Bundesregierung (2013). "Deutschlans Zukunft gestalten. Koalitionsvertrag zwischen CDU, CSU und SPD"[Coalition agreement], available at https://www.bundesregierung.de/Content/DE/_Anlagen/2013/2013-12-17-koalitionsvertrag.pdf?__blob=publicationFile, last accessed 5 September 2018.

Bundesregierung (2018). "Ein neuer Aufbruch für Europa. Eine neue Dynamik für Deutschland. Ein neuer Zusammenhalt für unser Land. Koalitionsvertrag zwischen CDU, CSU und SPD" [Coalition agreement], available at https://www.bundesregierung.de/Content/DE/_Anlagen/2018/03/2018-03-14-koalitionsvertrag.pdf?__blob=publicationFile&v=2, last accessed 15 June 2018.

De Feo, A. (2017). 'The European Budget: Motor or Brake of European Integration', in: Becker, S., Bauer, M.W. and De Feo, A. (eds.) *The New Politics of the European Union Budget*, Studies on the European Union, Baden Baden: Nomos.

De Grauwe, P. (2014) *Economics of Monetary Union*, Oxford: Oxford University Press.

Economia.rai.it (2016). "Visco, Bankitalia: Un ministro delle Finanze europeo? Sì ma dotato di unico bilancio", available at http://www.economia.rai.it/articoli/visco-bankitalia-un-ministro-delle-finanze-europeo-sì-ma-dotato-di-unico-bilancio/33727/default.aspx, last accessed 15 June 2018.

Eucken, W. (2004). *Grundsätze der Wirtschaftspolitik*, Tübingen: Mohr Siebeck.

European Commission (2015). "Completing Europe's Economic and Monetary Union", available at https://ec.europa.eu/commission/sites/beta-political/files/5-presidents-report_en.pdf, last accessed 5 September 2018.

(2017a). "Reflection paper on the deepening of the Economic and Monetary Union", available at https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-emu_en.pdf, last accessed 5 September 2018.

(2017b). "Communication from the Commission to the European Parliament, the European Council, the Council and the European Central Bank. A European Minister of Economy and Finance", available at https://ec.europa.eu/info/sites/info/files/economy-finance/com_823_0.pdf, last accessed 5 September 2018.

Fabbrini, S. (2015). *Which European Union? Europe After the Euro Crisis*, Cambridge: Cambridge University Press.

Fromage, D. (2018). "The European Parliament in the post-crisis era: an institution empowered on paper only?", *Journal of European Integration* 40:3, pp. 281-294.

Fuest, C. (2018). "Is the Grand Coalition Leading Germany towards a Transfer Union? The Euro Junktim", *ifo Viewpoint* No. 193.

Genschel, P., and Jachtenfuchs, M. (2015). "More integration, less federation: the European integration of core state powers", *Journal of European Public Policy* 23:17, pp. 42-59.

Hinarejos, A. (2013). "Fiscal Federalism and the European Union: Evolution and Future Choices for EMU", *Common Market Law Review* 50, pp. 1621-1642.

Istituto Affari Internazionali [IAI] (2016). "Rapporto sulla politica estera italiana: il governo Renzi", available at http://www.iai.it/sites/default/files/iaiq_17.pdf, last accessed 5 September 2018.

Jones, E. (2018). "Italy and the Completion of the Euro Area", in: J. Erikkson (ed.), *The Future of the Economic and Monetary Union. Reform Perspectives in France, Germany, Italy and the*

Netherlands, Swedish Institute for European Policy Studies, Report Nr. 1, pp. 26-38.

König, J. (2018). "Mehr Transfer als Stabilität? Bewertung aktueller Reformvorschläge für die Euro area", *Argumente zu Marktwirtschaft und Politik*, Nr. 140.

Konrad-Adenauer-Stiftung e.V. (2014). "Shaping Germany's Future. Coalition treaty between CDU/CSU and SPD", available at http://www.kas.de/wf/doc/kas_36853-544-2-30.pdf?140212155238, last accessed 5 September 2018.

Levrat, N. (2015). "The European Union: From International Relations to Intergovernmental Relations", in J. Poirier, C. Saunders and J. Kincaid (eds.), *Intergovernmental Relations in Federal Systems: Comparative Structures and Dynamics*, Oxford: Oxford University Press, pp. 174-205.

Ministero dell'Economia e delle Finanze (2016a). "A Shared European Policy Strategy for Growth, Jobs, and Stability" available at http://www.governo.it/sites/governo.it/files/ASharedPolicyStrategy_20160222.pdf, last accessed 1 September 2018.

(2016b). "Italian contribution on deepening the EMU", available at http://www.mef.gov.it/inevidenza/documenti/Proposal_CL_23_May.pdf, last accessed 4 September 2018.

Official Journal of the European Union (2016). "Treaty on European Union [TEU] and Treaty on the Functioning of the European Union [TFEU]", available at http://europa.eu/pol/pdf/consolidated-treaties_en.pdf, last accessed 5 September 2018.

Schäuble, W. (2017) "Non-paper for paving the way towards a Stability Union", available at https://www.sven-giegold.de/wp-content/uploads/2017/10/17-10-10-Non-Paper-BMF-on-Reforming-ESM-09-10-2017.pdf, last accessed 15 June 2018.

Schwazer, D. (2018). "Germany's approach to euro area reform", in: J. Erikkson (ed.), *The Future of the Economic and Monetary Union. Reform Perspectives in France, Germany, Italy and the Netherlands, Swedish Institute for European Policy Studies*, Report Nr. 1, pp. 49-59.

Il Sole 24 Ore (2017). "Padoan: un superministro Ue darebbe un'accelerazione efficace", available at http://www.ilsole24ore.com/art/notizie/2017-09-15/padoan-superministro-ue-darebbe-un-accelerazione-efficace--093926.shtml?uuid=AEvQ6bTC, last accessed 4 September 2018.

Der Spiegel (2012). "Perfekte Lösungen brauchen lange", available at http://www.spiegel.de/spiegel/finanzminister-schaeuble-ueber-die-geburtsfehler-des-euro-a-840867.html, last accessed 5 September 2018.

Xanthoulis, N. (2018). "The Commission's proposal for a European Minister of Economy and Finance: Institutional empowerment, constitutional tensions and the ministerial taboo", *CERiM Online Paper Series*.

Weidmann, J. (2014). "Die Währungsunion als Stabilitätsunion" (07.04.2014), available at https://www.bundesbank.de/Redaktion/DE/Reden/2014/2014_04_07_weidmann.html, last accessed 18 June 2018.

Weidmann, J. (2015). "Der Euro am Scheideweg zwischen Souveränität und Solidarität" (12.11.2015), available at https://www.bundesbank.de/Redaktion/DE/Reden/2015/2015_11_12_weidmann.html, last accessed 4 September 2018.

Weidmann, J. (2018). "Für Anleihekaufe wäre Enddatum vertretbar gewesen" (07.01.2018), available at https://www.bundesbank.de/Redaktion/DE/Interviews/2018_01_07_el_mundo.html, last accessed 15 June 2018.

RE-SOLIDARIZING EUROPE AND DEFUSING THE CRISIS

Maurizio Ferrera, University of Milan

Carlo Burelli, University of Piemonte Orientale

The very existence of the European Union is today under attack by an increasingly virulent Euroscepticism. In our view, the prime root of this "deep" political crisis is the sharp misalignment between the new nature of the EU after the establishment of EMU, its authority structure, and the normative order which underpins cooperation and the "sharing code" among the member states. Dangerous centrifugal forces feed on the apparent lack of awareness among national and European politicians about the "deep" causes of prolonged instability and existential threats. Yet survey evidence signals that a "silent majority" would be potentially available to support a far-sighted project of institutional reforms and of solidarization of the EU.

EMU as a complex adaptive system without adequate steering

EMU has produced an unprecedented fusion of national economies by bringing to completion the single market and introducing a common currency. When the degree of interconnection and the pressures to mutual adjustment among the parts of a collective goes beyond (or is made to go beyond, as with the formal establishment of EMU) a critical level, such collective becomes a complex adaptive system (CAS). This is the key notion of complexity theory. The emergent properties of a CAS are not merely causally active but become irreducible and irreversible. Irreducibility means that it is virtually impossible to disentangle systemic from sub-systemic causal dynamics: systemic properties are non-localizable and non-aggregative. Irreversibility means that initial conditions cannot be reconstituted via decomposition. The breakup of the euro (strongly advocated by some Eurosceptic parties) would not bring back to life the Greek or Italian economies as they functioned under the drachma or lira. Likewise, Brexit shows that it is very difficult for a Member state to disentangle itself from the EU order and certainly costlier than staying out altogether – or having stayed out in the first place rather than joining and then exiting altogether. As aptly noted by Bauböck, 'the European Union has become in this – prosaic and not at all romantic – sense a community of destiny' (2017, p.33).

Yet, precisely because causal dynamics intersect in complex and chaotic ways, the European Union remains vulnerable to collapse, as each crisis becomes exponentially more difficult to disarm. In complex systems, nonequilibrium is the norm rather than the exception. Steering a complex adaptive system like the European Union is thus difficult and demanding: a change in the policy making mindset is required. Complex systems should focus on resilience, i.e. the capacity to adapt to external and internal shocks even under severe adversity. Contrary to mainstream economics and economic policy - emphasizing equilibrium, determinacy, rule-based deductions - complexity economics recommends 'putting carefully thought-out controls in place' in order to safeguard a systemic resilience based on heterogeneity and dynamic adaptation.

Conceiving the EU as a CAS allows us to better diagnose a prime root of the existential crisis, namely the misalignment between its irreducible properties and its authority structure. The latter is today unsuited to steer the EU qua complex system as it lacks adequate instruments for addressing the common risks generated by integration as such, as well as the negative externalities arising from democratic interdependencies. These flaws make polity maintenance an extremely difficult task, continuously exposed to the risk of existential failure.

EMU is still largely steered within the traditional frame of 'methodological nationalism', i.e. treating the Member States and their political economies as intrinsically self-determined units. But this summation logic can no longer serve as an effective compass (let alone as the only compass) for making policy choices and, even prior to that, for arriving at correct causal imputations. Public policies always suffer from interaction effects which are difficult to disentangle. Yet, with the advent of EMU, interaction effects have grown exponentially: local outcomes have multiple roots and some of them are not local, but systemic. It must also be noted that interaction effects also result from horizontal 'democratic externalities' (Nicolaïdis, 2013, p. 351). Domestic leaders face problems for their own demos which are the consequence - sometimes quite visibly - of other EU demoi's decisions and policies (Cheneval and Nicolaidis, 2016) and, in turn, adopt solutions that are very likely to generate cross-border effects (Bellamy, 2013, p. 505). National self-determination is obviously still possible and can make a great difference in terms of functional performance. But in a growing number of sectors, the separation of responsibilities between supranational, transnational and national actions and dynamics has turned into a difficult balancing act, subject to major epistemic constraints (after a point, we just cannot know).

A second root of inadequacy is that this delicate balancing act is largely performed by non-majoritarian institutions, entrusted with the task of identifying and applying rules and technical formulas for steering national fiscal policies (Chalmers et al., 2016). The belatedly acknowledged challenge of interdependence has been met, in other words, by adopting a technocratic mode of governance based on strict surveillance, discipline and sanctions and aimed at an ever-closer top-down harmonization of the standards and practices of Member States.

The institutional reforms adopted during the euro-crisis have not only proved ineffective in terms of outcomes but have also been eroding the necessary conditions for polity maintenance, unleashing the demons of populism and pushing them into attacking the EU as such: for its lack of democratic representation, its constraining rules on budgetary decisions and its erosion of territorial sovereignty and border controls (Hutter et al., 2016; Kriesi et al., 2012).

A faulty moral order

Aligning the fact of EMU-induced "fusion" in the economic and monetary spheres with an authority structure capable of effective functional steering and polity maintenance requires the mediation of an adequate symbolic framework or, more precisely, a 'moral order'. Moral orders are sets of principles defining 'what is proper to do and reasonable to expect' (Wuthnow, 1989, p. 14) in associational relationships, accompanied by clear normative criteria 'by which people and their activities are valued' (Harré, 1987, p. 219). In the political sphere, a key component of the moral order are principles and criteria about sharing, i.e. what - and why- the members of the collectivity owe to each other. A certain degree of adequacy between such norms and the facts of socio-economic cooperation and institutionalized "togetherness" must obtain in order to buffer legitimation dynamics.

Togetherness evokes ideas such as continuity and compactness: in a word, solidarity (from the Latin term *solidus*, which refers to 'a firm and compact body'). Solidarity is a contested concept, but its prime meaning is relatively straightforward: it connotes, precisely, the set of feelings of belonging together, which supports attitudes of mutual acceptance, cooperation and support. Solidarity in this sense is partially grounded on the interest in the integrity of a shared form of life that includes one's own well-being, which gradually becomes ethically charged and turns into a moral community, whose members feel 'co-responsible' for the actions and desires, faults and merits of each other.

The early architects of the EU were aware that economic integration required a solidaristic ethos to activate mutual feelings of community and sustain EU integration. The *Thomson Report* prepared with the view of establishing the European Regional Development Fund (set up in 1975), stated in turn that a harmonious development of the Community as a whole was a 'moral and human requirement': without sustaining local communities, the 'idea of European unity' would be doomed to 'disenchantment'. In 1977, the European Commission appointed a high-level working group on the budgetary implications of EMU, chaired by Donald MacDougall. The final report suggested that a future 'Federation in Europe' should in principle adopt a public budget of 'around 20-25% of aggregate GDP, as in the U.S.A. and the Federal Republic of Germany', although MacDougall considered 5-7% a more realistic figure in the beginning (as it is known, the EU budget today only amounts to ca. 1% of aggregate GDP). The Report proposed a *Community Unemployment Fund* to cushion temporary setbacks, a budget equalization scheme for weak member states up to 65% of the average fiscal capacity, and a 'conjunctural convergence facility' to counteract cyclical crises (MacDougall, 1977, pp. 12–13). It was through this sequence of initiatives that the 'social dimension' of integration made its silent, but tangible appearance within the EU symbolic and institutional framework and that the value of solidarity – in particular inter-territorial solidarity – came to be a part and parcel of the European 'ethos'.

Contrast this early sensitivity with the current predicament. The transition towards a 'Union of national adjustments' is a dramatic change of paradigm in both descriptive and prescriptive terms. The new outlook assumes that the EMU framework - as currently configured - is essentially well designed and that structural adjustment is fundamentally a matter of homework and rule compliance. The derogatory connotation attributed to the idea of a *Transfer Union* in Brussels and in various Northern capitals testifies to this anti-solidaristic drift of the EU value framework, especially for the Eurozone. The 'myth of the beggar', the idea that solidarity would prevent market pressure and remove incentives to reform has rapidly prompted a de-solidarizing and harshly conflictual polarization between 'deserving' richer and 'undeserving' poorer Member States, saints and sinners, industrious ants and indolent grasshoppers.

Solidarization: how feasible?

The difficulty of further strengthening and solidarizing the EU is often imputed to the shift from 'permissive consensus' to 'constraining dissensus' on the side of national constituencies (Hooghe and Marks, 2009). No common identity, no demos, no electoral room for a political union, let alone a Transfer Union: this is the prevailing line of the reasoning. But can we confidently say that domestic public opinions share this unsolidaristic ethos?

A survey we recently conducted has provided surprisingly hopeful results (Ferrera and Pellegata, 2017). We asked 9326 respondents in six countries (France, Germany, Italy, Poland, Spain, Sweden) to investigate their disposition to support a solidarization of Europe. First, we tested what kind of symbolic image citizens associate to the EU. Four different metaphors were proposed by the survey: 1) the EU as the 'common home' of all European citizens; 2) the EU as an 'apartment building' in which national peoples, with legitimate diversities, live next to each other; 3) a 'playground' (a commons) that facilitates mutually beneficial economic exchanges; 4) a 'sinking ship' from which Member States should escape as fast as they can – the Eurosceptic view. The preferred image turned out to be the apartment building (30.1%), followed by the playground (26.0%), the common home (23.8%) and, finally, the sinking ship (20.3%).

The survey also asked more concrete questions about possible EU policies inspired by pan-European solidarity norms. Almost all respondents (89.1%) agreed that the EU should ensure that no citizen remain without means of subsistence. In addition, more than three respondents out of four were in favour of a specific EU funded scheme to fight poverty.

One may object that people may be in favour of solidarity, but they are not really willing to pay for it. Yet, 77% of respondents were in favour of an increase of the EU budget to support jobless people during a crisis. In particular, the fact that more than two thirds of Germans are ready to support a partial mutualisation of the risk of unemployment is remarkable, considering the reluctance of the German government when it comes to mutualisation policies. In addition, more than three out of four respondents in the six countries were in favour of increasing the EU budget to foster social investment policies (75.9%). By contrast, 'only' 56% supported the introduction of Eurobonds, a percentage that drops to 37.3% if one considers only Germany. Yet, even these numbers mean that potentially one every three Germans is supportive of Eurobonds, a fact which sharply contrasts with the absence of political parties in Germany championing this proposal.

It must also be noted that the results of our survey have been robustly confirmed by other recent investigations (e.g. Gerhards et al., 2017). On this basis, it can be suggested that voter resistance and electoral constraints cannot explain that process of de-solidarization of the EU which we have described above previous section. Quite to the contrary, a 'silent majority' seems to potentially available for supporting a strategy of realignment between the deep togetherness created by the EMU, on the one hand, and the institutional and symbolic architecture of the EU, on the other. The absence of such strategy represents a clear failure of European political elites. An elective (i.e. choice based) partnership such as the EU, based on forward looking objectives, can turn onto fully fledged "familiy of nations" to the extent that their leaders engage in some fraternal nudging. The exercise of 'socioemotional leadership', capable of developing a collective fraternal idioculture has become difficult in a world increasingly based on fluid social relationships, self-seeking behaviours and rational-legal authority (Brint, 2001). But the EMU elite has made long steps in the opposite direction, emphasising difference and apartness between national communities and their governments, denigrating, also symbolically, any mechanism of mutual support, promoting a historically unprecedented rule-based formalization of political authority: almost a deliberate recipe for undermining the conditions of polity maintenance.

Conclusion

In conclusion, the inability to govern the unstable new reality of Europe's irreducible and irreversible integration is alarming. While a polarizing political rhetoric divides Europe's quibbling politicians, there still is a surprising amount of consensus that could be activated by responsible leaders.

In the run-up to the German elections of 2017, Angela Merkel and Wolfgang Schäuble repeatedly stated that in EU politics 'this is no time for visions'. We disagree. As famously argued by Max Weber, world images and visions can sometimes operate as switchmen, channelling historical developments towards new directions. But ideas need political 'carriers'. Today we see some promising ideas with potential popular support, but no available carrier. In this post crisis but still turbulent phase, the long-term sustainability of the EU cannot be taken for granted.

References

Bauböck R. (2017) *Citizenship and Collective Identities as Political Sources of Solidarity in the European Union*, in Banting K. and Kymlicka W. (eds.) *The Strains of Commitment: The Political Sources of Solidarity in Diverse Societies*, (New York: Oxford University Press) 80-106.

Bellamy, R. (2013) *'An Ever Closer Union Among the Peoples of Europe': Republican Intergovernmentalism and Demoicratic Representation within the EU'*. Journal of European Integration, Vol. 35, No. 5, pp. 499–516.

Brint, S. (2001) *Gemeinschaft Revisited: A Critique and Reconstruction of the Community Concept.* Sociological theory, Vol. 19, No. 1, pp. 1–23.

Chalmers, D., Jachtenfuchs, M. and Joerges, C. (2016) *The End of the Eurocrats' Dream: Adjusting to European Diversity* (Cambridge: Cambridge University Press).

Cheneval, F. and Nicolaidis, K. (2017) *'The Social Construction of Demoicracy in the European Union'*. European Journal of Political Theory, Vol. 16, No. 2, pp. 235–260.

Ferrera, M and Pellegata, A. (2017) *Can Economic and Social Europe Be Reconciled? Citizen Views on Integration and Solidarity*, REScEU Working Paper, www.resceu.eu, last access 01/09/2018

Gerhards, J., Lengfeld, H., Ignácz, Z. S., Kley, F. K. and Priem, M. (2018) '*How Strong Is European Solidarity*'. BSSE Working Paper, No. 37.

Harré, R. (1987) *'Grammar, Psychology and Moral Rights'. In Chapman, M. and Dixon, R.A. (eds) Meaning and the growth of understanding: Wittgenstein's significance for developmental psychology* (Berlin; Heidelberg: Springer), pp. 219–230.

Hooghe, L. and Marks, G. (2009) *'A Postfunctionalist Theory of European Integration: From Permissive Consensus to Constraining Dissensus'*. British Journal of Political Science, Vol. 39, No. 1, pp. 1–23.

Hutter, S., Grande, E. and Kriesi, H. (2016) *Politicising Europe: Integration and Mass Politics* (Cambridge: Cambridge University Press).

Kriesi, H., Grande, E., Dolezal, M., Helbling, D. M., Höglinger, P. D., Hutter, P. S. and Wüest, P. B. (2012) *Political Conflict in Western Europe* (Cambridge: Cambridge University Press).

MacDougall, D. (1977) *Report of the Study Group on the Role of Public Finance in European Integration* (Brussels: Commission of the European Communities).

Nicolaïdis, K. (2013) *'European Demoicracy and Its Crisis'*. JCMS: Journal of Common Market Studies, Vol. 51, No. 2, pp. 351–369.

Wuthnow, R. (1989) *Meaning and Moral Order: Explorations in Cultural Analysis* (Berkeley: University of California Press).

SUMMARISING COMMENTS

CONCLUDING REMARKS: ECONOMIC CULTURES AND THE POLITICS OF INTERDEPENDENCE

Visnja Vukov
Universitat Pompeu Fabra

Introduction

Integrating diverse economies and societies under the umbrella of ever wider set of common rules has been a persistent challenge for European integration, from the launching of the Single Market, through the creation of the monetary union, and the subsequent Eastern enlargement. The Eurozone crisis, in particular, has brought the problem of North-South imbalances firmly onto the EU agenda, raising further questions about the economic, but also institutional and cultural, divergence as a source of inherent tensions in integration. The crisis has also fuelled political challenges, with the rise of the Eurosceptic parties in many Member States rendering "united in diversity" an ever more elusive and contentious goal. What are the main aspects of this diversity that matter for the ongoing crisis and how has the crisis affected different economic institutions and cultures in Europe? What are the prospects for political responses that would contribute to enhancing mutual benefits from diversity across Europe, rather than leading to disintegration?

The study of Germany and Italy as the principal focus of this volume offers a great opportunity for exploring these questions. On the one hand, Germany and Italy are paradigmatic cases of Northern export-oriented growth model and co-ordinated market economy *versus* the Southern demand-led model and mixed market economy (Hall and Soskice, 2001; Molina and Rhodes, 2007, Baccaro and Pontusson, 2016). Comparative analysis of these two countries can thus show how domestic institutions and economic cultures mediate their vulnerability to the crisis as well as the political responses to it. Indeed, many scholarly analyses of the Eurozone see precisely the North-South diversity as the key source of the systemic weakness of the monetary union (Hall, 2014; Johnston and Reagan, 2016). At the same time, however, both Germany and Italy are countries with important *internal* diversity, be it the diversity of religious denominations and their associated economic ideas, as apparent in the Protestant and Catholic traditions in Germany, or the diversity in social capital and economic capacities, as apparent in Italy, which itself unites differentially competitive North and South under the same political and economic institutions. The contributions to this volume are based primarily on the discussions of Germany and Italy, but also tackle broader questions of European integration and thus offer numerous important insights for scholarship and practice of politics in Europe. While it would be impossible to elaborate on all of them in detail, the goal of these concluding remarks is to point to some of the most important ways in which this volume advances our current understanding of the economic and political challenges in Europe and opens promising avenues for further research. The paper will be organised around four main themes that emerge from the contributions: the role of diversity in the interpretations of the crisis, the notion of interdependence, the importance of economic cultures, and the politics of crisis responses.

Diversity and the crisis

The causes of the Eurozone crisis have been widely debated in the academic and policy discussions, with positions ranging from placing the blame on the fiscal profligacy of the Southern countries and their weaker governance structures, to the incompleteness of the European Monetary Union with a single currency but multiple states. In comparative politics and political economy, the view that has gained the most attention has been informed by the Varieties of Capitalism (VoC) approach (Hall and Soskice, 2001), and, more recently, the Growth Models perspective (Baccaro and Pontusson, 2016). For the VoC, in particular, one important systemic weakness of the Eurozone stems from the diversity of socio-economic models and institutions governing markets in the North and in the South (Hall, 2014; Johnston and Reagan, 2016). One of the key aspects of this diversity is usually seen in the wage-bargaining institutions, with co-ordinated bargaining in the North yielding higher export competitiveness *vis-à-vis* the lack of such co-ordination in the European South (Höpner and Lutter, 2017, Hancke, 2013, Iversen and Soskice, 2013).

While institutional diversity certainly represents an important aspect of understanding the challenges of monetary integration, the contributions to this volume nevertheless revise this stylised account in several ways. To begin with, the standard image of wage co-ordination between the public and private sector is challenged by Di Carlo (Chapter 3 in this volume). In contrast with the predominant views, his analysis shows that wage restraint in the German public sector does not result from effective inter-sectoral co-ordination or the dominance of the social block concerned with export competitiveness. Rather, it stems primarily from the particular structure of the German federal state. Similarly, public sector wage inflation in Italy has more to do with its role as socio-economic stabiliser and with the dynamics of political party coalitions in Italy, than with the inability of the government or the export-oriented sector to tame the demands of the sheltered public sector employees (Di Carlo, Chapter 3 in this volume. Given that public sector wages are a key element of the overall labour cost differentials in the Eurozone, this analysis provides an important corrective of the VoC based approaches.

Another pertinent question is whether labour costs and the concomitant loss of competitiveness actually represent the most important drivers of imbalances and crisis in the Eurozone. Erik Jones' analysis of the Italian case (Jones, 2018) clearly shows that many of the usual narratives about the crisis do not apply to Italy. Contrary to the widespread image of the lack of competitiveness, high labour costs and excessive public and/or private debt as the problems in the Eurozone South, Italy was pushed into crisis primarily due to the reactions of the financial markets and sudden capital outflows motivated by fears of contagion, rather than by domestic fundamentals (Jones, 2018). Thus, instead of focusing predominantly on domestic socio-economic models leading to imbalances in the Eurozone, it might be more fruitful to examine the implications of financial market integration and the importance of capital account movements. In addition, as Kohl and Spielau argue, wage-bargaining institutions are not the only domestic institutions that matter, as Europe is also marked by the diversity of housing regimes which itself might tilt the economy and capital inflows towards non-tradeable sectors, such as construction, rather than export-oriented ones (Kohl and Spielau, this volume). Academics but also policy-makers hence need to look beyond the focus on competitiveness and especially labour costs as the drivers of imbalances, and, instead, pay more attention to the financial market integration, capital movements and the institutions which govern non-tradeable sectors in order to address the systemic weaknesses of the Eurozone.

Interdependence

A further challenge for comparative analysis stems from the fact that the Eurozone crisis made it very clear that European economies have become deeply interdependent so that the German responses to the crisis cannot be understood without taking into account Italian political and economic dynamics and *vice versa*. Including the premise of interdependence presents a host of conceptual and methodological challenges for comparative analysis, from the adequate choice of the unit of analysis to the selection of a research strategy that could reflect causal processes in the world in which "*no polity can realistically connect cause and effect through its own institutions and policies without regard for the actions of others*"

(Schmitter, 2009: 18). For comparative political economy, taking interdependence seriously would also mean departing from the prevailing methodological nationalism and understanding socio-economic models, such as the German and Italian models, as part of a common and complex system, rather than as self-contained comparative units of analysis.

Many contributions in this volume already take a step precisely in that direction. Ferrera and Burelli (this volume) make a strong argument for conceiving of the EU as a complex system, which is both irreducible and irreversible. Similarly, German export success partly appears as a *result* of the crisis, rather than preceding it, and is also associated with the concomitant return of capital from the periphery to the core, rather than merely resulting from superior German institutions (Manow, this volume). The extent of North-South interdependence is particularly relevant in the illuminating comparison of Germany and Japan, where Japan's experience figures as a useful counterfactual as to what would have happened had Germany not been part of the Euro and the EU. As Estevez-Abe (this volume) shows, Germany's capacity to become an exporting powerhouse was crucially shaped by its participation in the Eurozone. The latter provided additional quasi-domestic markets and prevented the German currency from appreciation, while membership in the EU protected it from bilateral trade negotiations with the US – all the advantages that Japan was not able to enjoy. An important point is thus that *Modell Deutschland* functions as well it does precisely because the other countries in the Eurozone are *not* the same as Germany and because Germany managed to benefit from integration far more than other, in particular peripheral, countries (Ferrera and Offe, 2018).

With Germany and Italy as the focus of this volume, many contributions naturally focus primarily on the interdependence of European North and South, which was particularly strengthened after the creation of the Euro. For Ferrera and Burelli, it is precisely the creation of the Eurozone that set the EU on the path of irreducible and irreversible integration (Ferrera and Burelli, this volume). Yet, as important as the Eurozone and its North-South integration is, one might add that the dynamics of European political economy cannot be fully grasped without taking into account the simultaneous increase of West-East interdependence. 1997, the year of the birth of the Stability and Growth Pact, is, at the same time, the year in which the EU officially decided to start accession negotiations with countries of the former socialist *bloc*. Besides the creation of the Eurozone, the late 1990s were thus also the period in which East European countries became increasingly integrated in the European market and opened their economies towards foreign direct investment – an openness often helped by various aspects of the EU enlargement strategy (Bohle and Greskovits, 2012, Vukov, forthcoming).

This East-West integration has many important implications, both for the North and the South of the Eurozone. As Manow shows, the re-location of German business to the East helped to keep wages under control (Manow, this volume). Furthermore, it also increased the productivity of the German economy through the re-organisation of cross-border production chains. The four Visegrád 4 countries, taken together as a region, is the largest German trading partner, thanks, primarily, to transnational production chains. After the USA, they are also the largest supplier of components for German exports (Poplawski, 2016). The borders of competitive German industry are thus far from coinciding with the borders of German socio-economic institutions.Similarly, the first channel through which the Italian financial system turned out to be vulnerable in the 2008 financial crisis was through its exposure via subsidiaries in Eastern Europe (Pagoulatos and Quaglia, 2013). The map of interdependence among core and peripheral countries in Europe cannot thus be confined to the North-South monetary integration. Rather, it is part of a more complex picture in which North-South coincides and overlaps with the East-West interdependence, and in which monetary union represents only one among several forms of core-periphery integration, each with their own developmental challenges (Bruszt and Vukov, 2018).

Taking interdependence seriously is thus crucial for better theorising about the causes and consequences of the crisis. But it is also necessary for normative reasons – understanding interdependence can lead to different attributions of responsibility for the crisis and is thus one of the key aspects of considerations of justice in the Eurozone (Morgan, this issue). Furthermore, the awareness of interdependence is also a fundamental ingredient of solidarity (Sangiovanni, 2018). Social sciences thus have an important role to play in providing the foundations for such an awareness and in contributing to public debates with insights that would go beyond methodological nationalism.

Economic Cultures

An important innovative aspect of this volume is its focus on the ways in which economic cultures, traditions and predominant ideas shape economic integration in Europe. That markets are embedded in broader social relations and norms is a well-known premise of economic sociology which has more recently received increased attention, especially with the revival of the work of Karl Polanyi. Notwithstanding this, not much has been done to date to tease out what exactly this means for the organisation of markets in Europe and, in particular, for their integration. Hien (this volume) tackles precisely this question with his analysis of the impact of different religious traditions on post-War economic institutions and responses to the crisis in Germany and Italy. The Protestant roots of ordoliberalism with its emphasis on individual self-reliance were instrumental in the German approach to the economic crisis of the 1930s and have also been the backbone behind the conditionality that German leaders required from Southern countries after the Eurozone crisis. On the other hand, Catholic social doctrine condemning the "evil individualistic spirit" and promoting corporatist institutions shaped some of the key elements of the economic order in post-War Italy (Hien, this volume). In addition to cross-national differences in policy *ideas* about crisis responses (Bruno, this volume), the concept of economic cultures suggests that we should explore the ways in which these ideas stem from broader norms, traditions, historical experiences and historically-shaped forms of meaning-making (Hien, this volume). The politics of European integration thus also implies integration of such diverse economic cultures and the key question is how to govern this diversity in a way that would foster co-operation (Joerges, this volume) rather than cultural conflict.

The notion of culture usually implies sort of a *long-durée* perspective – if institutions are sticky, traditions and values are usually seen as even stickier and more difficult to change as they emerge from deep layers of historical experience. Moreover, culture is often assumed to mean *national* culture, nation seen as the most stable and durable cultural community, tied by language, common history, and, in some cases, religion. Yet, the contributions to this volume challenge both of these assumptions. The story of economic culture in post-War Germany is very much the story of cultural change, with multiple shifts and mutual adjustments between Protestantism and Catholicism (Hien, this volume). Similarly, Blome (this volume) brings a fascinating account of changing family values and gender norms in Germany, though not in Italy. Further research would thus need to explore what prompts such cultural change and under what conditions it is more or less likely to happen. Moreover, the papers also challenge the view of monolithic national cultures. Germany managed to successfully combine economic ideas and institutions stemming from both Protestantism and Catholicism, while Italy also seems far from a nationally unique economic culture, as noted already by Putnam (1993) and as apparent in the different implications of corporatism in the North and South of Italy (Hien, this volume). The diversity of economic institutions is also paralleled by the diversity in political choices which again demonstrate a clear divide between the Italian North and South (Kriesi, this volume). An important question is thus what enables more or less sustainable configurations of economic and cultural diversity, and whether Europe could possibly learn something from the experiences of its internally diverse Member States.

The concept of economic cultures, as elaborated in this volume, builds upon the Varieties of Capitalism (VoC) literature but seeks to complement it by showing how socio-economic institutions emerge out of historically specific practices and how they are also embedded in economic ideas, traditions and exercises of "meaning-making". While the contributors here recognise various amendments and criticism of the VoC, one line of criticism which I believe is particularly relevant for the study of Europe is the one developed by Crouch (2005). In his book, *Capitalist Diversity and Change*, Colin Crouch takes issue with the VoC argument of institutional complementarity and consistency as the roads to viable and/or competitive capitalist models. Rather than celebrating neat institutional homogeneity, Crouch argues that it is institutional heterogeneity that facilitates innovation, by presenting actors with alternative strategies when existing paths seem blocked, and by making it possible for them to make new combinations among elements of diverse institutional configurations (Crouch, 2005). Perhaps, the same could be thought of culture: one might even posit that it was precisely the cultural diversity and the possibility of productive cultural re-combinations between Protestant and Catholic thought that contributed to the relative success of German post-War model, either in its more corporatist or in its more liberal version. The key issue for Europe thus remains the question of the forms of governance that could bring about new institutional and cultural re-combinations, and that could foster the appearance of 'institutional entrepreneurs' (Crouch, 2005), capable of using the elements of diversity for creating institutional innovations and fostering new paths. "United in diversity", the famous motto of European integration thus may not be simply about creating conditions for harmonious co-existence of diverse and stable *bloc*s. Instead, it should be thought of as the search for the modes of channelling change (Joerges, this volume) in mutually beneficial, rather than mutually destructive, ways.

Politics of interdependence

How to attain such governance is, of course, a political question *par excellence* and the one that can hardly be answered in a single volume. As Ferrera and Burelli (this volume) argue, the EU has evolved into a complex system, but one which lacks adequate instruments to address the risks of integration and to govern the interdependencies among its Member States. The contributions here point to numerous deficiencies of European governance and several ways in which it has become particularly problematical in the aftermath of the Eurozone crisis. Historically, European integration has been based upon integration through law, which has always had its limitations, visible primarily in the de-politicisation of decision-making. After the crisis, however, the EU has witnessed the shift towards *integration through crisis*, which made it simultaneously less democratic and less legitimate (Scicluna, this volume). Furthermore, Mangold (this volume) argues that the European Commission has increasingly turned from being an "honest broker" towards becoming a political actor, while not being directly politically accountable to the electorate. The problem of accountability is also emphasised by Ferrera and Burelli (this volume), who submit that the structure of authority in the EU suffers from two important shortcomings: it continues to treat the Member States as self-determined units rather than taking the complex interdependence among them into account, and its governance is based largely upon non-majoritarian institutions which function through technocratic surveillance, discipline and sanctioning. While the EU can certainly be seen as a possible means to resolve the emerging democratic deficit of nation-states which are increasingly limited in their policy options because of globalisation and growing interdependence (Joerges, this volume; Innerarity, 2018), it has failed to supplant this deficit with new democratic procedures and forms of governing interdependence at the supranational level. Such authority structure has also helped fuel the rise of populism with citizens increasingly turning against the EU, which they perceive as undermining territorial sovereignty and lacking democratic representation (Ferrera and Burelli, this volume; see, also, Kriesi, this volume).

What are the prospects for changing this kind of dysfunctional authority structure? The papers in this volume offer a mixed picture. On the one hand, the findings show important differences among the German and Italian élites in in how they view the crisis and possible European-level solutions (Puntscher Riekmann and Wydra, this volume; Bruno, this volume; Quaglia, this volume), as well as their mutual distrust (Pellegata, this volume), on the other. Nevertheless, survey results also show that the majority of citizens in Italy as well as in Germany tend to attribute the blame for the crisis to the banks, rather than the excessive spending of the Southern Eurozone members (Pellegata, this volume). In other words, the narrative of Southern responsibility which is predominant in the overall discourse and élite representations of crisis in Germany (Ferrera and Offe, 2018) seems to be endorsed by only one third of the German population. Similarly, the surveys carried out within the RESCUE project show that the majority of Europeans across the Member States are in favour of an increase of the EU budget to support jobless people during a crisis and display a solidaristic ethos when thinking about Europe (Ferrera and Burelli, this volume). Thus, it seems that, at least at the level of citizens, there might be more space for trans-European solidarity and more scope for policies that would go beyond the zero-sum game than is commonly assumed. As Ferrera and Burelli argue, it would, however, require responsible élites who were capable of exploiting this solidaristic capital, which, to date, national political élites seem neither ready nor willing to take up.

What could be done to foster the emergence of political actors who would tap into this solidaristic capital? A useful starting-point here is Sangiovanni's analysis (2018) of the concept of solidarity as being constituted by two parts: recognition of mutual dependence, and the joint action that follows in its wake. While the importance of interdependence has already been mentioned, his discussion also suggests that one of the key distinguishing features of joint action based upon solidarity as opposed, for example, to love, is that we are disposed to share the fate of our fellow man only in ways that are related to the shared goals of our joint action.

> "When we act in solidarity with one another, we take into account only our relation as defined by the ground of our solidarity, and hence *disregard* what else might divide us. What matters is that we are *workers*, not that you are a farmer and I am a factory worker; what matters is that we are *fellow nationals*, not that I am a poet and you are a banker' (Sangiovanni, 2018). [italics in original]

From this point, it seems that one of the key problems with Europe and its current political institutions is precisely that they fail to foster visions and political projects that would enable the creation of trasnsnational relations of solidarity which emphasise aspects of identity *other* than the national one. Solidarity among Europeans where it would matter that they are both workers, rather than a German worker and a Romanian worker; or that they are both feminists, rather than a Swedish feminist and an Italian feminist, is not actively forged in any of the European electoral arenas, precisely because such arenas remain organised around national electoral institutions.

In addition to national democracies and national forms of representation, governing interdependence in Europe might thus also require transnational forms of political representation in which at least some political élites would have stakes precisely in creating new coalitions and forging new solidarities which transcend national boundaries. While this is not an easy task, the alternative that is currently in place is leaving all contentious EU-level issues to the outcomes of national elections and having them debated primarily through the prism of national interest. As we can see in a number of European countries, not least Germany and Italy, such a prism primarily strengthens various strands of nationalism which, in its extreme versions, may also take the form of attacking the basic tenets of liberal democracy. Matching economic integration with the creation of political institutions that could foster polity-building based upon the notion of interdependence, mutual trust and solidarity remains a challenge that Europe will need to resolve if it wants to ensure not only the path of integration, but also democracy itself.

References

Baccaro, L., and J. Pontusson (2016), "Rethinking Comparative Political Economy: The Growth Model Perspective", *Politics & Society* 44 (2): 175-207.

Bohle, D., and B. Greskovits (2012), *Capitalist Diversity on Europe's Periphery*. Ithaca NY: Cornell University Press.

Bruszt, L., and V. Vukov (2018). "Governing market integration and development - lessons from Europe's Eastern and Southern peripheries: Introduction to the Special Issue". *Studies in Comparative International Development* 52(2): 153-168.

Crouch, C. (2005). *Capitalist Diversity and Change*. Oxford: Oxford University Press.

Ferrera, M., and C. Offe (2018), 'Order in the Eurozone: Maurizio Ferrera and Claus Offe in Conversation' VerfBlog, 2018/7/13, available at: https://verfassungsblog.de/order-in-the-eurozone-maurizio-ferrera-and-claus-offe-in-conversation, DOI: https://doi.org/10.17176/20180713-104316-0.

Hall, P.A., and D. Soskice (2001), *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*, Oxford: Oxford University Press.

Hall, Peter A. (2014), "Varieties of Capitalism and the Euro Crisis", *West European Politics* 37 (6): 1223-1243.

Hancke, B. (2013), *Unions, Central Banks and EMU: Labour Market Institutions and Monetary Integration in Europe*. Oxford: Oxford University Press.

Höpner, M., and M. Lutter (2017), "The Diversity of Wage Regimes: Why the Eurozone is too Heterogeneous for the Euro", *European Political Science Review*, pp. 1-26.

Innerarity, D. (2018), *Democracy in Europe: A Political Philosophy of the EU*, London: Palgrave Macmillan.

Iversen T., and Soskice D. (2013), "A Structural-institutional Explanation of the Eurozone Crisis." Unpublished manuscript. Cambridge MA: Harvard University, Department of Government, available at: http://www.people.fas.harvard.edu/~iversen/PDFfiles/Iversen&Soskice_euro2015.pdf.

Johnston, A., and A. Regan (2016), "European Monetary Integration and the Incompatibility of National Varieties of Capitalism", *Journal of Common Market Studies*, 54 (2): 1-19, 318-336.

Jones, E. (2018), "Italy and the Completion of the Euro Area", *European Policy Analysis* 2018:1. SIEPS Swedish Institute for European Policy Studies.

Molina, O., and M. Rhodes (2007), "The Political Economy of Adjustment in Mixed Market Economies: A Study of Spain and Italy", in: B. Hancké, M. Thatcher and M. Rhodes (eds), *Beyond Varieties of Capitalism: Conflict, Contradictions and Complementarities in the European Economy*, Oxford: Oxford University Press, pp. 223-52.

Pagoulatos, G., and L. Quaglia (2013), "Turning the Crisis on its Head: Sovereign Debt Crisis as Banking Crisis in Italy and Greece", in: I. Hardie and D. Howarth (eds), *Market-Based Banking and the International Financial Crisis*. Oxford: Oxford University Press, 179-200.

Popławski, Konrad (2016), "The Role of Central Europe in the German Economy. The Political Consequences." OSW Report June 2016.

Putnam, R. (1993), *Making Democracy Work: Civic Traditions in Modern Italy*. Princeton NJ: Princeton University Press.

Sangiovanni, A. (2018), "Solidarity." Unpublished manuscript. Paper presented at the conference "Responses of European Economic Cultures to Europe's Crisis Politics: The Example of German-Italian Discrepancies", Villa Vigoni, 25-27 June 2018.

Schmitter, P. (2009), "The nature and future of comparative politics" *European Journal of Political Research* 1 (1): 33-61.

Vukov, V. (forthcoming), "Europeanizing development: EU integration and developmental state capacities in Eastern Europe", in: M. Matlak, F. Schimmelfennig and T. Wozniakowski (eds.), "Europeanization Revisited", EUI – RSCAS Working Paper Series, European University Institute (EUI), Robert Schuman Centre of Advanced Studies (RSCAS), Florence.

TWO ANNEXES

ORDER IN THE EUROZONE: MAURIZIO FERRERA AND CLAUS OFFE IN CONVERSATION

Maurizio Ferrera, Claus Offe

MF: You have recently written a lot about Europe and the increasing North-South divides within the Eurozone. You are also one of the few influential German intellectuals who openly criticizes German governments and their orientations on EMU. Do you see a nexus between the EMU's dysfunctionalities and the social and political crisis, especially in Southern Europe?

CO: Yes, I certainly do. The monetary regime of the Euro under which 19 very diverse national economies within the EU now live and operate is plainly dysfunctional. It does not serve its alleged and promised purpose of convergence but does the exact opposite. It is economically and politically divisive: Some participants win, others lose and the gap becomes wider.

The Euro ties the hands of the losers, roughly the Mediterranean region of the EU. They can no longer adjust to challenges of competitiveness by devaluing their national currency because there is none any more. If they need to adjust, they must do so „internally", i. e. by depressing wages, pensions, and state (in particular welfare) expenditures, all of which is detrimental to growth, employment, and the prospects of reducing public debt through a fiscal dividend resulting from growth. Today, Italian GDP per capita is still 8 per cent below of what it was in 2008. Yet that does not seem to be enough to boost Italian unit costs of labor, the key determinant of competitiveness in international trade. The living conditions of ordinary people have been severely depressed, giving rise to discontent, resentment and angry if often misdirected protest. Loser economies are no longer allowed, under the EMU regime, to set their targeted rate of inflation because that is done by the ECB. At the same time, the extremely low interest rate, also determined by the ECB, benefits the winners by making their public debt easier to service. For instance, experts speak of 294 billion Euros, a figute that comes close to an annual Federal budget, that the German public debt burden has been made lighter since 2007 through low interest rates. Another way in which the Euro benefits winner countries is that it works as an export subsidy due to its uniform external exchange rate. Absent the Euro, the new Deutschmark would dramatically appreciate its exchange rate with the outside world and German export industries would largely collapse as a consequence. No wonder that winners such as, most of all, Germany indulge in their obsessions with automatic rules and austerity. Yet the German government does not show any inclination to share this windfall profit with those whose plight has indirectly given rise to it. This all looks like what the Hungarian-born historian Karl Polanyi, referring to the "veritable abyss of human degradation" that occurred under early capitalism, has called a "satanic mill". One feature that makes the mill particularly „satanic" is the fact that nobody, neither losers nor winners, can rationally (and actually does in earnest) opt for leaving the Euro. Unilateral exit from the EMU is, in spite of some demagoguery to the contrary, a plain non-starter due to the huge damages exiteers would have to cope with as a consequence. Unless there is a way to reform and to some fair compensation of losers, we remain trapped in the „mill". Yet the longer it operates and inflicts damages on losers and grants profits to winners, the harder it becomes politically to embark on a serious path of reform that opens a credible prospect of convergence. Such reform, together with winners funding large scale border-crossing investments programs, remains the only collectively rational way out. But for charting such path time may be running out.

MF: This logic was partly there from the beginning of EMU. Don't you think that some institutional reforms introduced in the early 2010s – such as the Fiscal Compact, the strengthening of supranational *controls and conditionality, the adoption of democratic "monsters" such as reverse qualified majority rule for macro-economic and fiscal decisions – have severely aggravated EMU's dysfunctionality?*

CO: Absolutely. The new tools of enforcing „discipline", austerity and control are widely recognized to be counterproductive in their effects. But they are the only tools the EU, driven by a constant and no doubt realistic fear of the disasters the „markets" may inflict upon its stability, has at its disposal and which are within the reach of the intergovernmental making of treaties between EU member states. They confirm the image of „Brussels" as an illegitimate foreign power imposing rules without being itself subject to democratic accountability. We now have a rich evidence in Europe of the electoral outcomes to which this economic and monetary regime gives rise. The EU lacks the requisite state capacity to deal with the partly disastrous consequences caused by the operation of its monetary system. If the EU were a federal state, and a democratic federal state at that, it would have at its disposal the governing capacity to tax and to redistribute its resources across state borders and compensate losers for at least parts of their systematically generated losses. In its present institutional shape, it is still far from having the authority to do so.

MF: The obvious question is then: cui prodest? Who are, let us name then, the EMU winners? And do you think there was a deliberate power strategy?

CO: As I said, Germany has been the main beneficiary of the institutional architecture and measures that were put in place since 2008. That fact need not be due to what you call a „deliberate power strategy" or conspiracy of sorts. Power, as political scientist Karl Deutsch has famously pointed out, is the ability to afford not to learn. In that sense German power consists in the unwillingness of German political elites (as well as, it must be added, major parts of ill-informed non-elites) to promote and adopt reforms needed to remedy the worst institutional pathologies of the EMU. Such reforms are not only affordable for one of the biggest and currently one of the wealthiest economies of the Eurozone; they are even dictated by its long term and well-considered interest in making the EMU a robust and inclusive monetary regime.

MF: As the largest Member State and as the economic powerhouse of Europe, one would expect Germany to somehow serve as a benign hegemon, capable of reconciling her own national interests with the interests of others and especially with the long term economic and political sustainability of the EU

CO: During the long crisis Germany has in fact largely abdicated its responsibility in and for Europe. The German government's obsession with rules, austerity and conditionality has been the main driving force behind the growing divergence of EMU economies and the devastating social shocks which has hit Southern member states. Germany has tried to push through her own economic and social model, based on flawed assumptions that we might call a „flower pot theory". Such theory is the favorite mode of thinking of winners. Their message: the rules that have worked so advantageous in „our" case are the same that would work to the benefit of „you" as well – if only you could overcome yourself to follow „our" rules which you are most welcome, in fact required, to adopt and follow. Flowers in separate flower pots develop similarly if you use the same seeds, the same fertilizers etc. What is wrong with this comfortable mode of thinking is that it ignores and denies systemic interdependence. However, there is a powerful intellectual antidote. It is captured in a sentence by authors Mathijs and Blyth, often quoted in the scholarly literature on the EU. It reads: „The Eurozone as a whole cannot become more like Germany. Germany could only be like Germany because the other countries were not." Germany is like Germany, we might add, because of its reaping of unreciprocated advantages from the system of EU member states and their interdependencies – the opposite of separate flower pots.

MF: In the flower pot theory a key role is played by rules and decision making procedures. The motto of German and Northern elites during the crisis has been pacta sunt servanda. That is fair enough. But Roman law foresaw an additional clausola rebus sic stantibus: treaty obligations can remain unfulfilled due to a compelling change in circumstances. Only the jus cogens based on basic principles was peremptory, with no possibility of derogation….Can we say that such rather obvious distinctions have been forgotten during the crisis – or possibly even in the original design of EMU?

CO: This question takes us into the difficult field where we must explore the relation between rules and decisions. Rules of social and political life are not in any sense „given"; they are man-made and have been adopted at some point by decision. Following rules as a matter of routine can be a highly efficient way to avoid the need to make decisions. But social agents can also decide to break rules rather than comply with them, and sometime there are even good and justifiable reasons for doing so, e. g. when the rebus sic stantibus proviso does not apply. For instance, the rules may be biased and favor one of the conflicting parties to which they apply. Nota bene: uniform rules do not create a level playing field. Absent such reasons, there are reasons to enforce rules. But efforts at enforcement can fail, or it can involve the violation of other rules. It all boils down to the issue of how we judge the quality of those respective reasons. This conflict may be resolved by bending or temporarily suspending rules in order to avoid having to break them, or by reforming them. Insisting on rules being valid once and forever can be an attitude that is driven by self-interest of those whom the rules favor rather than an attitude inspired by sincere respect for the rules. As we easily recognize, each of these ramifications play a role in the day-to-day discourse and conflicts over European integration and Eurozone politics.

MF: Another shibboleth of neoliberal doctrine is that we cannot separate control and liability: whoever decides to do something must be solely held responsible for its consequences. This is simply poor sociology. In a complex system such as EMU is it still possible to determine with any politically relevant precision those effects which can be traced back to domestic policy decisions and therefore implicate national "responsibility"? Moreover, it is in the nature of all social interaction that we are not rewarded for all positive effects we cause for others, nor are we bound to compensate others for all the negative externalities we cause for them. Of course I am not denying that there are numerous policy areas in which domestic decision still make the difference and therefore do implicate national responsibility. And we know that some governments even cheated Brussels when the crisis erupted. But don't you think that the rhetoric of "saints" and "sinners" espoused by German leaders (including social, media and intellectual elites) has grown beyond limits of epistemic, moral and political acceptability?

CO: I couldn't agree more. Again, the questions takes us into the field of legal philosophy. To what extent can actors alone be held responsible for the misfortune they suffer or the gains they achieve? Again, winners tend to ascribe their profit to their own talents and efforts, while losers like to frame themselves as victims of adverse circumstances. Winners depict losers as having failed to obey the commands of prudence and moral consistency, while losers look at winners as having benefitted from sheer luck or the uncompensated help of others. These conflicting narratives must be checked case by case for their relative merits, and care must be taken that the narratives of winners do not prevail over other narratives and frames, as they often tend to do in the multilingual and hence fragmented public sphere of the EU.

The German framing of the problem of the EMU and the EU is often described and criticized as an obsession with „order". In fact, the economic policy doctrine of „ordo liberalism" that was canonized by committed protestant professors and politicians in the early post-war period of the Federal Republic is inspired by the deep intuition that a stable and robust social order is best built when rules are irreversibly put in place and decisions and discretionary interventions – be it by corporate actors or political authorities – are banned or kept to a minimum. This doctrine has always reminded me of a story told by Bertolt Brecht in his collection of anecdotal sketches called *Flüchtlingsgespräche* (conversations of refugees [from Nazi Germany in the 1930s]). One is a physics professor, the other a metal worker. The latter concludes their conversation on the nature of order by musing: „We might put it this way. Where nothing is in its right place, there is disorder. Yet order is where in the right place there is nothing." The professor agrees: „Order is a phenomenon of something missing." Just to illustrate: As reported in a recent comment in the *Financial Times* (May 6, 2018), one paragon of fiscal probity and austerity, namely Nicolae Ceausescu, the Romanian dictator, boasted a budget surplus of 9 billion dollar in 1989. By the end of that year, his regime had suddenly collapsed and he was no longer among the living.

GERMANY IS QUIETLY REBALANCING ITS ECONOMY – BUT THIS WILL NOT FIX THE EUROZONE'S FLAWS[278]

Donato Di Carlo[279]

Max Planck Institute for the Study of Societies, Cologne

Ever since the financial and sovereign debt crisis, the political and economic implications of Germany's unbalanced economy have lured the attention of academics, policy institutions, the public and politicians across Europe and beyond. Frequent are the pleas made to the German political establishment to rebalance its export-oriented economic model, increase fiscal expenditures and thus rein in the world's largest current account surplus. The issue has become so controversial that one reads economic commentators venturing into picturesque appraisals, comparing today's Germany to Nicolae Ceausescu's Romania.

But what is Germany being criticised for? In essence, the controversy revolves around macroeconomic policy making and what the German growth model implies for the rest of the world. There are four constitutive elements in this debate. Two pertain to the sphere of macroeconomic policy proper, i.e. wage and fiscal policy. One has to do with an empirical manifestation of macroeconomic policy in the German balance of trade, i.e. persistent current account surpluses. The last criticism is centred on the growth model itself and considers the implications of the German export Weltmeister for the European Economic and Monetary Union (EMU), as well as global imbalances). In what follows I focus *solely* on the EUROpean perspective and leave the issue of global imbalances to others.

Germany's 'unbalanced' economy and the EMU

German policy makers, the argument goes, should rein in the country's trade surplus and allow for symmetric adjustments in the EMU. Germany is accused of engineering economic growth at home by free-riding on other European countries' aggregate demand. Some even go as far as to argue that Germany is "artificially" and "purposefully" repressing domestic household consumption, government spending and private investments to sustain a *mercantilist model*. Germany allegedly refuses to correct trade imbalances and – given fixed exchange rates – grows at the expense of other EMU participants, which have to go through painful internal devaluations and fiscal austerity. What is thus being asked of Germany is to reduce its budget and trade surpluses to provide a more symmetric adjustment mechanism to the single currency via the expansion of its domestic demand for EMU exports.

In the eyes of the critics, Germany's increased imports are thus supposed to work as a functional equivalence for the lack of supranational adjustment mechanisms in the monetary union. In other words, Germany should act as a *fixer of last resort* in the Eurozone and, to fulfil this role, domestic macroeconomic policy should follow suit. Since participating in the EMU entails a loss of sovereignty over exchange rate and monetary policies, both criticism and policy advice focus on wage and fiscal policy.

278 This piece has originally appeared, in the form of a blog post, on the *LSE Europp Blog* on 14/9/2018, available at: http://blogs.lse.ac.uk/europpblog/2018/09/14/germany-is-quietly-rebalancing-its-economy-but-this-will-not-fix-the-eurozones-flaws/, and on *Social Europe* on 20/9/2018, available at: https://www.socialeurope.eu/germany-is-quietly-rebalancing-its-economy-but-this-will-not-fix-the-eurozones-flaws.
The version presented here has been slightly modified with respect to the original blog post in order to incorporate critiques and suggestions.

279 I am grateful to Benjamin Braun, Sebastian Diessner, Martin Höpner, Fritz Scharpf and Jachim Truger with whom I had the chance to discuss these issues to refine my thinking. All mistakes are my sole responsibility.
I am especially thankful to Dr. Paul Steinhardt who has written a thoughful critique to my original piece. This has helped me substantially to refine my thinking and correct initial mistakes I had committed. His critique has appeared as a blog post (in German) on the *Makroskop blog* on 28/9/2018, available at: https://makroskop.eu/2018/09/wissenschaftliche-sensation-deutschlands-stilles-rebalancing-wurde-entdeckt.

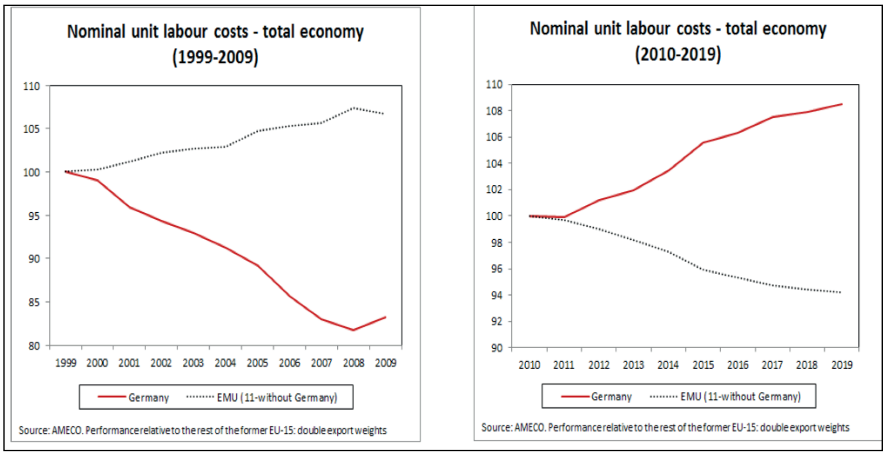
Let's start with the criticism. People concerned with wage policy argue that Germany has undergone a substantial internal devaluation of its unit labour costs (ULCs): wages have fallen behind the economy's productivity rates in both the private and public sector, thus yielding a cost and price competitiveness premium to the German export secto rbest captured by its remarkable ULC-based Real Exchange Rate (REER) depreciation. Those who point at fiscal policy stress the German budget surplus, bemoaning the lack of government spending. Deflationary wage policies (decreasing real wages) are said to deter household consumption at home and imports from abroad. An austere fiscal policy contains the government's final consumption and contributes to keeping imports artificially low. At any rate, the combination of a restrictive wage and fiscal stance represses total domestic demand (public and private), leads to relatively low inflation, REER competitiveness and trade surpluses – which prevent the possibility for other EMU participants of adjusting via an export-led recovery.

Now the policy advice: what should Germany do? Policy remedies follow consistently from the critiques. ULCs in Germany should rise faster than its competitors' so as to experience an appreciation of its REER and hence a loss of the competitiveness (unfairly) acquired before 2008. Additionally, the German government should spend more money. The effects of this policy mix would set in motion two complementary mechanisms for adjustment. On the one hand, the wage and price inflation deriving from higher wage rates and an expansionary fiscal stance will decrease (ULCs- and CPI-based) REER competitiveness and help rebalance the current account – allowing other EMU countries to "breathe". On the other, increased households' purchasing power (due to higher real wages) and government consumption will increase domestic demand and imports from abroad.

What has Germany done since the crisis and what can it possibly do, given the institutional setting?

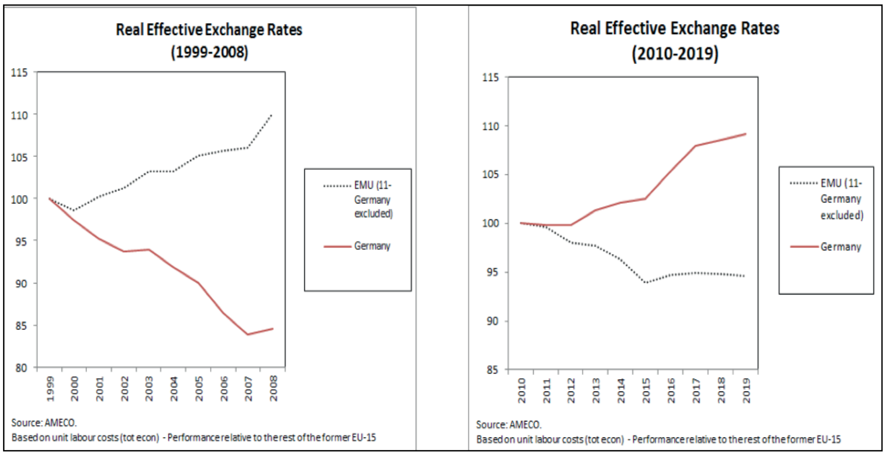
In general terms, the criticism on such a high current account surplus is certainly valid. Yet, what the critiques have in common is that they rarely ask what Germany has done since 2010 to address these issues. It thus seems appropriate to ask whether the trends of wage restraint and fiscal austerity, visible before 2008, have been reversed in the post-crisis era or whether Germany continues to "beg her neighbours".

Figure 1: Unit labour costs: total economy (1999 and 2010=100)



ULCs in post-crisis Germany (figure 1) have increased steadily. Since 2010, the trend of internal depreciation so much pronounced during 1999-2008 has been reversed and Germany has undergone a substantial REER appreciation (figure 2) vis-à-vis its EMU peers, forced into a path of internal devaluation. The REER competitiveness gained in the pre-crisis period has not been fully reabsorbed yet. Still, the trend has clearly reversed.

Figure 2: Real Exchange Rates in Germany and the EMU (1999 and 2010=100)



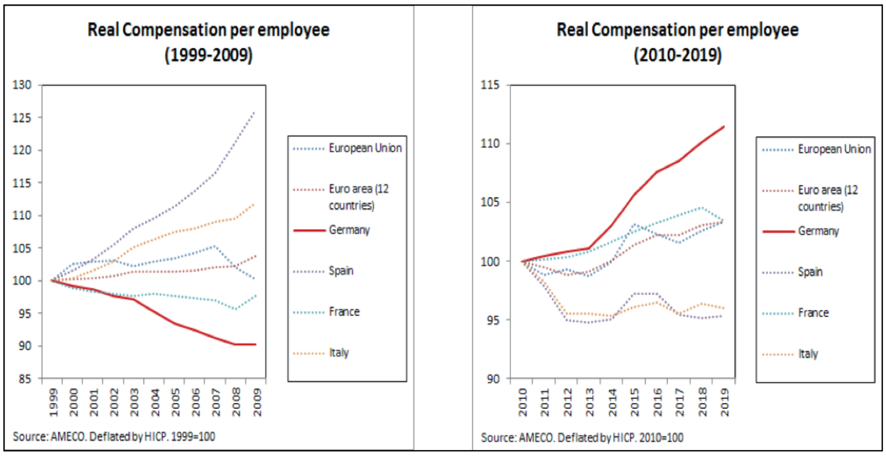
Surely, criticising Germany for its own sake may lead to one always ask "how much is enough". This would perhaps be a fair question given the remarkable pattern of wage restraint observable before the crisis. But a constructive and – *realistic* - critique should go beyond a mere numerical macroeconomic argument and include institutional structures in order to elaborate on the feasibility of an extraordinary internal appreciation, given the German wage setting systems.

Tarifautonomie allows for no government interference in private sector wage negotiations and, frankly, it sounds quite absurd to expect the German government to ask the social partners to *price themselves out of the market* in order to purposefully lose competitiveness *vis-à-vis* its EMU peers.

Regarding public sector wage setting, after the reforms of the mid-2000s it is now the finance ministers of the *Länder* who are in charge of negotiating wage increases for the public employees they are in charge with, i.e. the majority. Given that the *Länder* lack the possibility to manipulate their marginal tax revenues - and that personnel pay is the most burdensome item in State administrations' books (approx. 45% of total expenditures)- it would be pointless to expect substantial wage increases in the TV-L contract without a fiscal federalism reform that attributes more money to subnational governments. Even more fundamental is that it is unclear why one should expect the finance minister of a German State to respond to Eurozone imperatives, while being accountable to their local constituency.

The only instrument the German government could use to intervene in wage-setting is to legislate for an increase of the minimum wage above inflation. This has already been agreed and the government is about to ratify an above-inflation increase of 4%.

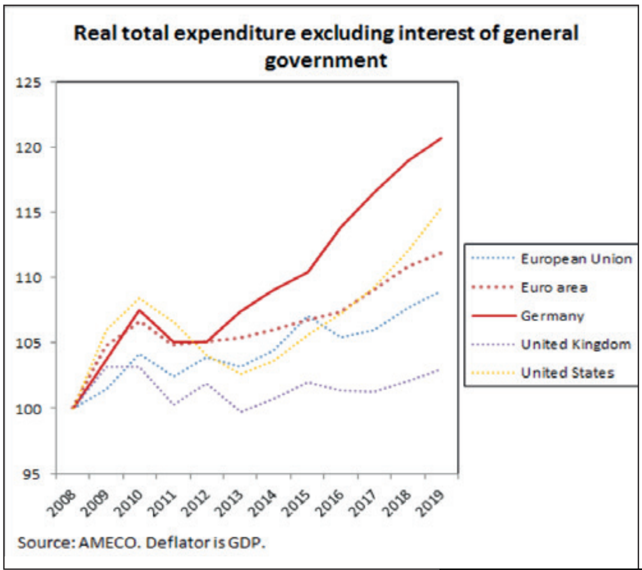
Figure 3: Real Compensation per Employee, deflator is HCPI (1999-2019)



Even assuming that it would be structurally possible to raise German price inflation far above the EMU average via wage push inflation, this is likely to create more damage than relief. Given Germany's size in the EMU, it will rather put enormous political pressures on the soon-to-be new governor of the ECB to tighten monetary policy. The effect for the EMU would be the opposite of the desired symmetric adjustment: countries in the periphery would be pushed into even direr straits.

What about the German finance ministers, are they really so stingy? In terms of real government expenditures (net of interest payments), Germany has since the crisis spent considerably more than most other OECD countries, even more than the increase in spending in the United States – often praised for its post-crisis Keynesian stance.

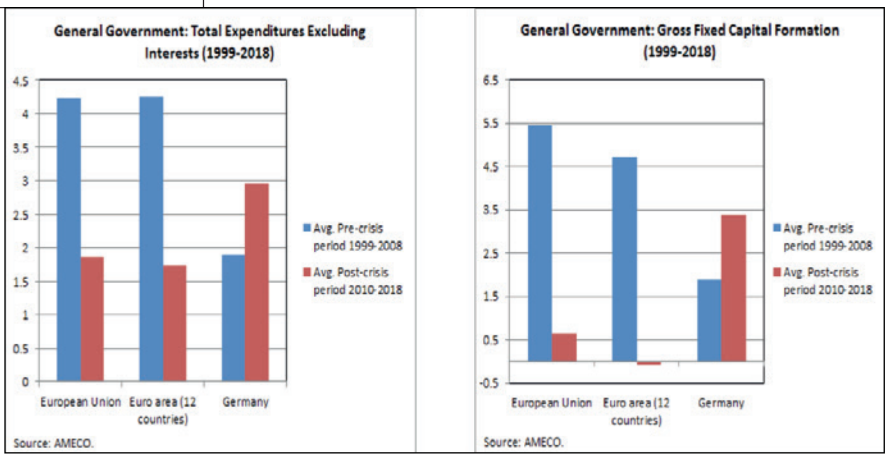
Figure 4: Real total expenditure excluding interest of general government (2008=100)



The fact is that focusing on the budget surplus may be misleading since, in a buoyant economy, it is relatively faster growth of revenues that drives the calculation up. It is thus perfectly possible to continue expanding investment spending at a moderate yet steady pace, while still remaining in a territory of surplus. It is certainly true that the public-investments/GDP ratio remains below the Eurozone average and that there are innumerable fields in which Germany could (and should) invest more (e.g., in physical and digital infrastructure). I certainly agree with this plea. But one should also notice that, according to BMF data, since 2005 public investment spending in Germany has been increasing at an average annual growth rate of 3.8%, *i.e.*, at a faster pace than both total expenditure and nominal GDP.

Calculations based on AMECO data also confirm a reversal of the trend: a moderate but steady expansion of Governments' expenditures. In the decade before the crisis (1999-2008), total expenditures in Germany (excluding interests) have increased at an average annual rate of 1.9% (4.2% in the EU – 4.2% in the EMU). After the crisis spending has increased at an annual average of 3%, while it has collapsed to 1.9% in the EU and 1.7% in the EMU. The same trend can be observed with regard to Government's gross capital formation. During the pre-crisis era, annual average growth of investment spending in Germany was 1.9% while it has increased at an annual pace of 3.4% during the period 2010-2018, while in the EU as a whole, in the post-crisis period it has been fallen to 0.6% (from 5.5%) and even negative in the EMU, -0.1% (from 4.7%).

Figure 5: Governments' total expenditures (excluding interests) and gross fixed capital formation (1999-2018)



Since gross fixed capital formation of general government does not consider the effect of capital depreciation, a better measure to look at additional investment activity on tangible and intangible assets is *net fixed capital formation* (gross fixed capital formation – depreciation). Figure 6 shows the impressive decline in public fixed capital formation in Germany since 1991. Before the crisis, two periods are striking: 1993-1997 and 2000-2005.

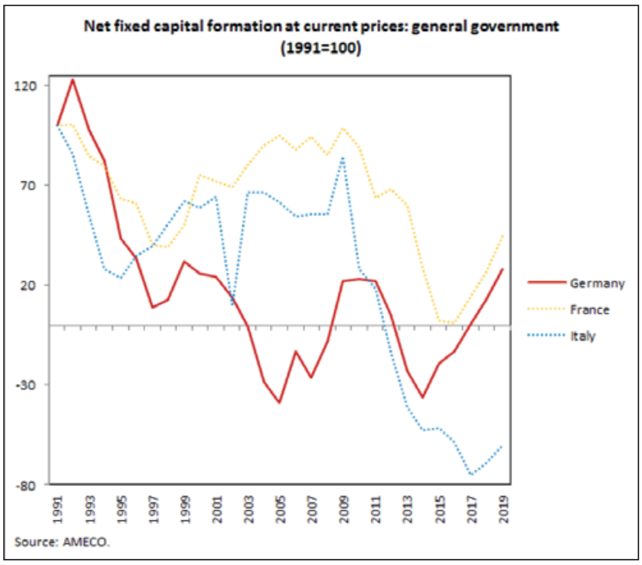
There are three ways in which this fall in public investment can be interpreted: (1) to read these shifts as the result of a conscious mercantilist strategy aimed at compressing domestic demand and price inflation to maintain export-competitiveness at the expenses of trading partners; (2) to read them as the fetishism for balanced budgets at all costs; (3) as lack of administrative capacity to plan and implement investments. I would argue that there is a fourth, more historical, interpretation.

On July 17th 1992, the *Bundesbank* raised interest rates to unprecedented levels in German post-war history (even higher than the June 1973 peak). This engineered an economic slowdown whose effects would be felt for fifteen years. The *Bundesbank*'s policy had the precise purpose of punishing the expansionary fiscal stance of the Kohl government (meant to pay for reunification) and the wage setters' loss of discipline (both the private sector *IG Metall* and the public sector ***ÖTV***) which ensued from the inflationary post-reunification period (in the 1991 and 1992 wage rounds). In this contingency, throughout the 1990s, the Kohl government *decided* to slash public investment, to reduce the size of the unified public sector and to force public sector wage restraint in order to rein in the budget deficit and comply with the Stability and Growth Pact (SGP) by the fiscal year 1997. Ironically enough, it was Mr. Theo Waigel who wanted the SGP which then haunted Germany until 2006. During the early 2000s, Germany (a then sick man) had hard disputes with the Economic Commissioner Pedro Solbes (in the Prodi Commission) to comply with the 3% fiscal rule which it repeatedly broke, unpunished. In a scenario in which the Commission barks at your back, the easiest way for a government to bring the budget deficit down in the short term is to cut/freeze public sector wages (and benefits) and slash public investment – this is, in fact, what also the countries of the EMU periphery did after 2010/2011. This is surely not a smart long-term strategy, but it does the job, if that is the political objective to be achieved in the short term, given the rules of the game at a specific point in time.

From a more historical perspective it becomes hard, in my view, to claim that Germany purposefully (and in bad faith!) neglected public investments. Germany could not spend more in the early 2000s because it had already fiscal problems due to high unemployment and low growth, hence weak revenues and high social expenditures for automatic stabilisers. My interpretation is rather that this was a contingent strategy and that now that times are good again, the trend of public investment (as well as of domestic demand) will gradually increase, as it has already gone back to the levels of the mid-1990s and is now line with the trend of public spending expansion in France.

It makes much more sense, instead, to argue that the countries which are desperately in need of public and private investments are those asymmetrically hit by the crisis – it is sufficient to look at Italy in figure 6.

Figure 6: net fixed capital formation at current prices: general government (1991-2019)



Surely enough, one can ask how much is enough. But, again, considering that approximately 2/3 of fiscal spending in Germany takes place at the decentralized level, we should ask ourselves why should local administrators respond to Eurozone imperatives while being accountable to their local constituencies?

German Federal and local administrators would be better off investing in the future of their citizens, especially given the cheap funding possibilities Germany enjoys today. This is an obvious statement with which it is easy to agree. But, realistically speaking, I don't see why one shouldn't also be open to the possibility that, more simply, the *timing* may be wrong to ask Germany for a Teutonic New Deal: it is perfectly conceivable, in fact, to imagine German local administrators to currently maintain a preference for a moderate (yet steady) expansion of investment rather than a massive fiscal stimulus.

In other words, there seems to exist an inconsistency in the very pre-conditions for the implementation of Keynesian economic policies in a system of multilevel governance: *i.e.*, a clear mismatch between the possibility – and the incentives – for German fiscal authorities to implement Keynesianism at home (in Germany) with the hope to engineer Keynesianism abroad (in the EMU). This is because of the asymmetric effects of an incomplete EMU. After all, to be completely honest: didn't Keynes also say that hoarding money in good times is functional to governments' countercyclical spending in hard ones?

What about Germany's current account surplus vis-à-vis its European partners in the single market? Ever since the crisis, German exports of goods to the EU have decreased substantially relative to its imports. The intra-EU export/imports ratio has been going down significantly. In fact, the core countries of the EMU, together with the Visegrád Group, show a higher exports/imports ratio than Germany.

It will be argued, perhaps correctly, that the bulk of this decrease is due to fiscal austerity and wage restraint in the periphery of the EMU. I am not in principle against this objection, but I would like to ask the reader to consider two qualifications. First, figure 6 shows that when the ratio for Southern European countries starts going up after the beginning of austerity measures in 2010, the German adjustment in the single market, which started in 2008, is almost completed, i.e. lower imports from Southern Europe are not the whole story here. Secondly, the collapse of demand in the South could(and should!) have been avoided regardless of the German current account surplus: it is due to the lack of stabilization mechanisms at the supranational level and, especially, to bad policy choices.

So, where does the German current account surplus come from? Neither from the EU Single Market, nor from the Euro Area.

Ever since summer 2008, Germany's trade surplus with EMU partners has disappeared and the current account surplus has been driven solely by extra-EMU trade. In this sense, Germany quietly *exited the euro* in 2008 to then assail international markets in 2011. OECD statistics show that the driving markets behind export growth in Germany have been the US, the UK and the People's Republic of China - all of them outside the EMU.

It is exactly this that makes Donald Trump and his colleagues very angry. Global imbalances and the German extra-EMU current account surplus do constitute a serious political and economic issue in advanced capitalism, not least because the surplus makes Germany (and hence the whole EMU) fragile *vis-à-vis* exogenous shocks beyond her control. But in this essay - it is good to repeat - I leave this issue out of the analysis and only deal with the EUROpean perspective.

Here again, it will be argued that the closing of the intra-EMU surplus is due to the fall in imports from the Periphery. Again, I would subscribe to this objection if it weren't for the fact that reasoning in this way constitutes a *genetic fallacy*: the fact that since 2010 the German intra-EMU surplus has disappeared because of austerity and internal devaluations in the periphery does not make the intra-EMU rebalancing less true.

Figure 7: Intra-EU exports divided by intra-EU imports (2002-16)

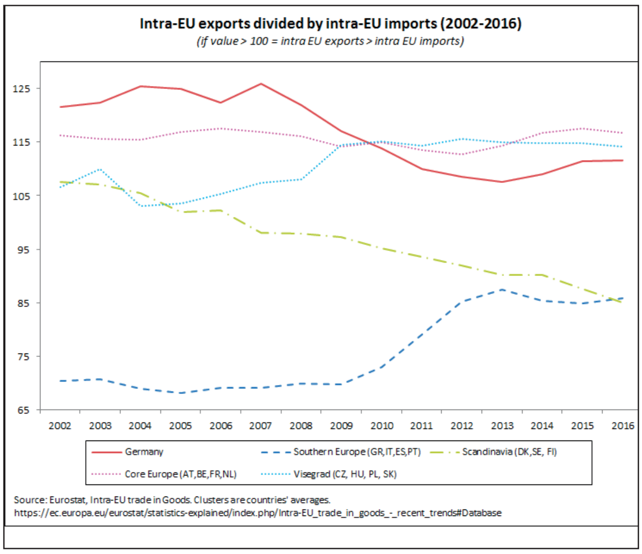
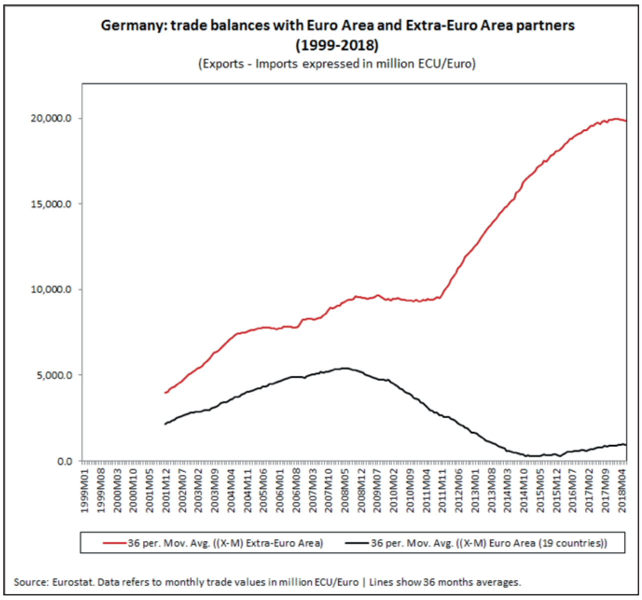
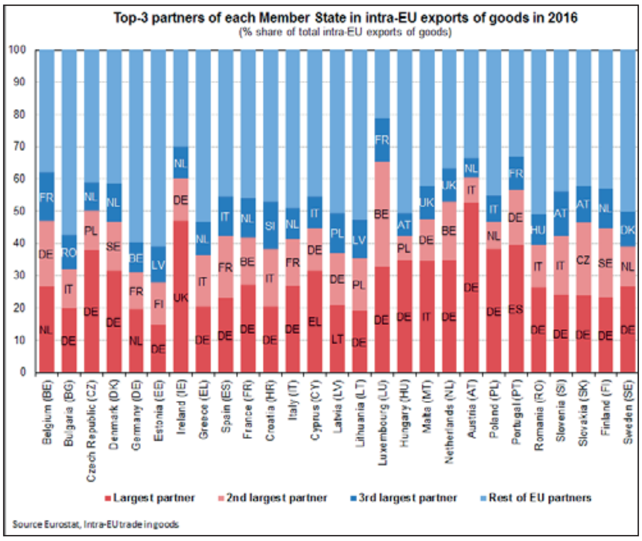


Figure 8: German trade balances with the Euro Area and Extra-Euro Area partners (1999-2018)



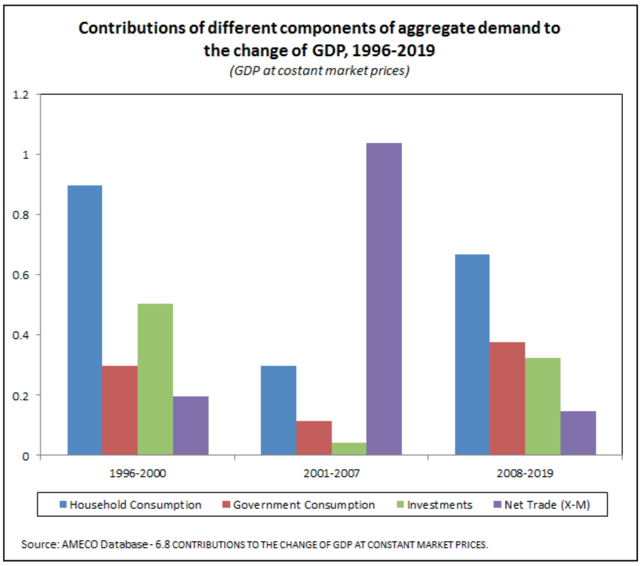
As far as the single market is concerned, Germany is virtually the largest importer for all its members. Germany, thanks to its size and industrial sector at the core of the EMU, already provides a very wide market for EMU exports. This will not come as a surprise to many, but it is simply taken to show that there will be limits to the extent that Germany can realistically expand its imports from its EMU peers – especially until these upgrade their productive structures (with smart investments – not via internal devaluations!). Will, on the other hand, asking Germany to slow down its extra-EMU export engine benefit the EMU? I think it is hard to tell. Possibly, it is instead likely to reduce German imports from its EU trade partners even further.

Figure 9: Top-three partners of each member state in intra-EU exports of goods (2016)



Is economic growth in Germany driven by exports, *i.e.* net trade (exports minus imports)? Or, in other words, does Germany "steal" growth from abroad? When decomposing GDP growth (Figure 10) in the aftermath of the crisis, we ascertain that export-led growth is an historical parenthesis rather than a structural feature of the German economy. GDP growth was strongly driven by net exports during 2001-2007. In the aftermath of the crisis, given increased real wages and government expenditures, GDP growth has been driven mostly by household consumption, public and private investment. Yes, the export share in total GDP remains high in relative terms, but data suggests that net exports have not been the main drivers of GDP growth in post-crisis Germany: the trend has been reversed.

Figure 10: Contributions of different components of aggregate demand to change of GDP (1996-2019)



CONCLUSIONS

Before moving to the conclusions I shall make clear what this essay does *not* argue, in order to avoid any misunderstanding. I am *not* arguing that the German current account and fiscal surpluses are good and desirable. Most importantly, I am *not* arguing that what documented here is enough for Germany and the EMU to cheer up, as well as I am *not* arguing that German wages should not rise further or that German authorities *shouldn't* invest in the future of their citizens. My aim was to play a bit the devils' advocate and ask two questions which seem to be forgotten in this very controversial debate: what has Germany done since 2010 to address its unbalanced growth? And, from a realistic and constructive perspective, what could Germany do given its institutional setting (i.e. wage setting structures and fiscal constitution)?

In so doing, I have attempted to go beyond a pure macroeconomic reasoning based on accounting identities and tried to push the reader into reflecting upon historical contingencies and the institutional constraints on a strategy of Teutonic Keynesianism that shall rescue the Euro from itself. I would argue that, contrary to what is usually claimed, there are indications to maintain that the pre-crisis trend is being reversed and that Germany has made some important steps towards a "quiet" rebalancing. This is good news and should be kept in mind if we aspire to having constructive politics in the EU.

But does this mean that Germany, and the EMU, are safe and sound? No, not at all.

As for Germany's extra-EMU current account surplus, there is probably only one person realistically capable of tackling the issue. This person sits in Washington and we should expect him to sooner or later deal with it. It is likely to be nasty and the EMU should be ready when the next exogenous shock will arrive.

An incomplete EMU remains fragile and requires upkeep. German politicians are not immaculate in this story and, if they want others to stop teaching them how to run their fiscal and wage policies, they should stop opposing projects to fine-tune the EMU and venture into a serious reform plan that envisages *blühende Landschaften* for EUROpe as a whole and not for Germany alone. Whether they like it or not, they belong to a common project now.

There seems to be one priority around which accusers and defendants should come together before the next shock arrives: to avoid asymmetric macroeconomic adjustments based solely on the compression of wages and public investment. Two institutional changes could serve the purpose. Broadly speaking, a pan-European unemployment benefit scheme based on national (or better regional) PPPs would work as an automatic stabiliser to support household consumption when countries most in need are forced to switch them off in their budgets. Secondly, one could imagine an ECB that supports a European Growth Bond by the European Investment Bank in the context of a proper European Investment Plan. Unfortunately, the importance of both these reforms for the stabilisation of the EMU has been eclipsed by the attempts to create a Capital Markets Union to engineer a financial fix to the structural flaws of the EMU.

A complete monetary union is likely to relieve these conflicts and bring benefits also to the Germans. I may be wrong, but I do not seem to remember anyone in my life that has ever argued that Lombardy should undergo an internal appreciation *vis-à-vis* Sicily (or *vice versa*). We do not even seem to discuss publicly whether Sicily runs a current account deficit or a surplus (although regional finance is indeed a hot topic, I agree). To those who argue that an EMU with pan-European automatic stabilizers will turn into a permanent structure of uni-directional fiscal transfers to the South, one should remind two points.

First, Germany is a big country with relatively deprived areas as much as Italy is a big country with relatively rich and prosperous areas. Shifting the political discourse around fiscal transfers to the regional dimension (NUTS 1 and 2) would probably help to avoid poisonous nationalist discourses and would enable us to see how all countries would stand to benefit from a system of supranational automatic stabilisers calibrate on a regional basis - even the "*Wessi*" *Germans* and the Northern Italians, the "*non terroni*". Secondly, had the EMU had a system of supranational automatic stabilisers in place since 1999, the Germans - or better parts of Germany - would have been net receivers for approximately half of the EMU's existence. The simple intuition here is that insurance systems exist exactly because we live in an uncertain world and cannot foresee exogenous shocks. Indeed, if we could, we wouldn't let them occur – I guess just like in that Tom Cruise movie, Minority Report.

Given its high current account surplus, Germany is, today more than ever, a very fragile country in a world in which free trade and liberal values cannot be taken for granted anymore. Since German authorities are now under the impression of being immortal, they think that a pan-European insurance system is not in Germany's long-term interest. I wonder what the answer would have been, had one asked them about the merits of a pan-European unemployment benefits scheme in 2001/2004. This is, basically, a *time inconsistency problem*. It is a short circuit which, to be solved, requires *today* an *irrational politician* in Germany to drive a process of institutional change which *tomorrow* will benefit also Germany and the People of Europe.

A big obstacle to a constructive debate remains, alas, the fact that German authorities have never bothered to acknowledge the issue of German responsibilities in the first place. This is regrettable and does not pay justice to the need to play cooperatively in a monetary union. Yet, it is also time for critics (me included) to face the fact that, while being *necessary*, an acknowledgment of the problem of Germany's unbalanced growth will not be *sufficient* to trigger the supposed spectacular German expansion that shall cure the sorrows of the young Euro. In my view, it is a mistake to insist that Keynesianism in Germany will fix the Eurozone's problems: Germany should not and cannot be the *fixer of last resort* for the single currency. Supranational adjustment mechanisms are needed for the stabilisation of the Eurozone in hard times-even if I am aware that this is easier said than done. But we should start from somewhere.

QM-05-18-106-EN-N

Publications Office

With the support of the Erasmus+ Programme of the European Union

doi:10.2870/83554
ISBN:978-92-9084-711-3