Europe's 'structural reform' agenda is little more than a fairytale

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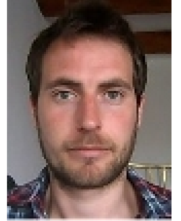
The policy response to the Eurozone crisis has incorporated a number of different elements, including the structural reform of European economies. ***Aidan Regan*** *argues that this 'structural reform agenda' has been defined in exceptionally vague terms, and that it is still unclear precisely which reforms would lead to tangible economic improvements in European countries. He writes that with the European Parliament due to hold elections in May, there may be an opportunity for opposition parties to politicise the issue and subject prevailing policies to proper scrutiny.*



There are four actors who have dominated the political and policy response to the Eurozone crisis: the executive of the German Federal Republic, now a super majority between the Christian and Social Democrats, Finance Ministers who make up the Economic and Financial Affairs Council (ECOFIN) of the European Union, the European Central Bank (ECB), and the executive of the Economic and Financial Affairs Commission, that is, the Department of Finance of the European Commission).

This is a complex institutional relationship with overlapping power asymmetries. Two of these actors (Germany and Ecofin) represent national interests. They bargain over and defend what they consider to be the comparative advantage of their own nation-states. For Ireland this means a willingness to veto anything that would lead to corporate tax harmonisation. For Germany it means a willingness to veto anything that would lead to Eurobonds or debt mutualisation. These strategic positions, like any preference, are not set in stone and could, in principle, change. In this matrix German interests dominate for obvious reasons – they are the biggest and richest member-state of the EU.

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The other two actors (the ECB and the Economic and Financial Affairs Commission), in theory, represent pan European interests. They are supranational actors that are supposed to defend the shared interests of the 18 member-states of the euro currency, and the 28 member-states of the EU. They favour more fiscal harmonisation and generally support more political integration than Germany is willing to concede. But given the huge heterogeneity among the 28 member-states, it is becoming increasingly difficult to identify what a 'common interest' actually is. Despite this, it is not unreasonable to assume that these supranational actors would have some conflict with powerful member-states, such as the Conservative German government, over how to handle the Eurozone crisis.

This, however, is not the case. Why has there has been no serious confrontation between these actors on how to resolve the crisis? The easy answer is that supranational actors such as the Commission have simply internalised the preference of Germany. But differences have emerged, particularly between the German government and the ECB. Furthermore, these actors are not homogenous agents with a single preference. They fight like cats and dogs within their internal systems, particularly within the European council. But it must be observed that the degree of policy consensus between the national and supranational levels is remarkable. What explains this, other than

‘Germany gets what it wants’?

One potential answer is ideology. Ecofin (Finance Ministries) is primarily represented by Wolfgang Schauble, the German Finance Minister. The German Executive is primarily represented by Angela Merkel, the Federal Chancellor and chief executive of the Christian Democratic Party. The ECB is led by Mario Draghi, and the EU Finance Commission is headed by Oli Rehn. What these elite actors share is a political preference for a certain economic idea. This is not meant in the narrow sense that they might all be neoliberals who want ‘austerity’. The Commission and the ECB are perfectly aware that fiscal contraction, in the long-run, is a self-defeating strategy for the Eurozone as a whole. Nor is it a case that they are all ardent libertarians. They differ on the speed of European banking Union, the mutualisation of debt, fiscal harmonisation and social policy. The German executive would never argue against the need for social insurance, even if they want a radically reduced welfare state.

So what is the core economic idea that they share? It is the magic economy dust formula of ‘structural reforms’. It is the idea that if national governments just sprinkle enough structural reforms into the economy to enhance market competition they will, eventually, generate the conditions for employment growth. This is captured perfectly in a recent analysis by Marco Buti, the Director General (DG) of the Economic and Finance Commission. He outlines a trilemma for the Eurozone: we cannot have the welfare state in a fixed monetary union that requires reducing fiscal deficits to 3 per cent of GDP. This is true. In order to keep the welfare state, he proposes a consistent policy ‘trinity’: banking union, symmetric adjustment (i.e. inflation in the core) and deep structural reforms. These, we are told, will generate the conditions for economic growth. In turn, with full employment, the welfare state is secure.

This is the core idea behind the policy response to the Eurozone crisis and it is worth stating clearly if its merits can be tested against rational argument and empirical evidence. The argument is as follows: the only way to keep the welfare state in a single currency is to generate full employment. This cannot come about through fiscal or monetary policy unless a member-state leaves the euro. The only solution is structural reforms.

Hence, the most important European policy in responding to the crisis are deep structural reforms. But Buti never defines, measures, compares or even vaguely outlines what this actually means. None of the ECB, ECOFIN, and EU commission policy statements ever do. The only actor who has a clear idea of what structural reforms are is the German Federal government. They make no apology for arguing that holding down wages, cutting pensions, liberalising employment protection, creating unpaid jobs and reducing government administration will solve the Eurozone crisis. Needless to say, they don’t say it at home. Politics is the main problem.

But the point to be noted is that the empirical non-falsifiability of structural reform policies is the idea that underpins the consensus between the national and supranational levels. It enables all of the actors to sell a policy that no one understands or can even refute. It is a fairytale. Promoting structural reforms as a panacea for unemployment is the equivalent of a political party saying we need votes to win an election, or a trainer saying to an athlete, just run faster. Structural reforms are, ultimately, a short-hand to say more markets and less politics.

In an ideal world of perfect competition, within a single market with no transaction costs or rigidities for capital and labour, we probably would create full employment. But to propose this as a serious policy-strategy that will lead to full employment and strong economic growth is no different to those self-proclaimed revolutionaries who argue that nothing can change until everything changes: i.e. until we abolish capitalism.

Where does Europe’s magic improving economy dust formula lead us then? The German government will not change their preference for ‘structural reforms’ because they are convinced that the Hartz Reforms (I-V) are what underpins the competitive resilience of the German economy. I have argued elsewhere that this is not the case. ECOFIN will not change their preference because it would require spending resources and reversing a Treasury mentality of permanent austerity. The ECB will not change as they want the Karma of an optimal currency area, total flexibility of adjustment in prices and wages.

This leaves the Commission, which is currently dominated by the Economic and Financial Commissioner, Oli Rehn.

He is, unlike Angela Merkel, a classic neoliberal, and not likely to change his preference for pure markets any time soon. But contrary to some fatalistic predictions, it seems to me that the Commission is the only actor capable of challenging the structural reform agenda, and therefore overcoming the 'joint decision' trap of the European Council.

This brings me to the European parliamentary elections in May. Given the treaty changes introduced after Lisbon, the European parliament will have the final say on the next President of the European Commission. This means that the political group who can create a majority in the European parliament will nominate the executive. Presently the European Peoples Party (Christian Democrats such as Enda Kenny and Angela Merkel) have a majority. But if this changes, everything is up for grabs. Would it make sense for opposing parliamentary groups to politicise the structural reform agenda? Or at least confront it with empirical evidence?

All of this assumes, however, that a new Commission, under new leadership, would have the political capacity to create a 'dissensus' in the context of a German dominated consensus. It also assumes that the elections won't result in a victory for the populist right, which, I fear, is where the magic dust formula is likely to lead us.

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Note: This article gives the views of the author, and not the position of EUROPP – European Politics and Policy, nor of the London School of Economics.

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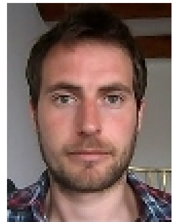

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