

## After Brexit, the EU must break with neo-liberalism and address the discontents of globalisation



*in the economies of member states.*

*How should the European Union react to the decision of the British people to withdraw from the union? This is the question that has been at the centre of the political debate in Europe since the Brexit vote. **Paul De Grauwe** outlines a future scenario in which the EU could succeed after Brexit. He contends the union must address discontent with the type of globalisation it has championed throughout its existence. It must break with neo-liberal dogma and focus its efforts on investing*

### Whose democratic deficit?

The starting point in trying to answer the question of how the EU should be reformed in the wake of the Brexit vote is the observation that the European Union has a very negative image today, not only in the UK but also in other parts of the EU. According to many analysts, this has to do with a democratic deficit of the EU hollowing its popular legitimacy.

There is certainly a lack of democratic accountability in the decision-making process at the European level. But is it necessarily true that the democratic deficit of the EU is worse than that of individual member states? Legislation in the European Union is enacted by the Council of Ministers and the European Parliament. The ministers are sent by their national governments. And the latter have come about as a result of democratic elections in each country. MEPs are elected directly in pan-European elections. Thus, the decision-making bodies in the European Union have the same democratic legitimacy as national governments and parliaments. If there exists a democratic deficit, it is arguably the same at the national and the European levels, and the legitimacy of both national and European institutions should be questioned and their proceedings reformed.

### Globalisation

I see a deeper cause of the dissatisfaction with the European Union. I argue that this dissatisfaction has a lot to do with the inability of the European Union to set up a mechanism that would protect the losers of globalisation. Worse, the EU has reduced the capacity of national governments to take on the role of such protectors, while at the same time virtually nothing has been done to create such a mechanism at the EU-level.

Free trade creates an incredible dynamic of innovation and, in consequence, material prosperity. That prosperity, however, does not benefit everyone equally. Many people are better off thanks to globalization. But many others are not. Some even have seen their welfare decline because they've lost their jobs or because their real incomes have fallen.

As globalisation creates material welfare on a macro scale in the countries that partake in it, it should be in principle possible to compensate the losers that come about through this process. This argument most economists find strong enough to defend globalisation with. But the political obstacles towards organising such redistribution towards the losers of globalisation are plentiful. This supposition poses a problem in most industrialised countries, but it has been exacerbated in the European Union.

## Globalisation and its discontents

European institutions have become major promoters of globalisation. The single market and the trade agreements reached by the European Commission have widely opened up Europe's gates to the wider world. There is nothing wrong with that per se. Except for the fact that, there has been a complete failure to secure the necessary compensation for the ones who lost out on globalisation. European institutions have no power over social policy, which has been kept in the hands of the national authorities. However, the hands of these authorities have been shackled by the very same European institutions' fiscal rules.

European fiscal rules not only make it extremely difficult to redistribute the fruits of globalisation to the less fortunate members of society. What is worse, they have often amplified their hardships. For at least five years now the European Commission has pushed all member states of the Eurozone into an austerity straightjacket that has produced economic stagnation and rising unemployment mainly among those who had already been hit badly by globalisation. It will come as no surprise that many have turned their backs at the European institutions that seem distant and ready to inflict punishment on millions of people living in hardship.

Not only the fiscal rules but also the structural reforms that have been imposed by the same European institutions are to blame for the rejection of the European Union by many people. European policy makers have adopted a uniquely neo-liberal discourse. According to which, workers must be flexible (read: they should be happy when their wages fall, when they can be dismissed quickly and when they receive fewer unemployment benefits). The neo-liberal policymakers that now dominate the European Union preach that social security is unproductive and should be downsized. These policies are euphemistically called structural reforms. They are imposed on millions of people, mostly the losers of globalisation, by European institutions and national governments alike.

The problem of the European Union today is that, instead of helping those who suffer from globalisation, it has set up policies that hurt these people even more. It is no surprise that the losers revolt. If the EU continues with austerity and such structural reforms, the revolt will spread and will take the form of further attempts to exit the Union. It is time the European Union takes the side of the losers of globalisation instead of pushing for policies that mainly benefit the winners.



Anti-globalization protesters in Edinburgh during the start of the G8 summit

## Solutions

This can be done in two ways. The first one is to stop imposing structural reforms on the member states. The rationale for these structural reforms has been that they promote economic growth and therefore should benefit everyone in society. The empirical evidence of a positive link between structural reforms and economic growth, however, is very weak. In a recent econometric analysis of the OECD countries, we could not find evidence that reforms in the labour markets and in the product markets boost economic growth (De Grauwe and Ji: 2015). This is also confirmed by a recent study conducted by the IMF (2015). We do find, however, that investment, both private and public, has a strong positive effect on economic growth.

The latter result points the way to the second change in economic policies that European policymakers should initiate. This should consist of boosting public investment in countries that suffered severe collateral damage from the ill-conceived austerity programs imposed by European institutions.

A boost in public investment can only be achieved by changing the fiscal compact that imposes structural budget balance in the member states of the Eurozone. This compact has the unfortunate implication that public investment can only be financed by current revenues. A more destructive rule for economic growth has probably never been imposed. When politicians are told that the cost of public investment should be fully borne by present taxpayers (voters) while the benefits will accrue to future taxpayers (voters) it cannot come as a surprise that the political incentives to engage in public investment are weak. This is what is happening today. Thanks to this unintelligent rule, public investment in the Eurozone is at a historically low level.

It is often said that allowing public debt to increase will saddle our children with an unbearable debt burden. This criticism confuses gross and net debt. When productive public investments are undertaken by issuing government bonds, our children will inherit both productive assets and government bonds. Today the cost of issuing government bonds is close to zero in many Eurozone countries. If governments manage to invest in productive assets that have a return higher than zero, our children will inherit assets that create revenues exceeding the cost of borrowing. They will not understand why we have not done so when borrowing was so cheap.

I am a proponent of more political integration in Europe. Today, however, grand schemes for “more Europe” should be put on the back burner. As long as European politicians continue to follow ill-conceived neo-liberal economic policies one cannot ask people to follow them in constructions for more of the same.

*This article gives the views of the author, not the position of the Brexit blog, nor of the London School of Economics. Image by [Asbestos: Attribution-Share Alike 2.0 Generic](#).*

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