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Introduction to "Economic and Financial Governance in the European Union after a decade of Economic and Political Crises."

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ABSTRACT
This paper offers the Introduction to the Special Issue "Economic and Financial Governance in the European Union after a decade of Economic and Political Crises." We introduce the five papers. We distill three important lessons they offer for EU integration.

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COVID-19; economic and Monetary Union; Eurobonds; European sovereign debt crisis; global financial crisis

Policy Highlights

- Crises create consensus, especially when it comes to setting new objectives
- Crises do not always show the *path* towards these new objectives, or the choice of institutional structure to accomplish these objectives;
- In the EU, institutional change in times of crisis is inspired by institutional structures previously conceptualized or adopted.

The 2008–09 Global Financial Crisis and the 2010–13 Sovereign Debt Crisis in Europe had a dramatic impact on the European Union (EU). Both crises led to a major contraction of the real economy and both revealed a number of fundamental weaknesses of the financial system of the EU. The consequences of these crises were far-reaching. Besides the economic and political impact of these crises in EU Member States, they also led to important changes in financial governance in the EU.

Several institutional structures and governance changes made during and following the crises aimed to avoid, and respond better to, potential future financial crises. In this Special Issue we will zoom in on some of these new institutional structures and governance changes.[1] Each paper of this Special Issue approaches an aspect of the governing context that surrounds the Euro Area, considering historical relevance, sources of influence for decision-making, and institutional design of the oversight of the Euro Area. The aim here is not to provide a comprehensive account of all the crises-induced changes that happened in the EU.[2] In fact, the history of the EU is littered with change

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invoked by crisis (D'Erman and Verdun 2018). Rather, the papers provide an in-depth analysis of a change, or a force that contributed to changes in Financial Governance in the EU.

Below we first briefly introduce the five papers. Next, we reflect on the important insights they offer for EU integration: exactly how do decisions regarding governance structures in the EU come about; and, what lessons do we learn from these studies that inform the broader literature? The historical context of European integration offers an important reminder of the benefit of hindsight – that many of the significant critical junctures of either deeper cooperation or divisive fragmentation are often better understood with the both the passage of time and the tool of comparison and contrast. The five papers of this Special Issue and our reflections offer some interesting insights and hypotheses regarding the birth and evolution of institutions in the EU. We apply our framework to analyze the likely forces at work as the EU and its member states combat the consequences of COVID-19 in the years to come.

Mourlon-Druol (2020) situates the early European Economic Community's (EEC) attempts at articulating the need for a proposed single currency within the context of a slowly-evolving crisis, namely slow economic growth in combination with high rates of inflation in the 1970s. He argues that this period of economic headwind initiated some notable developments within the EEC discussions surrounding the purpose and utility of a possible single currency; and that these reflected in, and impacted how the EU approached solutions to the perceived problems in the design of Economic and Monetary Unification (EMU) after 2008.

An example of one of these post-2008 institutions is the European Systemic Risk Board (ESRB), which Ehrmann and Schure (2020) analyze in composition and in action. The design of the ESRB lacks direct regulatory power, which some see as an example of the inefficiency of EU governance. However, the authors argue this conclusion is premature. By making an in-depth comparison with the National Transportation and Safety Board, a critically acclaimed United States (US) institution involved in systemic risk management, they show that the lack of regulatory power may actually be an important asset in the long run, as it might help safeguard the independence and objectivity of the ESRB.

The examination of Ehrmann and Schure sheds some important light on the context of leadership, and authority within EMU and the EU as a whole – a subject taken up by Schöller (Ehrmann and Schure 2020). A recurring question is whether institutions at the supranational level are "all bark but no bite"? Yet, if they are not, then does the supranational level intrude too far into the domestic decision-making prerogatives of spending and taxation? Schöller (Schoeller 2020) focuses on the role of Germany during the Euro Area crisis in this context. Germany has been variously labelled as a "reluctant hegemon" (Bulmer and Patterson 2013) and a "ordoliberal leader" (Young 2014) in terms of its responses to the sovereign debt crisis. Schöller shows that the record of German leadership after 2008 has been mixed: Germany's willingness to lead in recommending austerity policies helped to enhance obtaining EU competence in banking supervision, while, at the same time, its disinclination from considering burden-sharing policies weakened the development of financial assistance institutions.

Henning (2020) unveils a perhaps surprising source of influence behind the design of new EU institutions after 2008: the United States Government. Henning details the timing and nature of US assistance in terms of the advice of US policymakers, as well as through the International Monetary Fund (IMF). The US sought to contain financial contagion for its own purposes. In doing so, it actively supported the development of new policies and mechanisms to strengthen the EMU framework. Henning's contribution shows that the US Government's influence on the European Union is a matter of both the past and the present.

The last contribution, by Demertzis and Wolff (2020) highlights the question whether the current EMU governance structure has essentially been completed in the past decade. Specifically, their analysis looks at the institutional steps that would fix the issue of the "asymmetrical EMU" (Verdun 1996), that is, monetary union without a fiscal union (see also Howarth and Verdun 2020). Demertzis and Wolff argue that the steps are, first, the completion of the Banking Union; second, the centralization of funds and delivery of some public goods at the EMU level; and third, the full federalization of critical economic functions. By describing the pragmatic initiatives needed for solving the incongruities of EMU, Demertzis and Wolff also articulate the inherent political tensions that underscore the reasons for having arrived at the asymmetric design of the EMU in the first place.

The findings in this Special Issue seek to contribute towards the research on how actors in the EU reach decisions about the governance structure of EMU. We draw three lessons from the contributions in this Special Issue: (1) Crises foster consensus. They clarify the need for new objectives; yet (2) Crises do not always show the path towards those new objectives or the shape of the institutional solution; (3) Chosen solutions in times of crisis are inspired by models previously conceptualized or adopted.

Lesson 1. The crises that hit the EU resulted in a broad consensus among politicians and policy makers regarding the need for change. The crises even led to a degree of consensus regarding what some of the necessary changes had to be. As such crises are important catalyzers for institutional change. For example, Ehrmann and Schure (2020) mention that institutions for macro-prudential policy sprung up internationally after 2008, besides the ESRB in the EU. However, the Special Issue contributions show that change takes time and may perhaps stall, even in the context of a broad consensus regarding a change that is deemed necessary. We believe this characterization applies to the Banking Union: there is broad consensus regarding the need for it, through this project is not yet completed as of yet.

Lesson 2. Notwithstanding the increased clarity, the crises that hit the EU did not establish consensus about everything. There is for example disagreement about the desired *finalité* of the EU or EMU. The crises also do not inform actors about *how* to reach decisions about the new governance structure. The *finalité* for EMU in Demertzis and Wolff (2020) includes fiscal union, besides monetary union and they argue that importance alone is not sufficient for reaching that end goal; hence the need for following a carefully designed sequence of steps towards a more symmetric EMU.

The final lesson we draw from the Special Issue contributions concerns *how* institutional change happens. The Governance and International Relations literatures on this subject distinguish several complementary perspectives on the dynamics of post-2008 institutional changes:

- A historical institutionalist perspective, which couches decisions as being embedded within the prevailing institutional design of the EU as a whole (Verdun 2015)
- An intergovernmental framework which asserts that responses to crises were limited by member state negotiations and lowest-common denominator decision-making (Hodson 2019); and
- A neo-functionalist emphasis on the role of supranational and transnational actors, as well as financial market interdependence, which encouraged euro area members to seek "optimal" common solutions (Niemann and Ioannou 2015).[3]

Lesson 3. While the contributors of the Special Issue do not explicitly attempt to test the explanatory power of these complementary theories, they do offer interesting insights on how decisions are taken. Mourlon-Druol (2020) and Henning (2020) show that a historical institutionalist perspective is of critical importance to understand institutional change in the EU after 2008. Specifically, Mourlon-Druol (2020) demonstrates the role of models that have been discussed and explored in the past. Such "off-the-shelf" models arguably become particularly attractive solutions when a heightened urgency emerges due to a crisis. The case discussed by Henning (2020) offers further support of the conjecture that chosen paths in times of crisis are inspired by approaches and models previously conceptualized or adopted. He stresses the continuing role of the US as a catalyzer for change in the EU during times of crisis. By contrast, Schoeller (2020) is in our view best understood from an intergovernmentalist viewpoint. He shows that the German government opposed burden-sharing of the cost of the crises among EU member states. Burden-sharing through EU level solutions or direct transfers between member states was not deemed to be in the national interest of Germany.

At the time of writing this introduction, European countries are in various stages of physical distancing measures due to the worldwide COVID-19 outbreak. Although the COVID-19 outbreak started as a purely public health crisis, the measures to fight it have enormous implications for the EU economy, the internal market, public finances, and possibly also financial stability (Alexandrovich 2020). Observers wonder how long this period will last and whether the corona crisis will be a transformative or merely a temporal upset.

The lessons we draw from this Special Issue suggest that the corona crisis offers an important window of opportunity for institutional, hence transformative, change. Presently, this crisis has drawn the attention of national governments towards local stimulus measures and the potential of nationalizing key industries (Reuters 2020). Seeing that crises clarify the need for new goals and institutions one would expect some public health initiatives at the EU level, as well as policy discussions and institutional development in the areas of public finance and macroeconomic policy coordination.

We learnt that crises build consensus. In April 2020, a consensus emerged in the Eurogroup to offer financial support to member states that are hit severely by the corona crisis, so that those who do not have sufficient fiscal space can take appropriate action to fight this crisis. However, there is no consensus as of yet regarding the instrument to provide financial support. Two options are being considered for crisis relief funding: (1) namely provide funding through existing institutions, such as the European Investment Bank (EIB) or the European Stability Mechanism (ESM); or (2) create what is essentially a new institution, namely Eurobonds. Lesson 3 provides insights into both short- and medium-term responses to crises. In the short term its implication would be that financial support to member states will be provided through the EIB or the ESM, not a new institution, such as Eurobonds. Yet, the medium-term implication of this lesson would be that the topic of Eurobonds will remain on the agenda during the corona crisis, possibly in the context of a discussion to fund modest expenses on a public good at the EU level. The discussions of whether to set up Eurobonds had member states divided on whether to support the goal in principle. Even among those who were supportive of the idea, there was lack of clarity on the institutional structure, the legal provision, and rules that would support such a goal (Alfageme 2020; Financial Times 2020).

In summary, the current economic crisis facing the EU as a result of COVID-19 is indeed garnering consensus on the need for a joint response. At the same it is both highlighting the fissures in policy preferences among member states and is relying on institutional proposals that are already on-hand. Indeed, the lessons from this Special Issue suggest the corona crisis will lead to developments as identified by Demertzis and Wolff (2020), namely further progress towards completion of the Banking Union, as well as funding and delivery of some additional public goods at the EMU level. Whether or not these can be achieved will depend on the path chosen.

Notes

1. The contributors of this Special Issue and a related forthcoming symposium came together for a two-day workshop in February 2017 at the University of Victoria in Canada, funded by a grant through the Social Sciences and Humanities Research Council of Canada (SSHRC).
2. Numerous excellent works already exist which outline the timeline of the crises and/or the detail of the responses. Examples include Welch (2011) and Howarth and Verdun (2020).
3. This list is not exhaustive. There are also a number of analyses that draw on these or a combinations of these theoretical traditions to explain EU institutional changes in light of the financial and sovereign debt crisis (e.g. Jones, Keleman, and Meunier 2016; Schimmelfennig 2018).

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