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THE EUROPEAN

The European View

The EU will be a better place with the UK in it

The euro crisis – a handmaiden of change

Seeking Mr Cameron's position



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The European View

As the debate around Britain's membership of the EU continues to rage, attention seems to focus at one EU member state in particular. Germany has been the point of reference for all those labouring over what the future for the European Union holds, but recently it has been resting heavily on the consciousness of policy-makers in Britain as well. *The European* has invited a host of politicians, think tanks and economists from Germany to discuss Germany's vision of the EU, its relationship with Britain and its view on the EU debate in the UK.

Everyone in Britain, not least the government, is awakening to the fact that Germany is one of the must-have allies in any sort of EU negotiations, especially when it comes to Britain's future in the EU.

Those that believe that a 'renegotiation' of Britain's membership terms is possible acknowledge that for such an arrangement to be successful Britain needs to persuade Germany to accommodate its demands.

Those that believe that the EU needs to reform (perhaps to resemble something more in Britain's liking) know very well that they will only be able to have their vision materialise if Germany supports it.

They all recognise that the future of the eurozone (and Europe's economic well-being) depends to a large extent on Germany's wish to see the process of European monetary and economic integration succeed.

But despite all the above and all the speculation involved, Westminster and Whitehall seem to ignore the messaging coming from Berlin and German policy-makers.

The German Chancellor, her Finance Minister, and a whole host of other senior politicians have been as quick to argue how important Britain is for the EU as they have been to point out how wrong it is to pursue a 'renegotiation' of its membership terms.

Similarly, the contributors in this issue of *The European* display respect and amazement in equal measure when it comes to the UK's role within the EU and its attitude towards it. They all converge towards the argument that Britain's future lies firmly within the EU and any attempt to remove itself from the EU's core will be damaging both for Britain and the EU.

Britain is invited to join in and take part in forming the future of the EU. Whether it chooses to do so or remove itself to the edges of the world's biggest economy and common market depends on its people and their elected representatives. But no one can say that its friends and allies didn't offer a word of advice when it mattered.

Petros Fassoulas

Chairman, European Movement UK

The EU will be a better place with the UK in it

We are aware that the UK thinks of the European Union primarily as an economic project, a single

market, rather than a political project. For us, however, the European Union is first and foremost a political project. This may explain why we in Germany stick by the European idea for all its imperfections. From our history, we have learned that we are better off coordinating policies with our neighbours. We are

very well aware of the fact that we have to pay a high price for it: we are the biggest net contributor to the European Union, we accept European rules in cases where we would probably be better off regulating things on our own, and we live with the administrative and legal imperfections of some of our fellow EU member states.

I admit that these circumstances sometimes constitute a serious burden. However, we accept it because in return, we get a political union which not only enables us to live in peace with our neighbours in the middle of Europe but also creates a common market that is of utmost importance for us in Germany. It is particularly important to us since a big percentage of our exports go to other EU member states: almost 40 per cent of all our exports go to eurozone countries.

We are deeply concerned about the ongoing discussions in the UK whether the UK should loosen its ties to the EU, or even leave the EU. I can very well understand why many people in the UK and elsewhere have great concerns about Europe and the way the European Union operates. We, too, are not happy with some of the developments in Europe, for example the EU budget and the excessive bureaucracy. A UK exit from the common project EU, however, would constitute a serious harm for Germany. Germany and the UK share a similar way of thinking and a similar approach to getting things done. It is always good to know that we have a like-minded ally at the negotiating table in Brussels. In my opinion, the British input is vital for the development of a better Europe.

This input, however, would be missing if the UK decided to withdraw from the EU or to retreat from some EU policy areas. The UK would no longer be part of the negotiations in Brussels. On the contrary, in

order to guarantee its access to the single market, the UK would be subjected to many regulations without having had any influence on the negotiation of those rules (regulation without participation). At the end of the day, this would also weaken the negotiating position of Germany.

In my view, the unlimited access to the single market is essential for large parts of the British economy. Take the City, for instance: an important role of the City is to act as gate to the European economy. The gate will only remain open if the UK applies all the rules, rules that then would be negotiated without the UK having any say.

We know that some politicians and political experts in the UK would prefer a “Europe à la carte” – receiving all the benefits of the single market and not having to pay any of the costs. Nobody can and will accept that kind of cherry-picking. Other member states would want to follow the British example. ‘UK à la carte’ would lead to ‘Poland à la carte’, ‘Italy à la carte’, etc., which would ultimately result in the dissolution of the so very important political union.

The EU will be a better place with the UK in it. That notion is also true for the UK itself. The European idea is worth the price we pay for it, and that we keep on working on it together.

There is an alternative to the UK’s exit from Europe: No longer stand in the corner but take a leading role in building a new and better Europe, for member states, for businesses and for citizens. Let us fight for a Europe that has a strong voice in the world. ‘Join the team’, as we would put it.

Ralph Brinkhaus

CDU Member of the German Parliament

The euro crisis – a handmaiden of change

As a German who has lived in Britain for the last 15 years, the gap between how Britons and Germans view the same events rarely ceases to astonish me. Judging by the tone of the British debate, the eurozone must be a uniquely dysfunctional place run by policy makers who 'just don't get it'. However, policy makers in Berlin believe that, instead of witnessing the inevitable demise of a supposedly misguided venture, we may be living through the birth pains of a stronger, more coherent and more dynamic economic and political entity in Europe.

Let us start with a few simple facts.

The eurozone economy is not doing well. At the end of 2012, its GDP was still 2% below the level of late 2007, before the various financial crises erupted. But despite having its own currency, the UK has fared worse with a loss in GDP of 3%.

In 2012, the eurozone as a whole had a fiscal deficit of roughly 3.3% of its GDP, miles below the deficit of around 8% for the UK.

The worst fiscal offender within the eurozone, Greece, apparently ran a fiscal deficit of around 9% of its GDP last year while its economy contracted by more than 6%. Adjusted for the impact of recession, even the weakest eurozone member is now in a less challenging fiscal position than Britain.

Starting as a Greek public debt problem in late 2009, the euro crisis changed its nature in the second half of 2011. It turned into an attempt by Northern European members and the European Central Bank (ECB) to impose a new set of fiscal rules and thorough pro-

growth structural reforms onto struggling parts of the euro periphery.

This drive for rules and reforms comes with a promise: all countries that sign up to and respect the rules will be kept in the common currency by all means. The tough love approach also comes with a threat. Countries that are seen as repeatedly flouting the rules do so at their own risk.

In the US, the UK and Japan, the central bank eagerly helps out if governments, markets or the economy get into trouble. In the eurozone, the central bank holds back until the last moment. The ECB apparently lets the crisis happen to force change.

Since late 2008, the US Fed and the Bank of England (BoE) have bought government bonds and some mortgage bonds worth more than 17% and 24% of their GDP, respectively. By contrast, the ECB has only acquired assets worth less than 3% of eurozone GDP. If the ECB had taken on assets as freely as the BoE, it would have bought an extra €1.85trn of such bonds, equivalent to the entire outstanding stock of Spanish and Italian sovereign bonds.

The ECB can afford to take a much tougher line than central banks elsewhere because the ECB is de facto the most independent central bank in the world. It faces 17 rather than one finance minister. As all changes to the ECB's mandate would have to be ratified by all 27 EU members, no country can threaten the ECB with such changes.

Eurozone countries are like members of a family. They quarrel. But they also help each other. In the eurozone, however, the donors have full control over any assistance they grant. Help thus comes in the form of conditional credits. Within nation states, help usually comes in the form of non-refundable transfers. The eurozone system of mutual support is much more

efficient and incentive-compatible than the transfer systems within nation states. This explains the rapid pace of pro-growth reforms and the front-loaded fiscal repair in the eurozone.

Reacting to some market turmoil and to significant reform progress across the euro periphery, the ECB finally made it clear at its press conference on 2 August 2012 that it will not let any solvent euro member go under: Since then, the tensions have eased. Leading economic indicators suggest that the eurozone economy could return to modest growth this spring.

For Germany and the ECB, letting the eurozone falter was never an option. Without a common currency, the ECB itself would cease to exist. And for Germany, promoting European integration is the key lesson which the country has drawn from the World Wars of the first half of the 20th century. So far, the German parliament endorsed all requests to put more German taxpayer money at stake in eurozone firewalls with majorities of roughly 85%.

Under the impact of the crisis, the economic imbalances within the eurozone are now diminishing rapidly. All countries at the eurozone periphery have raised their exports fast in the last few years. Spain has turned a deficit in its net exports of 11% of GDP in early 2008 into a small surplus by late 2011. Portugal and Ireland have achieved the same turnaround in

their external balances. Italy and Greece are seeing a major swing in their net exports as well. In addition, a wave of structural reforms is sweeping through the eurozone periphery. As a result, the eurozone that will eventually emerge from the current painful period of front-loaded austerity and structural reforms is likely to be a more flexible, coherent and dynamic place than before.

The future eurozone will be neither a nation state nor a full fiscal union with largely harmonised tax and spending policies and huge automatic transfers between regions. But it will be a region with rules that will make it much more difficult for member countries to live beyond their means in the future. This is the core of the fiscal pact ratified last year. The few elements that are still missing are some details of deficit surveillance and a joint supervision of banks within the eurozone. As tensions have subsided, the eurozone can now tackle these residual issues without undue haste. Although major risks remain, the region by and large now seems to be on the right track, with reforms starting to show first results.

Holger Schmieding

Chief Economist, Berenberg Capital Markets

Seeking Mr Cameron's position

David Cameron is expected to hold a speech about the UK's place in the European Union. Among other things, he is expected to discuss plans regarding negotiations between the UK and the EU for a 'new deal' and a possible referendum.

Week by week the expectations for this speech have been increasing. This has incited speculation because Cameron has not yet defined his position. What we do know is that the Prime Minister has received warnings and suggestions from many sides. The dispute over the role the UK should play in relation to the European Union is an expression of a conflict within the Conservative Party that has engaged the political elite

for months and is exacerbated by the tabloid press and the United Kingdom Independent Party (UKIP).

The Prime Minister would like to have kept his distance from EU-related topics in this term of office. His predecessors faced significant difficulties over EU issues due to the Union's unpopularity in Britain. Bearing this in mind, along with the fact that Cameron entered into a coalition with the only clearly pro-European party, the Liberal Democrats, it would have seemed advisable for him not to open discussions on fundamental questions. And there was no reason to assume that the EU would become such a dominant issue when his government entered office in May 2010. The Lisbon Treaty, a comprehensive reform of the European Union, had been in effect for half a year. A further extensive reform did not appear necessary, neither was it sought by other member states. At that time the consequences of the banking and economic crisis were not foreseeable, as they quickly gave way to a large-scale debt crisis. This resulted in an unprecedented pace of negotiations and efforts to further develop the EU.

Such times require a clear orientation of where the government's interests lie, which goals it wishes to achieve, and what the best strategies are to accomplish these goals. As an observer, one gains the impression that Cameron lacks such an orientation. This explains the great interest in the forthcoming speech. It raises the hope that this speech will finally define the UK's position: where should Britain's place be in the EU? What strategy will he use to secure British influence? And who will be Britain's partners in that process?

This situation plays into the hands of the so-called eurosceptics. They rarely miss an opportunity to push the Prime Minister around and to force him to make concessions. It is misleading to speak of eurosceptics. It is not eurosceptics who attempt to dominate these

discussions, but rather politicians who are convinced that it is in Britain's interest to leave the EU.

In a certain sense Cameron himself allowed this opposition to grow within his own party. It may have been in the hope of tackling the anti-European views within the Conservative Party which are still only held by a radical minority, or due to his own indifference towards EU issues, or both, but Cameron has continued to grant concessions to this minority to gain support for his own priorities. This first occurred in 2005 when he promised to withdraw his party from the EPP Group in the European Parliament and form a separate parliamentary group. This secured Cameron his election to the position of party leader. In 2009, after the European election, he finally implemented his pledge. As a consequence, the British Conservative Party's influence in the European Parliament became insignificant and Cameron is no longer represented at decisive preliminary meetings of the heads of government before EU summits, with dire consequences. The conflict over the best strategy for the government in EU-related matters is no longer carried out in the European Parliamentary Group, but in the House of Commons.

This is also the background for Cameron's veto of the Fiscal Pact at the EU summit in December 2011. A lack of preceding coordination, sufficient partners and support in the Prime Minister's own party prevented the negotiation of a settlement that all member states could live with. Thus, the United Kingdom found itself alone.

It is illusory to believe that those who are determined to have Britain withdraw from the EU will be satisfied with compromises. Their goal is an in-out referendum that they are determined to win. This raises questions as the Prime Minister now appears to consider offering a referendum. The idea is not for an in-out referendum, laying the foundation for further

discontent among the anti-Europeans. The government has rather begun to carry out an analysis of how EU law affects Britain – be it advantageous or in their view harmful. The goal is to identify all areas in which renegotiation is sought. The process is planned to be completed after two years, giving way to direct negotiations with the EU. These negotiations are to establish a new relationship with the Union. Finally, the voters are to be asked in a referendum whether they agree with this new relationship. This procedure makes it impossible to say at this point what this referendum will cover or even when such a referendum will take place.

Many Tories are counting on Germany more than anyone else for support in the negotiations. They are convinced that Germany has a great interest in keeping the United Kingdom in the EU and would therefore help negotiate a 'new deal' for the UK. They are correct: Germany does have a great interest in keeping the United Kingdom as a partner in the EU. This, however, should not lead to the conclusion that the British can count on German support for a new deal. Past reactions in Germany have been quite prudent. A group of British Conservatives visiting Berlin in September of last year was quite surprised to find out that their German colleagues had the impression that Britain is striding down a path leading out of the EU. The message was clear: what sense would there be in negotiating with a partner who ultimately does not want to be a member of the club? Gunther Krichbaum, chairman of the EU committee of

the German parliament, made the point even more clearly during a visit to London last week: 'In the broader sense of negotiating a new treaty, it is neither wise nor useful to open a Pandora's box.'

Furthermore, one must bear in mind that it will not suffice to have only Germany on Britain's side. Negotiations with the EU are not bilateral talks: the UK is on one side and the EU on the other. They are rather talks in a relation of 1 to 26. That does not always seem clear.

The Prime Minister himself continues to assert that he does not wish for Great Britain to leave the EU. However, one detects little active effort on Cameron's part to campaign within the United Kingdom in favour of the country remaining in the EU. He rather seems to expect the European Union to make him an offer that would allow him to persuade his country to remain in the Union. Conversely, this would mark a failure to fulfil his claim to be an active framer of policy. Instead, he has made the United Kingdom dependent on the EU in regard to the most important issue, namely membership, despite the fact that he actually opposes a relation of dependency.

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