



The David Hume Institute



Seminar 23 April 2003

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Professor Jim Rollo, University of Sussex

**“The Challenges and Opportunities of an Enlarged EU.
One Europe or Several?”**

Enlargement and Governance Challenges for the European Union

Jim Rollo

University of Sussex

Director, One Europe or Several?
Research Programme of the ESRC

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A Brief Road Map

- Examine three challenges in the context of EU Enlargement
 - the meat and potatoes issues of the budget, agricultural policy and the Structural Funds
 - the challenges to EMU from enlargement and and to the new members from EMU
 - and finally the constitutional challenges of enlargement
- from 2 perspectives that of an applied economist and that of Director of the One Europe Programme

Some numbers

- Enlargement
 - 10 countries, 75 million people of whom half are Poles
 - Poor (adds less than 5% to EU GDP)
 - agricultural (only Cyprus, Malta and Czechs have a sector of a similar weight to the EU average)

Agriculture, the Structural Funds and the Budget

- The Context
- Agriculture
 - the mid term review
 - the WTO
 - Enlargement
- Structural Funds
 - Copenhagen Council
 - the existing member states
 - the new member states
- the Financial Framework 2007- 2013

The Context

- Structural Budget deficits in the EU-15 core
- Stability Pact under pressure but necessary for EMU credibility
- everyone short of tax revenue
- existing payers look to cut net contributions
- existing net recipients look to sustain net receipts

Agricultural Reform and the mid term review

- support price cuts for all but Sugar
- Aim to make direct payments production neutral
- favour small producers over big (Minimum 1500 euro payments, degression above 50,000 euro)
- heavy regulation (environment, food safety, animal welfare)
- budget broadly frozen until 2006
- no discussion of frontier protection
- France and Ireland likely to resist; Germany mainly interested in cost but also food safety and environment; UK worried about impact on big farmers

The WTO dimension

- Doha Development round
- Demands from the rest of World
 - end production linked support
 - end export subsidies
 - increase market access for basic products
- mid term review only deals with part of that

The Enlargement Dimension

- Copenhagen left new members with no more than 25% of direct payments commonly financed in 2004 rising to 100% by 2013
- budgetary pressures if nationally financed top up
- big agricultural populations but poor infrastructure so may find it hard to take advantage of rural development funds and meet required standards for direct payments
- liable to be resistant to reducing border protection as main source of support to farmers
- looking for more direct budget support for infrastructure after 2006

Structural Funds

- Problems for the Funds
 - net contributors liable to lose willingness to pay
 - current recipients want to maintain position (eastern Lander, Spain, Greece, Portugal, mezzogiorno, even rich Ireland)
 - new members may have difficulty reaching cap of 4% of GDP
 - if so, may look for simpler disbursement rules/lower co-financing
 - if not, impact on structural funds could be 25Bn euros by 2013
 - unanimity on structural funds so everyone - net contributors, current beneficiaries, new members - has a veto

The Budget

- **The enlargement package was mean and that may poison the new members' attitude in future negotiations**
- **The net contributors have sown up the Budget until 2006**
 - total budget at barely more than 1% of GDP
 - agriculture capped
 - cost of enlargement cut below levels foreseen at Berlin Council in 1999 let alone Agenda 2000 document which prepared the 2000-2006 Budgetary Framework
- **financial framework 2007-2013 is the battlefield**
 - the 1.27% of GDP own resources limit is not on the table
 - agriculture is frozen in real terms at best
 - structural funds a matter of veto
 - other policies on the increase (notably external and R&D)

Dynamics of Enlarged EU

- How will the battle lines be drawn?
 - a new ‘Club Med’?
 - ‘Club Med vs ‘New Kids on the Block’?
 - ‘Old Europe vs New Europe’

EMU, Governance and the Dynamics of Enlargement

- Context
- The Single Monetary Policy and other EU Policies
- Enlargement and the increased complexity of economic policy making in the EU
- Challenges for the New Members
- Challenges for the existing policy framework

The One Europe? Context

- One Europe? set out in 1998 to examine 2 main set of issues with regard to EMU
 - The governance issues (Begg et al, www.sbu.ac.uk/euroinst/oneeurope/papers.html) emerging from
 - Decentralised fiscal policy making and centralised monetary policy
 - Regional policy implications
 - Other economic policy issues (labour markets and Lisbon process in effect)
 - The impact of EMU on the ‘outs’ and the ‘nearly ins’ (M Nuti, <http://facultyresearch.london.edu/docs/dp8.pdf>)

Did these turn out to be relevant issues?

- Stability Pact under strain (inflexibility of SGP ‘stupid’ R. Prodi, Le Monde october 2003)
- ‘all the institutional preconditions for a stable currency and for steadily improving the prospects for long term economic growth are in place in Europe today.’ ECB Monthly Bulletin Feb 2003 p 47
- ‘Although the popularity of intermediate [exchange rate] regimes [similar to ERM II] in emerging markets has declined.... corner regimes are in a ‘trial phase’ ... [and] ...floating plus inflation targeting will be worth monitoring.’ Discussion of exchange rate regimes for emerging markets (eg new members) ECB Monthly Bulletin February 2003 p.62

The Single Monetary Policy and other EU Policies

- Begg et al argue for more centralised economic policy regimes.
 - Danger that decentralised fiscal policy too tight in aggregate and insufficient incentives to comply with SGP
 - Regions more vulnerable to asymmetric shocks under EMU and need for increased central funds
 - Open method of co-ordination too weak and uncertain to deliver required economic flexibility

Enlargement and Increased Complexity of Economic Policy Making in the EU

- Increased diversity and number of small states and implications for
 - ECB governance (already problems with Finns on proposed reform)
 - Financial stability issues may be more pressing
 - Potential loss of political sustainability of structural funds as diverted eastwards?
 - Makes OMC more relevant but impact potentially less

Challenges for the New Members

- ‘Catch up’ growth and the appropriate exchange rate regime
- Managing ERM membership
- Managing EMU entry
- Fragile financial sector, foreign exchange inflows and EMU

Challenges for the Existing Policy Framework

- Does the increase in the number of sovereign states & in economic diversity
 - make reform of ECB governance impossible?
 - Require more or less centralised economic & fiscal policy making?
 - Require more diversified targets for monetary and fiscal policy regimes?

Is efficient reform of ECB governance impossible?

- The current proposal suggests that countries lose voting rights for varying lengths of time based on share of Eurozone GDP to conserve current total of 21 votes.
- This is thought to be too big for modern practice
- but regional chairs (following the 'Fed' model) are rejected as are IMF style Constituencies
- increase in number of small countries make any change which marginalises them further difficult

More or Less Centralised Economic & Fiscal Policy Making?

- This is the major conundrum
 - More diversity suggests less centralisation ie less prescriptive/ more flexible SGP

OR

- more centralisation but with much bigger ‘cohesion funds’ to help manage strains of ‘one size fits all’ policy regimes

More Diversified Targets for Monetary and Fiscal Policy Regimes?

- Rapid catch-up growth in new members combined with open capital markets and high fx inflows suggests
 - need for higher inflation target for new members
 - An SGP that is more subtle in its targeting eg recognises desirability of tight fiscal policy regimes in new member states

Conclusions?

- The existing tensions in the economic policy domain in the EU 15 will be significantly intensified by enlargement
- Whether this ends in more or less centralisation of policy may depend on whether the new member states (Poland apart) act similarly to ‘small states’ in the EU-15 and push for more integration/centralisation or not.

Highlights from the One Europe? Results and the Convention on the Future of Europe

- 4 areas
 - A Europe without borders
 - A diverse Europe
 - A flexible Europe?
 - Institutional Europe

Europe without Borders

- porous borders in Central Europe encourage informal ‘Europeanisation’ through trade, investment and movement of people.
- EU Membership with hard borders will be ‘EU-isation’ at the expense ‘Europeanisation’
- Social disruption and economic cost will follow for the excluded

A Diverse Europe

- Diversity across Europe at national and regional level is a source of cultural, social and economic dynamism
- Diversity especially marked in Central and Eastern Europe
- Risk that over-rigid EU policies or constitution will stifle some of the dynamism

A flexible Europe?

- Visions of Europe differ
- One size fits all may limit the ability of the EU to maximise the dynamic gains from integration east and south
- The challenge for European governance is to manage diversity and conserve dynamism

Competences, subsidiarity and institutional balance in the emerging draft Constitution

- The draft suggests very few sole competences for the Union or the member States.
- a focus on subsidiarity
- 6 member states and Giscard d'Estaing favour twin executives.
- A President of the Commission elected by the European Parliament

Institutional Europe

- The European Parliament increasingly acts like a normal parliament. Cleavages increasingly along European party and not national lines

Implications for the Convention on the Future of Europe – diversity

- The convention must engage with diversity of views at national and regional level notably and not only in the new members.
- Engaging national parliaments and regional bodies in scrutiny and legislation and emphasising mixed competences and subsidiarity makes sense.

Implications for the Convention on the Future of Europe – Flexibility

- The Open Method of Co-ordination a useful antidote to one-size-fits-all policies but serious costs in terms of enforcement, transparency and accountability

Implications for the Convention on the Future of Europe – Institutions

- The European Parliament increasingly acts like a ‘normal’ parliament and should be trusted with more powers to hold Commission and Council to account
- Paradoxically the European Parliament electing the President may reduce its independence - so consider direct elections?
- But beware the effect that partisanship may have on the traditional brokering role of the Commission particularly confronted with a stronger Parliament and President of the Council

Unifying Themes?

- The Challenges of Diversity
 - European visions and national cultures
 - big versus small
 - pursuit of growth versus pursuit of stability
 - flexibility versus rigidity

and this is not the end!

- Bulgaria/ Romania promised by 2007;
- Turkey to open negotiations in 2004?;
- Croatia has an application lodged
- rest of Balkans offered the possibility;
- Norway, Switzerland, Liechtenstein, Iceland
- Ukraine/Belarus?
- Russia??
- Transcaucuses????