Slide or growth in Europe?
Alternative economic policies and the European social model
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Abstract
Since the mid-1980s, the mismanagement of European economic policy has appeared as one of the main causes of the slow growth. After the brief 1998-2000 recovery, the blocking factors are again fully at play. The EU is all the more up against the wall as its enlargement to Eastern Europe represents an additional challenge. The EU is locked into a slow growth process and rising inequalities because of its institutional framework. Manifestations of its decline are multifarious. Most of the principles currently governing the EU are at issue. The welfare systems which appeared as one of the pillars of European societies have been gradually questioned. Alternative proposals are sketched out, laying first the emphasis on macroeconomic policies (European budget, ECB, wage policy, revival of the European Social Model). A new design of structural policies is proposed (an active research policy, an industrial policy, the reinforcement of public services, a preserved regional policy to assure cohesion, a reformed common agricultural policy, a more balanced trade policy). However, these proposals seem far removed from what can be ultimately expected from a EU-25. Several new leads could be envisaged within the framework of a Europe with differentiated management systems but capable of maintaining a cohesion policy and supporting large structuring programmes.

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Since the mid-1980s, the mismanagement of Europe’s economic policy has appeared as one of the main causes of the distortion between European and American growth rates. The EMS was functioning asymmetrically and the countries with weak currencies bore the adjustment costs burden. In 1985, instead of bringing solutions to the already identified blocking factors, it was decided to use market forces to rekindle Europe with the Single Market programme. According to the then prevailing liberal approach, growth and innovation were to be encouraged by both the completion of a large domestic market and the reinforcement of competition. In the early 1990s, financial liberalisation and the increasingly rigid EMS mechanisms made a change of the monetary regime necessary. The single currency prevailed without the obvious consequences in terms of economic policy organisation being ever envisaged. The project was shaky from the very beginning. However, the benefits of the single currency were thought to be determining and its costs largely underestimated. Furthermore, the transitory measures towards the single currency adopted in Maastricht in December 1991, added to the aftermath of the German reunification, contributed to the halt of European growth during the long 1992-1998 transition period. After the brief 1998-2000 recovery, the blocking factors were fully at play again and the risks of an economic slide reappeared. The welfare systems which were specific to each country and appeared as one of the pillars of European societies have since then been gradually questioned. The EU is all the more up against the wall as its enlargement to Eastern Europe represents an additional challenge.

The European Constitution project was a kind of answer, though largely open to criticism. Its rejection was salutary but did not result in a “plan B”. The EU is still suffering from persistent paralysis and is locked into a slow growth process and rising inequalities (1). Alternative proposals are sketched out, laying the emphasis on macroeconomic policies and the European Social Model (2) as well as on structural policies (3). However, they seem far removed from what can be ultimately expected from a EU-25. Several new leads could be envisaged within the framework of a Europe with differentiated management systems but capable of maintaining a cohesion policy and supporting large structuring programmes (4).

1. A persistent paralysis

The EU is locked into a slow growth process because of its institutional framework. Manifestations of its decline are multifarious. Most of the principles currently governing the EU are at issue.

The Growth and Stability Pact (GSP) has clearly shown its pernicious effects and its theoretical foundations have been much questioned (Créel and alii, 2002; Mathieu and Sterdyniak, 2003). In theory, the GSP has two functions within the framework of a monetary union. On the one hand, it is supposed to avoid a member country’s insolvency and on the other one to prevent a country’s budgetary laxity from resulting in negative externalities through higher interest rates. Both functions are badly carried out by GSP current instruments. Monitoring the public debt ratio in GDP % can prevent insolvency problems. The rules on the 3% of GDP ceiling and on convergence in order to reach medium-term budgetary equilibrium do not take into account the less indebted countries’ rooms for manoeuvre. They do not include either the positive effects on growth of public investments or education and research spending which are eroded by the GSP constraints. As for externalities on interest rates, the public deficit criterion is also ill-adapted. These externalities only appear in case of a higher rate of inflation or a significant levy on the area’s saving. The most adequate ratio to appreciate these effects is the current account balance in GDP % which integrates both adjustments of public and private savings and investment. A country like Germany with a simultaneous significant public deficit and big trade surplus should not be concerned.
Maintaining the GSP in its current form is little justified and is the first reason why European economies are locked into a slow growth process. The flexible measures adopted in 2005 bring only a very partial answer.

The ECB’s independence is reinforced with price stability as its main goal (an inflation rate inferior to 2%). The ECB’s status is unique in the world. In the absence of a European federal authority, the ECB’s autonomy in terms of monetary and exchange policy is broader than the Fed’s in America or the previous Bundesbank’s. The exchange policy actually comes under the ECB’s sole competence and evolutions of the euro have been hardly controlled since 1999. Following the positive effects of the initial depreciation of the euro, the risk of a lasting overvaluation has been present since 2004. Improvements brought to the functioning of the Eurogroup are modest. The problem of the external representation of the euro zone has not been solved yet. Unlike in the United States, no reference is made to the goal to preserve growth and employment. The common monetary policy is ill-adapted to countries whose evolutions are asymetrical. It is too restrictive for countries in recession and too laxist for those that are submitted to inflationary pressures. The ECB’s recent project to introduce differentiation between the government securitity it will accept as a source of refinancing according to the borrower’s rating reinforces the pressure. Such a general conception of monetary policy is a second factor little contributing to sustainable growth.

Competition rules repeatedly refer to principles of an open market economy and non-biased competition. State subsidies which are compatible with domestic markets are narrowly controlled. Conversely, the interventions likely to be made at European level to stimulate supply in such areas as R&D, education as well as subsidies to the industrial sector and to large infrastructure programmes remain extremely modest. Given the current constrained national policies and limited communautary interventions, structural policies are unable to overcome accumulated backwardness. It then appears that long-term growth does not get any support.

The areas of employment and social policies are subjected to mere, non-constraining “open coordination methods”, based on the exchange of information and best practices. No provision has been made in terms of wage policy, which would however represent a major stake within the framework of an enlarged policy mix. The “macroeconomic dialogue”, introduced in the Köln process in 1999 and gathering the ECB, national governments and European trade unions has been deprived of all its substance, with the ECB solely announcing its orientations without any prior dialogue. The development of a vicious circle with a downward pressure on wages and costs in each member country contributing to stop the growth process is no mere school hypothesis.

Lastly, a Social Europe is theoretically one of the goals of the European construction, which resulted in the implementation of Social and Structural Funds or the adoption of the Charter of Fundamental Rights. However, social policy comes under the sole competence of national states. Notwithstanding each country’s strong specificities, it is at the heart of the European model and is threatened with decline in many respects. First of all, social welfare is increasingly analysed in public debates under the sole aspect of its costs. “Social costs” must be lowered in order to preserve employment and develop competitiveness. The analysis of budgetary constraints, linked to increasing health care and pension costs, is biased. Social welfare is increasingly controlled by European authorities because of its impact on public accounting. Secondly, welfare expenditures provide a new field for private capital accumulation in such areas as pensions or health care. A new, increasingly non-egalitarian and costly model is taking shape, based on privatisation. The calling into question of social welfare is used to discipline the workforce. It is a matter of “workfare” vs. “welfare”. Lastly, the Bolkenstein directive, concerning services on domestic markets and which is still being
discussed, directly threatens social welfare and public services. Its insistence on the enforcement of the “country of origin principle” may encourage social dumping.

All in all, the construction of a liberal Europe is going ahead and problems of its functioning remain unsolved, particularly within the euro zone. The easy financing in euros of intra-communautary deficits represents a growth asset in the euro zone. However, given the disappearance of exchange rates as adjustment variables, the mechanisms for a return to equilibrium in a context of asymmetrical evolutions do not seem to be adequate. Each country will react very differently in the event of a similarly important shock (Mazier and Saglio, 2004). Without a federal budget and with national budgetary policies that are constrained by the GSP, the Monetary Union is helpless when faced with asymmetrical shocks. Pressure on prices and costs remains the only answer and may still become stronger, thus contributing to locking the EU into a slow growth process.

The various studies that have been carried out these last years to improve the coordination process have led to very few operational results (Jacquet and Pisani-Ferry, 2000). The Broad Economic Policy Guidelines that are submitted each year by the Commission represent a very conventional procedure, in which the liberal orientations are constantly reasserted, and without much practicality.

The enlargement to Eastern and Central European countries raises new problems. An optimistic approach consists in underestimating its impact and expecting an additional 4% growth within the next 15 years for the new countries (Bchir et al, 2003). However such an optimistic approach ought to be put into perspective. Although Central European countries seem to be in a better position, the most peripheral ones may become marginalised (Dupuch et al, 2003). Regional and income inequalities are likely to increase, which poses the problem of the CAP and regional policy. Unlike with the previous enlargements, the EU-15’s support is minimal since net transfers, for the 2004-2006 period, will account for a yearly amount of 0.8% of the new members’ GDP.

The functioning of the EU-25 will have to face many difficulties in the years to come. The trend for the European Union to become a free trade area submitted to sole rules of competition will be reinforced. As in the 1980s and 1990s, growth will not really be the order of the day. This construction fits in rather well with the liberal model, i.e. a huge single market, an independent ECB as the guarantor of price stability, a single financial market currently taking shape, competition and trade policies as incentives for the implementation of new liberal measures, a limited communautary budget and nation States that are paralysed by budgetary constraints. Weak growth will be partly offset by the new investment opportunities that the liberalisation and privatisation of public services will continue to provide to private capital. Due to the increase of income and regional inequalities, there will be losers and winners. However, the absence of growth, persistent social tensions, deadlocks of European policies and the backwardness in the fields of new technologies still remain a problem. The proposals contained in the Sapir (2003) report and aiming to boost Europe’s growth ought to be considered in this context. Though they make up a coherent cluster within the framework of today’s budgetary constraints, they constitute a minimalist approach towards European reflation.

2. A sketch for an alternative framework: the macroeconomic dimension

It is not our purpose here to bring answers to all the questions that are raised. However, we may sketch out several general orientations concerning the macroeconomic framework, the
European Social Model and medium-term structural policies\(^3\). While alternative economic policy choices may be quite easily explained as far as their principles are concerned, their implementation is a more complex thing. It is necessary to make a distinction between an enlarged EU where the risks of paralysis are big and where priority should be given to the preservation of cohesion and a more restricted dimension within which more modest initiatives could be taken.

An alternative policy will be based on a gradual increase of the European budget likely to play a stabilisation and redistribution role as well as to allow the funding of more active structural policies. The policy mix should mainly aim to sustain the demand. Its implementation will be made easier by the reform of the Stability Pact, an enlargement of the ECB’s goals and the taking into account of wage policies. The European Social Model will be reasserted as a core element. The renewal of structural policies at EU level will concern both the research and industrial policies so as to support medium-term supply, the agricultural and regional policies that ought to be pursued, and trade policy.

*The early stages of a European budgetary policy*

As regards budgetary policy, the setting of a federal budget would theoretically be the most adequate answer but it is out of reach. Two alternative solutions may then be simultaneously investigated.

The first one would mean a slight and progressive increase of Europe’s budget in order to reach 5% of GDP within a few years. Inner resources could be made available at European level corresponding to some well-adapted taxes such as a tax on saving incomes and corporate profits, which would allow to limit the effects of fiscal competition; a tax on financial transactions as well as on carbon dioxide emissions. In return, new expenditures would be made at European level in such areas as research, trans-European networks or the protection of our environment. On account of its limited size, the European budget would however play a very modest stabilising role in case of asymmetrical shocks. To come to terms with such shocks, an Employment Stabilisation Fund could be created, following the example of previous schemes that had been drawn up by the Commission itself (Italianer and Pisani-Ferry, 1992). Should its unemployment rate rise faster than the European average, a country would benefit from a transfer (either automatic or to be negotiated) from the European budget. According to estimates and provided these transfers are limited at 2% of GDP, the average annual cost for the European budget would be around 0.23% of GDP. In case of a negative shock of -1% of GDP, the stabilising and (redistributive) effect would be around 0.18% of GDP, that is to say comparable to the effect obtained in the USA through the federal budget.

The second solution would be to accept a deficit of the European budget. Financed through security issue, this deficit would remain modest, at around 1% of EU GDP so as to avoid too heavy a debt servicing in the future. With a debt capacity not exceeding 10% of GDP, long term debt servicing itself would not exceed 0.35% of GDP. Another and easier solution would be to increase the IEB’s and ERDB’s borrowing capacities. The money thus collected could be transferred to member states in case of a globally difficult economic situation such as an

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\(^3\) These orientations are partly to be found in the Euro-memorandaums that have been published each year since 1996 by the “European economists for an alternative economic policy in Europe group”; [www.memo-europe.uni-bremen.de](http://www.memo-europe.uni-bremen.de). They are presented more exhaustively in a collective work edited by Jörg Huffschmid “Economic policy for a Social Europe: a critique of neo-liberalism and proposals for alternative”, published by Palgrave MacMillan, UK, in September 2005. The more political dimensions related to the exercise of democracy and to the respective roles of the Council, the Commission, national and European parliaments are not dealt with.
symmetric shock, in order to fund specific national programmes. Such programmes could be easier to implement than major public works as reflationary measures. These transfers could also be envisaged in case of asymmetric shocks following a process similar to the Employment Stabilisation Fund’s.

Lastly, the Stability Pact should be reformed, taking into account some of proposals that have already been put forward, i.e. a public debt standard expressed in GDP %, a bearable current account standard, flexibility in the monitoring process so as to integrate effects of the economic situation.

**ECB’s independence and reinforced coordination**

The absence of any democratic control over monetary policy, nowhere else to be found, poses a major problem. This problem will remain difficult to solve as long as no fully European supranational legitimate authority is set up. Finding a solution will require a long process of political evolution on account of member states’ opposition to the adoption of a full-fledged federal organisation.

The ECB’s goal in terms of price stability (an inflation rate under but close to 2%) poses a problem. It contrasts with the British Chancellor’s goal (between 2.5 and 3.5%) and also with the Fed’s even less constraining position. Such a choice should be the subject of an in-depth public debate with political leaders. An excessive inflation eradication may lead an economy to fall into the “liquidity trap”, as illustrated by Japan’s case. Complete price stability limits the efficiency of monetary policy as an instrument to support the economic activity.

More fundamentally, broadening the ECB’s goal so as to encompass full employment and social cohesion would restore employment its central position in the economic policy. Such a change would ease coordination problems and would put the ECB on line with other central banks’ (including the Fed’s) goals.

Furthermore, the ECB’s modes of intervention ought to be diversified, on the model of Anglo-Saxon Central Banks’. In those countries, the Central Bank may buy (or sell) and be the sole holder of Government’s or Federal Agencies’ security instead of holding them subject to repurchasing agreements, in the form of mere guarantee, within the framework of the refinancing operations designed to help commercial banks. It may thus intervene more directly in the liquidity creation process so as to support the economic activity or curb deflationary pressures when it estimates that banks’ refinancing demands are insufficient.

Such a possibility was explicitly eliminated in the ECB’s case, notably because of the Bundesbank’s strong opposition for fear of inflation pressures linked to an excessive credit creation. A more dispassionate reappraisal of this point would be necessary.

The exchange markets’ instability points to another European monetary institutions’ major flaw, i.e. the absence of any clear orientation in terms of external policy. The exchange rate policy is in fact completely in the ECB’s hands and the European Council can only intervene in exceptional circumstances, for example in case of a “manifest misalignment”. The prickly problem of the euro zone’s international representation contributes to reinforcing this difficulty. The exchange rate policy ought to be appropriated again by the Council and the Eurogroup. The nomination of a “Mister Euro” to represent the Council would testify to this new role distribution. In general terms, the goal of the exchange rate policy could be the setting up of “flexible target zones” among the main currencies with more or less important fluctuation margins around reference parities calculated on the basis of fundamental equilibrium exchange rates.

An explicit exchange rate policy would also make the elaboration of a policy mix more coherent. In addition, democratic principles would be better respected since the Council, as the representative of national governments, is the only one to have unquestioned democratic
legitimacy. We would then get nearer to the institutional schemes prevailing in the USA or Japan where the Central Bank is not the only one responsible for the exchange rate policy. The current economic situation shows the seriousness of the problems linked to the absence of European coordination mechanisms and to the ECB’s status. Some progress could be made in several directions such as a better coordination of national fiscal policies following the efforts carried out since the late 1990s with the development of long-term fiscal programming and the convergence of national fiscal procedures, the beginning of fiscal federalism and the acceptance of a European budget deficit, the development of links between fiscal and monetary policies through the Eurogroup’s strengthened intervention capacities.

Reintroducing wage policy

To comply with the liberal doctrine according to which wage determination should be decentralised, wage setting mechanisms have so far been largely ignored. The risk is that excessive decentralisation of wage bargaining may induce destabilising dynamics. A better taking into account of income evolution appears as a necessary condition for an improved policy mix implementation at European level. Coordinated wage evolutions at European levels could imply the implementation of a multi-level bargaining system based on inflation rate anticipation but integrating national specificities and sectoral considerations. The integration of wages in collective negotiations at European level could take several forms in each country in keeping with its own traditions; i.e. regional branch negotiations in Germany, interprofessional negotiations in Sweden, branch negotiations in the Netherlands, “social pacts” signed in several European countries with very different social structures in compliance with the deadlines fixed by the Maastricht criteria. The result should be national differentiated wage evolutions, while maintaining a coherence with the policy mix components at the end of a gradual learning process. The never implemented “macro-economic dialogue”, though part of the Köln process, could then be rehabilitated.

Rehabilitating the European Social Model

Social welfare systems with contrasted forms varying from one country to another used to constitute one of the foundations of the European Social Model and made it clearly different from the American and Japanese models. Facing budgetary constraints, there was mounting pressure for a “modernisation” of those systems, by laying the emphasis on individual responsibilities and making individuals bear an increasing share of the financial burden. Depending on countries, this led to more or less extended privatisation waves and delegation toward financial actors. The Bolkenstein directive, relative to services in domestic markets, is a threat to social welfare and public services. In the face of such evolutions, it is indispensable to rehabilitate the notion of a European Social Model based on three pillars, i.e. full employment but with jobs corresponding to workers’ skills and getting them fair wages, social welfare for the elderly, the sick or the victims of accidents, based on an exhaustive social security system; social equity, that is to say the absence of social discrimination and excessive wage as well as spacial development inequalities and access to quality public services. Such a notion of a European Social Model contrasts with the more liberal, more non-egalitarian and less solider “American model”, which is more individualistic in its approach and in which market and competition mechanisms are the rule. It is against orientations clearly displayed in some of the Commission’s recent documents. There can be several versions of this model according to each country’s traditions and past experiences. The short or medium-term convergence of national models is not realistic. There is even a risk that the
increasing mounting disparities and reinforced competition at play within the enlarged European Union may put foundations of the European model into question. Current trends ought to be reversed, by showing that social welfare can be maintained on the basis of fairer – but just as efficient- public systems than private ones. This applies both to pay as you go pension schemes and to health care systems. Such questions obviously depend on national choices but are also increasingly submitted to constraints and directives imposed from Brussels. The rejection or the in-depth amendment of the Bolkenstein directive here appears to be an essential element at stake.

Furthermore, procedures could be implemented so as to compare and assess the policies carried out by the different member countries, based on the open coordination method that has been used within the framework of the European employment strategy since the late 1990s.

- Minimum levels, varying according to countries, would be fixed as goals to be reached in terms of minimum wages, social welfare and pensions. In some cases, more constraining procedures could be envisaged so as to ensure the enforcement of minimum standards, e.g. in terms of minimum wage or pension level that would be fixed in % of the country’s per capita income. In any case, a non-regression clause ought to be set up in order to avoid any form of social regression.

- In the context of a rising European budget, an amount varying between 0.5% and 1% of EU GDP could be devoted to a European Social Fund to finance social transfers aiming to reach some of the minimum levels previously fixed, notably in terms of pensions or social welfare. Such a Fund would primarily help the less advanced union members gradually integrate the European Social Model. It would thus revive the harmonisation and convergence principles that have ceaselessly governed the European construction for forty years.

Employment policies are another area in which progress could be made. Though these policies are unable to solve the unemployment problem, they play a positive role by contributing to help the less privileged social groups, rise qualification levels and improve working conditions. Within the European employment strategy framework implemented since 1997, the open coordination method has represented a unique process so as to help national policies through a repeated process of information exchange and a harmonisation effort in their goals and programmes. All in all, the measures that have so far been taken have reinforced the trend towards more flexibility.

However, the method can be retained and improved under several conditions. The restrictive framework of the Broad Economic Policy Guidelines as presently formulated and including the European employment strategy ought to be abandoned. Social partners should be more closely associated and workers’ representation reinforced. The goals should go beyond mere employment rates. Recommendations for more flexibility ought to be reappraised in the light of bad results that have so far been obtained. Active employment policies ought to be more inspired by Scandinavian countries’ experiences, giving more room to solidarity and offering wider choices than by schemes inspired by the workfare and more characterised by the mere disciplinary aspect.

As far as employment is concerned, European legislation is still in its embryonic stage, notably in the fields of part-time work, women’s labour and workers’ consulting. However, the standards that have been fixed are low and can even be wrongly used by the most advanced countries to justify backwardness in these areas. Enforcement conditions are not constraining in less advanced countries. Such a situation ought to be reversed considering the fact that the upward convergence of labour condition is one of the Treaties’ goals. Such a
necessarily gradual evolution could primarily concern the following points: the reinforcement of workers’ rights to training and education and the substantial improvement of labour conditions in some atypical jobs.

3. Towards more balanced structural policies

In terms of structural policies, the European institutional framework is characterised by several major trends; i.e. the preeminence of the communautary competition policy, the Single Market logic giving priority to economies of scale, the weakness of the communautary research policy, the absence of a truly European industrial policy, the overpowering CAP and regional policy, and lastly too liberal a European trade policy. Most structural public interventions are organised according to national specific models. However, in many cases the European competition policy plays an increasingly important role by imposing restrictions to national interventions which are not offset by broader interventions at European level, in accordance with the liberal doctrine. A return towards a more balanced situation is highly desirable, by giving impetus to a more active research policy, establishing an industrial policy at communautary level, reinforcing public services, giving regional policy a new orientation, maintaining –while thoroughly transforming it- the CAP and lastly redefining the European trade policy.

A more active research policy

The reasons for the deterioration of external performances in high technology areas in the 1980s and 1990s are many but essentially lie in the weaknesses of research policy, both at European and national levels. Compared with US policy in these sectors, national policies supported by diversified national innovation systems have lacked coordination. Global funding has been insufficient. The average R&D European effort represents around 1.9% of GDP against 2.5% in the USA and Japan and no country, with the exception of Sweden, does better than America. Research and technological development framework programmes (RDFPs) have suffered from several shortcomings : the insufficient commitment of large companies that have been reluctant to cooperate on major projects and have often proposed second-ranking ones, too complex a procedure that has been an obstacle for small and medium-sized firms, a multiplicity of goals which is hardly compatible with the uniqueness of communautary rules, the inadequate character of the pre-competitiveness notion, the perverse effects of the unanimity rule to the detriment of a necessary focus on priority projects and leading to sprinkling, the use by some countries of the RDFP as a substitute for dwindling national funding; and lastly the quantitative weakness (15bn euros for the 5th RDFP between 1998 and 2002; 17.5 bn euros for the 6th one, between 2002 and 2006).

As for the EUREKA programme, it is an intergovernmental cooperation mechanism whose flexibility is acknowledged and based on companies’ and laboratories’ initiatives. However, it has been subject to progressive erosion due to some nations’ lesser commitment, the smaller size of funded projects and a loss of financial credibility.

Several improvements have been carried out in the last years. The abandonment of the rule of uniqueness since June 1999 has opened the way for larger selectivity at RDFP level. The possibility to exceed the pre-competitiveness criterion should permit the funding of projects closer to industrial application. The 2000 Lisbon Summit clearly stated the will to catch up in the knowledge economy area but the mobilised means have so far consisted in mere incantations. It is necessary to go further than this.
Rationalising procedures

RDFP procedures have become too complex. Specific regulations ought to be implemented according to the nature of operations that are funded, distinguishing between public research, of a more fundamental nature, and industrial research:

- as far as long-term, upstream research is concerned, greater freedom of proposals ought to prevail, essentially based on public funding;
- as for industrial research, the definition of priorities would be based on firms’ continuous participation, with a real commitment from bigger firms, but the latter should not be the only ones to impose their views;
- for short-term projects and in order to bring more direct support to small and medium size firms, the benefits from the EUREKA programme ought to be mobilised. This programme, while keeping its flexible functioning, ought to be integrated to the RDFP so as to overcome today’s deadlocks.

Communautary-funded support to small and medium size industries’ innovation ought to be transferred to regional bodies for greater efficiency. Some of the RDFP aids actually correspond to a cohesion goal in favour of some nations and ought to be integrated to the regional aid policy financed by Structural Funds.

Setting up new means both at budgetary level and at the level of the instruments that are mobilised

- The RDFP financial provisions ought to be increased to around 0.4% of EU GDP, so as to permit the funding of major schemes at European level without dismantling national programmes.
- Specific cooperation programmes could be launched in separate areas, based on autonomous but somehow continuous budgets and structures.
- European technological agencies in charge of the promotion and coordination, at European level, of programmes in the fields of IT and biotechnologies could be set up.
- European public research organisations, more in charge of fundamental research, could also be set up.
- The creation of a European patent is a key issue for the protection of intellectual property in sensitive sectors like biotechnologies and IT. The cost of patents in Europe is much superior to what it is in America and a European patent would limit the complex nature of the procedure and reduce translation and examination costs.

Industrial policy and major programmes at European level

The notion of industrial policy is hardly to be found at communautary level and remains unfamiliar to many member states’ culture. It was acknowledged in 1994 only under the name of “industrial competitiveness policy”. It is restricted to horizontal measures aiming to improve companies’ environment and remains submitted to the overarching competition policy. A broader approach to industrial policy appears necessary and might be devised around the following points.

Rehabilitating big public programmes at European level

Several fields would be concerned. First of all, technological programmes concerning specific projects such as the Galileo project, which was revived at the March 2002 Barcelona Summit, or the troop carrier project. These high technology projects would stimulate several European research groups and laboratories and lead to the development of cooperation networks.
Secondly, infrastructure programmes that would appear as necessary complements to the liberalisation policies implemented in public services. Europe could set up masterplans in the areas of transports, electricity, gas, telecoms or the post office, including either publicly or privately funded investment programmes. Operation management would no longer depend on intergovernmental coordination but on financially independent operators in charge of the achievement of individual projects. Rail transport is the most exemplary sector where to initiate this kind of project, as illustrated by the December 2003 Commission’s recovery-plan.

**Setting up regulation instruments**

National regulation agencies have been created in several service sectors (telecoms, electricity) within the framework of liberalisation policies. The setting up of European regulation bodies, connected to these national agencies, seems necessary. Well-designed standardisation at European level may be a powerful instrument to reinforce European firms’ position, as illustrated by the GSM standard for mobile phones. Such a practice could be extended to many areas (technologies and clean goods, insulating materials). The reinforcement of standardisation bodies common to all European countries is to be encouraged.

Sectoral interventions, promoting specific infrastructures or instruments, could be set up in cooperation with the firms in the concerned sectors.

**A more pragmatic competition policy**

The European policy aiming to control anticompetitive agreements should be less concerned with maintaining strong competition considered as an efficiency factor. The economic dimension ought to be better integrated by admitting that in many sectors firms’ competitiveness is based on the lasting relationships existing between different protagonists, authorizing trade alliances and proposing standard contracts for cooperation agreements. The monitoring of concentration, as the key device of competition policy, should also be made more flexible. The definition of a “pertinent market”, on which the risk of having leaders is assessed, ought to be spread to the whole world instead of being limited to the sole European –if not sometimes national- dimension. A dynamic vision integrating markets’ future evolution instead of being restricted to the sole impact of effective competition should prevail. Concentration is generally more limited in Europe than in America and medium-size firms are weaker. Given the circumstances, European firms should be able to reinforce their positions without being penalised against non-European competitors.

Governmental aids are banned to prevent unilateral measures from creating imbalances and distorting competition. Theoretically, only the aids having a general impact and not benefiting certain firms or sectors are allowed. Practically, some dispensations already exist to help weaker regions, support small and medium-size firms as well as the environment and R&D sectors. The existing monitoring devices should be more flexible and coherent. By being more flexible, they would not aim, as at present, to promote a unilateral strategy of national aid reduction. By being more coherent, they would guarantee a better articulation of national aids monitoring with existing European policies, notably in terms of regional aids financed by Structural Funds or research-oriented aids.

**Preserving and reinforcing public services**

Public services, also known as “general economic interest services”, according to the Commission’s terminology, correspond to the supply of goods and services that are essential
to an individual’s daily life and to the exercise of his fundamental rights: guaranteed access to energy, health care, transports, telecommunications, education all over the territory, without any discrimination and on equal basis for everyone. They contribute to economic, social and territorial cohesion and may be provided, under certain conditions, either by administrations or by public or private companies. They are at the heart of the “European Social Model” but have been directly affected by the liberalisation and competitive policy implemented since the 1990s.

In the EU founding treaties, competition remains the basic principle, though there is a place for “general economic interest services”, by allowing nation states to define, with a relative autonomy, the range of their public services. On the other hand WTO, with its General Agreement on Trade of Services (GATS), constitutes a general framework which is particularly constraining and worrying for public services. The Bolkenstein directive accentuates this phenomenon. However, within such an unfavourable context, three points ought to be stressed as they give some room for manoeuvre:

- The acknowledgement of the “network” notion in various directives, characterised by persistently increasing yields in some sectors of activity, justifies the maintaining of a monopoly status in the corresponding areas and permits public interventions but without clearly explaining their form.
- The obligation of a “universal service” is also clearly admitted in sectoral directives with the following definition “a cluster of minimum services of a given quality, accessible to everyone at an affordable price”.
- The “general economic interest service” mission was recently reasserted in recent documents, notably in the European Charter of Fundamental Rights. Until now, these texts have had little operative impact but the principle of a European law may open a new legal framework.

Three options may be envisaged to preserve the role of public services.

The first one consists in allowing public services to keep their national derogatory status from European competition within the framework of clear directives that would give each member state the freedom to specify its public service missions and the practical details of their deployment according to its own traditions (funding methods, private or public operators).

The second option, more ambitious, is based on the principle of framework directive specifying the foundations of public services at the European level and setting up regulatory institutions. A broader notion of “public service” than the mere “universal service” would be chosen. The general framework directive would then be adjusted to each sector of activity, taking its specificities into account. Liberalisation should not be the only way and could be combined with inter-firm cooperation. Any new step towards liberalisation ought to be specifically assessed so as to take into account the problems previously mentioned.

The third option goes further by setting up a European platform of public services that would be made compulsory to all member states, include common objectives and joint interventions of European and national regulators. Such an option would mean reinforced control over increased competition and privatisation policies. But this goal seems difficult to reach considering each country’s previous practical experiences and very different traditions.

In relation to WTO and within the GATS negotiation framework, the European Union’s mandate which negotiates on behalf of all its member states should be based on a clear idea of
the public service notion at European level. Public services, which are commonly seen as a way for any individual to exert his fundamental rights, should enjoy a specific status during negotiations. The Bolkenstein directive, which is likely to deeply question public services and social welfare systems, ought to be thoroughly amended, with special attention paid to the health care and education sectors. It should be set back in the context of a directive on public services.

Lastly, the liberalisation of network services ought to be accompanied by an industrial policy at the level of national or European regulators, handling the distortions that inevitably occur and in charge of the relations between public and private companies. This policy should also contribute to the setting up of an ambitious European infrastructure policy, likely to increase the EU’s potential growth, and based on a broad appreciation of network externalities.

A continued regional policy in the context of enlargement

European regional policies play a significant role since both Structural and Cohesion Funds accounted for an average 0.45% of EU GDP between 1994 and 1999, with much more significant funding for southern countries. A decrease has been programmed (an annual 0.4% of EU GDP) for the period 2000-2006. The efficiency of Structural Funds in the reduction of regional disparities is a subject of debate. According to some, they do not seem to have much impact (Fagerberg and Verspagen, 2000) or else, though they are significant at an econometric level, their impact remains limited. The Structural Funds that are invested in infrastructures seem to have reinforced the convergence process between countries by accelerating the growth of poor countries’ already advantaged regions without reducing the internal regional inequalities. The efficiency of these Structural Funds seems to be all the greater as the concerned region is richer (Martin, 1999).

At operational level, the setting up of projects funded by Structural Funds and their subsequent implementation require complex interactions between regional, national and European institutions. In many countries, the setting up and subsequent management of these programmes appear to be overcentralised. Given the complexity of communautary files, the exacting controlstaking place at national level and the recourse to co-funding, Structural Funds are often very slowly used up.

Beyond these usual problems, the EU’s enlargement raises considerable challenges (Begg, 2002). The adhesion to the EU of new countries means a lower average EU income per capita and bars many regions currently benefiting from those Structural Funds from being eligible (below 75%), though their situation has not changed at all. According to the Commission’s 2002 Report on cohesion, the number of the EU-15 regions below the eligibility threshold would fall from from 46 to 19. It would be possible to raise this threshold to the same level as that of Cohesion Funds (90% of the EU income per capita) but it would entail budgetary constraints that would be very difficult to overcome within the framework of a European budget limited at 1.27% of EU GDP. Concerning new members, it is envisaged to limit transfers to 4% of GDP per country to account for their limited absorption capacity, following what could be observed during the enlargement to Southern European countries. This would represent an estimated cost ranging between 0.18% and 0.38% of EU GDP, depending on whether calculations are made at current prices or at PPP. Such a budget allocation does not seem to be unbearable.

Two scenarios may be envisaged if one rejects the full redeployment strategy of regional policy towards Eastern and Central European countries, as it was put forward by Sapir (2003) in his report.
-The more favourable one proposes a European budget that would increase significantly (by around 5% of GDP within a few years). This would give more room for manoeuvre, notably to raise the Structural Funds eligibility threshold. A larger number of weaker regions could thus benefit from transfers, particularly in the less developed countries of the EU-15, which would preserve the solidarity mechanisms across the whole EU.

-Should such a scenario not be decided on account of political constraints, a less ambitious compromise could then be sought. Like in the previous enlargements, new Structural Funds could be created in favour of the new members with a maximum budget allocation of 0.4% of EU GDP. Such funding could be ensured thanks to new instruments issued both by the EIB and EBRD. The current Structural and Cohesion Funds would be redistributed among the EU-15 members with a renegotiation of the eligibility threshold and allocation procedures.

In both scenarios the Structural Funds procedure ought to be reformed for more efficiency. More autonomy ought to be given to the local, regional and national development programmes that are co-financed by Structural Funds by simplifying the Commission’s control procedures. More interaction would be achieved with the previously mentioned European technological and trans-European infrastructure programmes.

A reformed CAP

Considering the real problems posed by the CAP, there have been many reform proposals and the CAP has effectively been softened since the 80s. Pressure for a more radical reform has mounted since the late 1990s. The general trend has been to reintroduce the market notion. Four proposals may in fact be brought out.

-The renationalisation of the CAP, i.e. its abolition, is a very alluring prospect in the UK and is also to be found in Sapir’s report (2003). The British are in favour of free imports for agricultural products with guaranteed prices paid to farmers, the difference between guaranteed prices and market prices being covered by subsidies that would be renationalised and whose amounts would be fixed by each state. This proposal is apparently clever as it is open to developing countries’ imports and in keeping with free trade principles. But it poses several problems. Consumers would in fact bear the effects of the strong instability of agricultural markets. Setting guaranteed prices –as well as production levels- is an awkward thing to do. If these prices are free, overproduction appears as a serious risk. The setting of individual quotas would be indispensable but it is rarely put forward.

-The Commission is trying to reform the CAP so as to reduce its cost in the enlargement context, find room again for budgetary manoeuvres and make it acceptable in international negotiations. Its position is to alter the nature of aids and to switch from surface or per livestock ones to a system that would encourage agricultural practices and the production of amenities. The mechanism linking aids to production would thus be dismantled and production, as well as prices, would become market-oriented. This position, in keeping with Germany’s, at least encourages “good practices”. But its reference to the market, which remains central, poses a problem since history shows that the market itself is unable to ensure proper regulation in the agricultural sector. The compromise reached by the Ministers of Agriculture in June 2003 is a curious, probably transitory mixture, lacking in coherence and essentially destined to give a better image in international negotiations. The decoupling will start in 2005 or 2007, according to countries. It will remain partial for some products while it will not apply to others.

-Agricultural problems play a key role within the enlargement to Central and Eastern European countries. Communautary subsidies have been limited at 25% of current amounts per ha or livestock head, progressively rising so as to reach 100% in 2013. This ceiling, which is frowned down upon by new members, is justified in the Commission’s eyes by the
constraints imposed by the current budgetary allocation, by the fear of an uncontrolled increase of agricultural surpluses in case of higher subsidies and lastly by the redistribution problems of internal incomes to candidate countries resulting from subsidies that would be too high, compared to average national incomes.

-International negotiations within the WTO framework also raise a last series of questions. Within WTO, the debate got off to a bad start with Anglo-Saxon countries seeking to preserve and promote their interests behind alluring proposals: the acceptance of subsidies encouraging “good practices”, the progressive decrease of the subsidies creating imbalances, the defence of developing countries by the Cairns group of countries that would only benefit highly productive agricultural countries and not the most disadvantaged developing ones.

Within the 2002 Farm Bill framework, the United States re-established the practice of guaranteed prices, while putting hypocritically forward again their will to reduce these agricultural subsidies so as to eventually return to the market mechanism system. A badly handled dismantling of the CAP within WTO would harm European farmers without bringing remedies to developing countries with traditional agricultural practices.

Within such a context, it is preferable to return to the “Rooseveltian” principles that were used to lay the foundations of the agricultural policy in the mid-1930s and openly recognise the “agricultural exception”. Agricultural products cannot be solely governed by international trade laws. The instable character of agricultural markets, by increasing risks, has very negative effects on the whole agricultural sector which, in the medium-term, will largely exceed the gains resulting from comparative advantages (the risk of rural areas’ desertification and disintegration in European countries, the absence of any short or medium-term alternative activity in the poorest countries). The benefits from trade development can appear only if the pernicious effects of free markets are corrected by agricultural policy measures, in developed as well as in developing countries. The lessons from the past show us that this implies measures to support prices, on condition that overproduction phenomena should be avoided thanks to production control measures (Boussard, 2003).

Guaranteed price systems ought to be coupled with production quotas. These prices must be sufficiently high so as to lead farmers to increase their production. Quotas must be individualised and fixed so that the sum total of individual (and national) ones should remain slightly inferior to the European Union’s overall consumption. Overproduction is thus avoided and free market forces are left at play to reach the equilibrium between Europe’s internal demand and internal and world supply. Consequently, imports are free within such a framework. If it were implemented throughout the European Union, such a mechanism would contribute to stabilise the world system. Consumer prices are fixed on the basis of world prices, and consumers have to bear the aftermath of international markets’ fluctuations. The difference between consumer prices and the prices guaranteed to farmers is covered by public subsidies. Prices are guaranteed in each zone according to its development and productivity levels. Production quotas may be exchanged, but not between different zones so as to avoid geographical concentration phenomena. Lastly, individual quotas may be used to reduce production, notably in the case of big farmers. Production quotas guarantee rents that can be assessed through quota price variations, since they are tradable. Regular negotiations may help prevent excessive rent increases.

Within this framework, Eastern European countries’ integration could take place on a more balance basis without distortions between countries since the same rules would apply. Quotas would be evaluated in each country on a historical basis, with productions whose future growth potential would be limited to prevent overproduction fears. Guaranteed prices would be sufficiently high to ensure farmers a significant increase of their incomes and enable them
to modernise their production methods. On the other hand, these prices should not be too high so as to avoid distortions with the evolution of non-agricultural incomes.
Likewise, a more balanced solution could be reached within the _Euromed Agreements_ framework. The principle of free imports would open new opportunities for those countries’ agricultures. However, they tend to have a deficit in their agricultural product trade because of the rise of their cereal imports due to demographic pressure. They are confronted with the necessity to develop their food self-sufficiency, which would imply the setting up of dynamic agricultural policies that would somehow differ from the free trade principles.

All in all, the proposed solution poses two kinds of problems.
- Fixing guaranteed prices is always a difficult exercise implying difficult negotiations, with much pressure from all sides. However, the experience at European level of 40 years of CAP may make the exercise possible. The existence of periodical negotiations guarantees that the necessary adjustments will be made.
- This proposal to reform the CAP falls out of step with WTO’s principles, which should not be surprising since it is based on the idea that agricultural goods cannot be solely governed by international trade laws. Within the WTO framework, agricultural subsidies can only be used in a very restrictive way. Some are acceptable (the “green box” : environment subsidies, rural development subsidies...) while based on the decoupling principle (no links with production levels or current prices). Others are not (the ‘orange box” : price supporting measures or subsidies that are linked to production amounts) or ought to be gradually reduced. The “blue box” category is intermediate and corresponds to the situation in which farmers have to limit their production, which may be the case with quotas.

**A more balanced European trade policy**

_New orientations for WTO_

For developed countries, WTO is a forum of negotiations where concessions are exchanged so as to limit counter-productive conflicts by seeking to set up a regulated international trade framework based on the respect of competition and benefiting all on an equal par. It currently functions as the perfect instrument for the dissemination of liberal policies by imposing across-the-board liberalisation rules without taking into account either national specificities (choice of a less non-egalitarian model, social model), or unequal development levels. WTO is largely dominated by big powers, mainly the USA and the EU, contributing to the early setting up of the main orientations of negotiations. Such a functioning is increasingly criticised by large and heterogeneous coalitions that may lead to deadlock situations during negotiations. But the organisation remains unchanged with its heavy and complex procedures, and the liberalisation process continues to serve the big powers’ economic interests.

Three points could be put forward by the EU: the democratisation of WTO, the reintroduction of a more differentiated treatment of subjects and the respect of fundamental rights.

- The WTO’s democratisation is necessary in order to deprive the big powers of their de facto control power and establish a more balanced functioning. This implies giving more power to developing countries within WTO by going beyond today’s basic and formal rule of one vote per country. Agenda setting should be the result of global negotiations, with more transparency. Conference and working
group presidencies ought to be more balanced. The WTO’s functioning needs complete overhauling.

- Liberalisation rules should no longer apply across-the-board to developing countries but take the inequalities in their development levels into account. The principle of a differentiated treatment was deprived of all its substance by the liberalisation wave. It should be reinstated within WTO and it should be admitted that constraints can no longer be exerted as before considering the existing obstacles to development. Income redistribution mechanisms at global level could be included in the WTO’s principles according to development levels. Developing countries could thus benefit from a relaxation in the management of Intellectual Property Rights (IPRs), just like what has just been achieved in the field of pharmaceutical products, or maintain some protective measures as regards market openings, public procurement policies or foreign investment inflows.

- The respect of fundamental rights (the right to health care, the respect of fundamental labour standards, the defence of public services recognised to be indispensable to an individual’s exercise of his fundamental rights) ought to be put forward along with the environment protection which is already admitted by WTO. It should not be considered as an alibi likely to cause the resurgences of protectionist practices calling the principle of free competition into question, as often denounced by the WTO’s experts.

New lines for negotiations

These new lines could lead the EU to propose new orientations within WTO towards developing and industrialised countries alike. The Dispute Settlement Body’s (DSB) functioning should also be completely reconsidered.

In relation to developing countries, northern countries should negotiate favourable asymmetries so as to allow them to catch up with their development within the next 20 years. Several areas are concerned by this prospect. Temporary protectionist measures could be accepted, combined with northern countries’ continued opening. Contrary to the positions that are currently put forward, the EU would stop constraining countries to open their markets more widely and opposing those that refuse to lower their customs duties. A softer and less arrogant approach, taking more into account each country’s or area’s specificities should prevail.

A similar asymmetry should also apply to the “Singapore subjects” concerning competition, international investment, access to public markets and trade exchange improvement. As already decided in July 2004, the EU should no longer put these questions - even the last two- forward. The EU should also stop promoting negotiations on these themes with the countries accepting to do so within the framework of multilateralism.

Previous regional agreements, such as the Cotonou or Euromed agreements, ought to be similarly softened. While intra-zone liberalisation is to be encouraged so as to increase regional integration, favourable asymmetries for less developed regions ought to be negotiated.

Intellectual Properties Rights (IPR) agreements ought to be made more flexible in favour of developing countries so as to encourage the promotion of national industries, i.e. by shortening the duration of patents and introducing derogatory measures to the regulation on imitations.
Transfers could be made towards the countries providing a skilled labour force so as to cover the education costs they have to bear. Such transfers would make the policy on temporary skilled labour towards immigrants that is currently enforced in the EU more acceptable. Lastly aid to developing countries, that is currently not only insufficient but also badly affected and used, ought to be increased, provided its management is completely overhauled.

In relation to the other industrialised countries and mainly the USA, and as regards its trade policy, the EU should put forward the European model specificities that it wishes to keep without limiting itself to the sole cultural exception. The “European Social Model” and its long-term implications for health and redistribution policies comes first, but also the public services which are not limited to the mere notion of universal service. This point also refers to the GATS renegotiation that will be dealt with later on.

On the other hand, the EU should aim to restore a more balanced position of its different partners’ positions in at least three areas: European public procurements and European financial markets which were opened without any counterpart and where the reciprocity principle ought to be the rule, IPRs about which the EU is increasingly on the defensive.

In terms of IPRs, research insufficiencies within the EU play a key role. The inability to set up a true community patent valid across the whole EU ought to be overcome too. National Offices’ lobbying is here at issue, but also the shortcomings of some national courts that are competent in the subject combined with the absence of a European Court. Besides these truly European weaknesses, America’s excessively dominant positions, notably regarding the patenting of living beings, ought to be more strongly opposed (Coriat, 2002).

The DSB’s functioning ought to be completely overhauled so as to make it less unfavourable towards developing countries. While guaranteeing the multilateralism principle, the DSB ought to be deprived and placed under the United Nations’ control. It would be indispensable to establish a clear division between areas likely to be unreservedly subjected to negotiations within WTO and those that ought to be placed under the aegis of the United Nations’ competent authorities so that rules and standards could be set up. WTO would then be asked to enforce trade sanctions within this framework. For instance, concerning IPRs on pharmaceutical products, World Health Organisation (WHO) ought to be the place where rules are agreed upon in terms of IPRs and trade according to the populations’ needs and sanitary conditions. As for agricultural products, a distinction must be made between natural products and genetically modified ones whose trade regulation ought to be set up with the Food and Agricultural Organisation’s (FAO) competent bodies. The negotiations concerning industrial goods and general services would be unreservedly part of WTO. Lastly, as far as social standards are concerned, aid to development is undoubtedly the best way to make them respected in developing countries. However, if the International Labour Office (ILO) is to play its monitoring role in this area, trade sanctions could be imposed within WTO on the countries that do not respect fundamental labour standards. A global institution coming under the United Nations would ultimately cover and coordinate WTO’s, FAO’s and ILO’s sectoral authorities whose contribution would be requested to set up those rules and standards. Political legitimacy and better coordination would thus be ensured (Cling et al., 2003).

From a more operational point of view, the WTO’s sanction mechanisms ought to be reconsidered so as to reinforce their efficiency by instoring compensations for damages and effectively requiring the sectors responsible for the sentence to make their contribution, which is not the case today. Lastly, on account of the complex issues dealt with the DSB, the less developed countries ought to enjoy specific technical support.
As regards their form, negotiations ought to be carried out in the EU’s name, not by a Commissioner who makes proposals and then gets mandated to negotiate by the Council, but by a Council representative, a Mr Trade, with clearer political legitimacy as the representative of national governments.

Renegotiating GATS

The Commission’s 2003 liberalisation proposals were, its own terms, “significant and substantial”. Whereas education, health and culture were not concerned and while the post office and telecommunications retain their universal service goal, the GATS’s current framework does not provide any guarantee concerning future negotiations. In its principle, GATS encourages gradual and general liberalisation. Many declarations show that health and education will eventually be more concerned (Jennar, 2003).

If such a drift is to be avoided, it is essential that the EU’s mandate negotiating on behalf of all the Member States should lie on a clear conception of a European public services going beyond the mere notion of a universal service. Public services correspond to the supply of goods and services that are essential to an individual’s daily life and to the exercise of his fundamental rights. They are essential to the nation’s economic and social cohesion. They should enjoy a specific status during negotiations so as to be clearly excluded from any subsequent liberalisation proposal.

4. The implementation procedures

As a mere indicator, the total cost of the previously sketched out policy is estimated to reach, when fully operating, an annual 2% of the EU-15 GDP, with the following distribution: 0.4% to research, 0.4% to industrial policy and major programmes, 0.4% to regional policy in favour of Eastern and Central European countries, 0.3% to the Employment Stabilisation Fund, 0.3% to the Social Fund. Both the CAP and the regional policy in favour of the EU-15 are supposed to represent globally unchanged amounts.

While the budget allocation remains globally acceptable, the conditions for the implementation of this policy are difficult in today’s context. Any substantial increase of the European budget, even if it is very progressive, seems unrealistic. The EU-15 deadlock situations will only be more frequent in an enlarged Union. It is necessary then to distinguish between what can be envisaged at the level of a EU-25 to avoid dilution in a sort of European United Nations Organisation, submitted to reinforced competition and mounting inequalities, and what can be rebuilt on a more modest scale to give more impetus to medium-term growth, while respecting the constraints imposed by short-term steering.

Ensuring the cohesion of an enlarged Europe

The European Union’s enlargement was necessary from a political point of view but it will be difficult to maintain the cohesion of an enlarged Union. Whereas the expected medium-term consequences for Eastern and Central European countries are positive, the short-term risks of an economic slowdown, mounting inequalities and polarised activities are real. In this prospect, the extension of both regional and common agricultural policies to Eastern and Central European countries appears necessary. Regional policy ought to be linked to some of the big technological and infrastructure programmes that are also envisaged. Lastly, in order to increase short-term flexibility, the exchange rate policy ought to avoid too rapid an integration to the euro zone in spite of some Eastern and Central European countries’ pressure. As a counterpart, the euro zone countries ought to provide some aid towards
financial stabilisation. All in all, supposing the CAP extension is achieved without any budget increase thanks to the reform currently under way, the financial burden would mainly concern the regional policy extension which could be achieved through new instruments issued by the EIB and ERDB. We should not forget either to add up the progressive gearing up of the European Social Fund.

**Increasing the euro zone’s capacities to react**

The EU-15 is divided into two, the euro zone and the non-euro zone, for a period which may last long. The consequences of this situation on short-term regulation methods are significant. The euro zone’s capacities to react must be improved, which implies a reinforcement of the Eurogroup’s means of action, a deep reform of the GSP, broader goals for the ECB and real coordination with the Eurogroup, the taking into account of wage policy and lastly the setting up of an Employment Stabilisation Fund to handle asymmetrical shocks. This last measure would be the only one to have a budgetary impact. A last and non-permanent instrument would remain to be devised to sustain growth, for instance under the form of a European loan with transfers to Member States to fund recovery programmes. Progress in these different aspects is likely to remain very uneven, notably on account of the heterogeneous nature of the euro zone countries, which may imply continuing difficulties. It is still impossible to say whether more progress would be achieved on a more modest scale.

**Mobilising resources around major structuring programmes**

Structural policies might open further opportunities for individualised programmes in different areas: master plans and large programmes in the transport, telecommunications or energy sectors whose implementation would be entrusted to European operators with autonomous budgets at their disposal, the creation -in the main fields- of European technological agencies and European research agencies. The possibilities of enhanced cooperation open up useful perspectives but the practicalities of their implementation ought to be made easier. The nature of expenditures (medium-term growth supporting investments) and the required financing amounts justify the recourse to loans mobilising EIB’s or ECB’s new instruments. Such a prospect may turn out a success but previous experiences have shown the heaviness and slowness of these operations. The medium-term impact of the whole process could thus remain quantitatively limited unless it were given considerable impetus.

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