CENTRE FOR EUROPEAN REFORM

Conference report: How to save the EU

Ditchley Park, Oxfordshire
3-4 November 2017

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Executive summary

November's conference, which brought together 50 leading economists, political scientists and experts on the EU, discussed ways to save the EU from nationalist and populist forces. Britain had voted to leave the EU in 2016; Poland and Hungary were now led by governments who were chipping away at the rule of law and the norms of liberal democracy; and support for populist right-wing parties – and to a lesser extent, the populist left – was on the rise in both Western and Eastern Europe. These developments raise many questions. Which social groups within the EU have lost confidence in it and why? What does the backlash against liberalism across Central and Eastern Europe (CEE) mean for the Union? Is the EU the answer to globalisation or is it hampering member-states' ability to deal with it? Can the EU help foster an inclusive European identity, allowing it both to absorb inflows of people from poorer countries and to let national and regional identities flourish? Could the euro yet become a force for closer political integration in the EU?

Most participants agreed that the backlash against the EU – or liberalism more broadly – was not solely down to poor economic performance. Though unemployment and job insecurity did contribute to support for populism, identity and immigration were at least as important. The two also interacted in complex ways, in part reinforcing each other, and were hard to disentangle empirically. Anti-EU sentiment was also as much about hostility towards elites as it was about European integration. Support for populist parties was not obviously driven by age: the young were anti-populist in some countries, such as Britain, but voted for populist parties in large numbers in others, like Italy. A unifying theme seemed to be a sense of insecurity, resentment of elites and illusions about life outside the European Union. The complexity of the EU's machinery and laws, its recent policy failures, and the inchoate benefits of the Union also made it an easy target for populists.

There was broad consensus that the EU had the potential to be a force for good in the globalisation process, both internationally and in protecting (or at least managing) the repercussions for its citizens. But participants also agreed that the EU often fell short of that potential. Many people at the conference voiced concern that the EU was not doing enough (or was not given the mandate) to fight the negative effects of economic integration, such as the increasing concentration of benefits in certain regions, or tax competition, which citizens rightly perceived to be unfair. Some also argued there was untapped potential to integrate more closely while creating more equitable growth at the same time. On a global level, the EU did have the power to shape globalisation's rules but was not using that power effectively.

Most participants thought the illiberal backlash in Central and Eastern Europe was of great concern, with Poland seen by many as the biggest problem, mainly because of its size. But the reason for the backlash was controversial. Some argued that economics explained at least part of it, as solid GDP growth had been faster than the growth in living standards: much capital was foreign-owned in these countries, and a sizeable chunk of profits were repatriated to Germany and elsewhere. Central and Eastern Europe's electorates viewed their countries to be rule-takers, not rule-makers in the EU, and they deemed the single market to be biased in favour of the Western member-states. Some participants argued CEE countries needed strategies to create more high-paying jobs, to make the economy work for their citizens. The risk for Europe was not so much an exit of any of these countries, but a de facto exit from the values and rules of the EU. Some argued that treating CEE countries as second-tier member-states was poisonous, as was lecturing them. Offering Poland a seat at the top table was crucial, said one. But most important, argued many, was to show that Europe fights on the side of average citizens, for example against corruption, in order to support the pro-European, liberal sections of CEE countries. There was no consensus on whether EU funds should be made conditional on democratic principles and the rule of law.

Participants agreed that the eurozone was not about to undertake big reforms. Some argued that it was futile to pretend otherwise and may in fact help the anti-EU cause. But others countered that cautious steps towards further integration within the eurozone were possible, and desirable. The conference's economists did not agree that re-nationalising fiscal policy was a good idea, especially the restructuring of public debt within the eurozone. While many saw the political benefits, the economics of national discretion in fiscal policy with a common monetary policy did not add up. The euro had proved to be a source of disintegration in the EU between euro-ins and euro-outs, with one economist saying that the euro could only become a source of integration if governments overcame their current zero-sum thinking on economic policy.

Populists had made migration a central issue, and many argued that migration from outside the EU was bound to increase rather than subside, with Africa being the main challenge in future decades. The debate heated up when it came to the economic benefits of migration, with some forcefully arguing that the benefits had been empirically demonstrated, and the academic debate had been won, but not the public debate. This led the conference to discuss ways to improve the debate about migration, and whether immigration from outside the EU could be integrated into a European narrative. There was consensus that being empirical about the facts was best, but politically unlikely to be of much help. But most agreed that the way in which politicians and the press framed migration was important, as the different perceptions of migration in European countries showed. Some argued that there was scope for the EU to act, such as in Africa or to better manage the influx of migrants. As one participant put it, it was not immigration per se that worried many, but the sense that it was uncontrolled and unlimited.

Session 1: Who is opposed to the EU and why?

There is no doubting the EU's loss of popularity among member-states' electorates. But which groups – socio-economic, regional and demographic – have lost the most confidence in the Union? Is their loss of confidence largely a product of weak economic growth and hence likely to dissipate with economic recovery? Or does it reflect something more visceral and permanent, rooted in a rejection of the openness represented by the EU and a desire for greater protection and national control?

The first panellist cautioned that political scientists do not fully understand why people oppose particular political institutions. Voters' views of the EU were framed by their national political allegiances and personal circumstances, rather than the EU's policies. People who lacked trust in their national institutions tended to trust the EU's institutions. Whether support for populism, and Brexit in particular, was driven by material economic concerns or identity questions was difficult to pin down. Brexit was mostly a vote by the lower middle-class rather than the poor. While there was a compelling body of evidence that identity questions did play a role in the vote, it was difficult to determine whether hostility to immigration was cultural, or the product of relative or absolute economic decline in particular towns and regions, and the insecurity that this had bred. The divisions within countries had to be bridged, for example through greater political devolution in the UK. Indeed, the solutions mainly lay within the national sphere, not the European; governments still had plenty of national policy scope to address people's concerns. Finally, populists were able to motivate voters by providing apparently simple solutions to complex problems: almost 2.8 million more people had voted in the Brexit referendum than had in the general election a year earlier.

The second panellist argued that both external actors such as Vladimir Putin and Recep Tayyip Erdoğan, as well as domestic politicians, saw anti-Europeanism as a source of power. But it was unclear whether the EU had really lost that much popularity among electorates. There was a need to distinguish between populism, opposition to certain policies and anti-European sentiment. Those three often came together in one form or another, but not everywhere. The panellist cited the examples of Germany, Italy and France, where populist parties were opposed to certain EU policies, such as austerity or the Union's refugee strategy, but were not anti-European as such. He saw mostly fear and envy and a resentment of elites behind the populist surge: elites were well-off and had the ability to navigate an increasingly cosmopolitan society, which many voters feared. Refugees were mostly just a scapegoat for such anti-elite sentiment. What we were seeing was not really a backlash against the EU, but a broader crisis of the Western psyche. The speed of change was overwhelming, and too many citizens felt out of control. They feared that their country had lost the freedom to choose its own path.

The third panellist argued that, in the Brexit referendum, Remain and Leave voters' views on life outside the EU differed. That was also true for voters in other EU countries, whose views on how the UK would fare outside were strongly influenced by perceptions of the costs or benefits of their own country leaving the EU. Brexit had therefore provided a unique lesson for citizens from other EU member-states on what life outside the Union would actually be like. Opposition to the EU was strongest amongst those that feared they were vulnerable to a loss of prestige or pay. The problem was not that jobs were disappearing, but that the new jobs had low pay and little prestige, such as caring for children or the elderly. Finally, anti-European sentiment was complex. For example, voters could justifiably want their country both to remain in the euro and to never have joined the currency union, because the costs of exit would be huge.

The fourth panellist argued that the economic and cultural factors that drove populism interacted in complex ways. For example, if economic conditions were good, people were more inclined to give politicians (or migrants) the benefit of the doubt. But this could turn to hostility if the economic situation deteriorated. Moreover, populism could be driven by an uncertain future. For example, voters whose jobs were more at risk of automation were more likely to support Donald Trump. The panellist also pointed out that variables such as distance from the economic core of the country, or a history of foreign domination, could help explain anti-European sentiment. Also, support for the EU was not very strong even among those in favour of it. That meant that it could flip quite easily and quickly. The complexity of the EU was fertile ground for populists, whose simple message – leave the EU and the nation-state would be free to help its people – would continue to be seductive. And it would be hard to preserve the EU once populists were at the heart of its decision-making mechanisms. We needed stronger and more inclusive economic growth; the political left should continue to uphold diversity as something to cherish and defend; but Europe needed to overcome its quest for an ever closer union, instead presenting its citizens with an endpoint or a steady state to be reached.

The discussion initially focussed on the 'economics versus culture' dimension of anti-European populism. One participant cited a report by the Centre for Economic Policy Research (CEPR), 'The European trust crisis and the rise of populism', which showed that high unemployment did prompt an increase in support for non-mainstream political parties. Also, that higher unemployment tended to go hand in hand with declining trust in national and EU political institutions. However, there was little correlation between rising unemployment and attitudes to immigration, though there was some evidence that worsening economic circumstances amplified pre-existing authoritarian attitudes. Another stressed that there was only mixed evidence that people blamed the EU for the worsening of economic conditions: when asked what they would like the EU to do better, far more people cited securing borders and combating climate change than improved management of the EU economy.

Many participants stressed that it was hard to distinguish the cultural from the economic. Economic forces shaped cultural identity and aggravated cultural insecurities and divisions. Economic decline in particular regions and in small towns had eroded the identities of those localities, denuded them of young people and left them feeling insecure and fearful for the future. Similarly, economic decline had a bigger impact on the identities of men than women, because stable, well-paid employment had been the bedrock of male self-esteem, and men found it hard to adjust to the loss of status as they moved from secure and skilled employment to often casual and unskilled work. People were especially worried for the future of their children, who they feared would have lower living standards and less status than they had. The answer did not lie in compensating the losers but in improving the pay and prestige of the jobs on offer, but this was no easy task, not least because of technological change. This held out the prospect of higher productivity growth, but large-scale losses of low- and middle-income jobs.

Several participants stressed that the roots of euroscepticism lay in the sense of insecurity that increased interdependence between European countries had bred. When people were feeling fearful of the future they looked to the nation-state for protection. EU governments had to make interdependence feel safe again. Some were sceptical it could ever do this; for them the EU was impossible to reform. At the same time, no-one should doubt the EU's resilience – it had survived huge policy errors in recent years. While it suffered from a profound lack of popular legitimacy, it was still strikingly robust. Others disagreed, arguing that the EU could be reformed if only governments made the case for the EU. After all, the differences in values between EU countries were smaller than they were within member-states themselves, casting doubt on the idea that growing cultural divides between countries could explain anti-EU sentiment. Part of the problem was a lack of leadership, but it was also hard to lead a public debate about the EU because the institutional questions were so complex. Put another way, addressing the democratic deficit required electorates to have more knowledge of EU processes, which they had little reason to learn about.

One discussant argued that we should not lose sight of the fact that the EU enjoyed broad-based support. The real division was between those (such as Germany) that were satisfied with the EU and saw no need for significant reforms, and those (such as France) that were dissatisfied and wanted reform. However, this dissatisfaction did not make the French anti-EU; they had elected an avowedly pro-EU president. Given the importance of the EU to Germany, Berlin should concede ground to France whatever the outcome of the coalition negotiations. Another concurred: the power dynamics between European countries needed to be acknowledged. Greek opposition to the EU did not matter that much, but Italian and French opposition mattered a lot. French and Italian concerns had to be addressed by Germany. In some ways the French and Italian situations were more worrying than the British one: it was young French and Italians who had turned against the EU, whereas Brexit was overwhelmingly a vote by the older cohorts; young Britons were strongly pro-European.

Session 2: Is the EU still the answer to globalisation?

What are the economic challenges confronting the EU? Is the Union hitting the limits of economic integration? Or is it possible that the EU's combination of intensive market integration combined with action against social and environmental dumping and tax competition provides the best hope of reconciling globalisation with national politics? If not, is it possible to return powers to member-states without imperilling the whole project?

The first panellist argued that the EU was currently on a shaky bridge on the way to economic integration, and could either go backwards or forwards to reach more stable ground. She suggested three policies that would help the EU to integrate further, and also tackle the increasing divergence in productivity and wages between the 'best and the rest' within European member-states. First, it was essential to complete the half-finished European banking union, and especially to reduce non-performing loans. Since zombie firms were capturing capital and labour, reducing economic dynamism, a completed banking union would thus increase productivity growth across the economy by funnelling savings towards more productive investments. Second, the still severely restricted single market in services should be developed further. The restrictions in services trade kept services firms small and did harm to exporting manufacturing firms, too. Finally, the digital single market was underdeveloped and needed to be completed to foster productivity growth.

The second panellist said that the EU was still a good response to the Rodrik trilemma (that countries must choose two of three options: far-reaching economic integration, national sovereignty and democracy), but fell short in some areas, and could even add to the challenges of globalisation. First, people in advanced economies did not think globalisation created widespread benefits, partly because the EU had not developed policies that effectively redistributed the spoils. Second, the EU had not done an effective job in handling tax competition. In fact, most prominent examples of tax arbitrage involved one or two European countries. Third, the EU had not always been able to protect its citizens against external forces. While it had successfully dealt with the Trump administration's threats over trade – Trump had directed his protectionist policies largely against China, not the EU – the EU had been free-riding on assertive US policy towards China and had not made enough use of the leverage trade policy provided to change Beijing's policies. Finally, globalisation had increased the demand for safe assets in advanced economies. The US stabilised and increased supply of such safe assets, while, during the euro crisis, the EU had implemented policies that curtailed supply. In doing so, the EU had contributed to the challenges of globalisation.

The third panellist asked if the EU could be the answer to globalisation not just for European citizens, but worldwide. He warned that on a global level, the rules of the international trade and financial system would be set by countries with vast economies, such as China, India and Brazil, and a high per capita GDP was not necessarily going to be a measure of influence. China did not adhere to an international order but believed that each country pursued its own interest. Beijing found dealing with the EU impossible, so it preferred to deal with individual countries, with Hungary being one of its main targets. He said it should be Europe's goal to underpin the international order in the interest of its citizens. As for internal policy, he argued that rather than federal risk-sharing mechanisms, the EU should strengthen private risk-sharing via equity markets. He added that it was not clear what the EU's optimal political organisation was, and that the subsidiarity principle somewhat obscured that issue.

The fourth panellist offered three ways in which the EU might be the answer to the negative effects of globalisation. First, it could raise living standards by way of the single market. Second, it could help European governments to pool their influence and hence to shape globalisation. This was more important than ever, given the US's retreat from a leadership role. Third, it could do more to help the losers: structural change always created winners and losers. He noted that conceptually, the EU had become more attractive as a solution to globalisation because no alternative solutions for European countries had really worked, but asked whether the EU really had the necessary capacity to respond to the pressures integration created. He noted that convergence had worked mainly for Eastern Europe, but not for the poorer countries of Western Europe. He pointed to a potential tension between high social standards and competitiveness, and suggested that the EU should create new EU-level funds – or expand existing ones – to help compensate people who lost out.

The discussion kicked off with a debate about leading and laggardly firms. Several discussants noted that more single market integration would probably make firms that were already leading more competitive, as well as widen the gap with less productive firms. As a result of increasing returns to scale, the benefits of globalisation and technological change were concentrated in specific firms and regions. This required governments to pursue more redistribution in order to curtail inequality, but it also made cultural divisions within countries more salient. Several participants questioned whether the main worry should be frontier firms and their dominant position, or unproductive firms. Some argued that while it was important to make sure frontier firms adhered to the rules, it was more important to ensure that low-performing laggard firms that paid low wages were allowed to go out of business.

Some participants worried that if the EU integrated banking, capital, services and digital markets, it would start to resemble the US, and suffer from similar political divisions. It was crucial to find a policy mix that could increase productivity and reduce inequality at the same time, for example by combining the US's market size with a European social model. Others stressed that there was no such thing as a European social model. Only when compared with the United States was Europe homogenous: there were big differences between member-states' social insurance and public services regimes. This could be a source of strength: at least one country of 28 was likely to have found a solution to problems others faced, too. For its part, the EU should focus on those questions that it could solve better than member-states or regions, such as a European social insurance policy. It should get more involved in creating EU-level training mechanisms and replace, not add to, national patchworks.

There was some debate over the trade-off between the European welfare model and member-states' competitiveness. Some argued that there was no such thing as national competitiveness. Instead, the sustainability of the European welfare model was linked to productivity growth, which member-states had the power to shape. Others disagreed: there was a trade-off, openness to trade and new technology did increase inequality. Some cautioned that it was impossible to solve the problems of technological progress and globalisation by only focussing on the 'border aspects' of globalisation. Productivity and greater equality were not exclusive, but complementary. Europe did not have to re-distribute, or compensate losers – regions that received EU money but voted for Brexit were the perfect example why this did not work. Instead, the EU had to promote adjustment to economic changes by way of structural reforms.

On the question of whether the EU was a global player, several thought that it was, but largely as a trade negotiator. The future of the EU did not need to be a federal union as long as the EU remained united on the most important international issues. And Europe was not a victim, but rather a driver of globalisation; the problem was that Europe continued to blame others for problems – the financial crisis being a good example – rather than owning up to its own role. If the EU saw globalisation as something that was done to countries, it could not become a positive force in shaping the global economy or its impact on Europe. Others added that the financial crisis had revealed strong interdependencies, even between the US and Europe, and that both sides had an interest in economic stability in other parts of the world.

Session 3: What does the illiberal backlash in its newer members mean for the EU?

Living standards between Eastern and Western EU members have converged significantly. Can convergence be maintained in the face of growing hostility to liberal norms in the region? Or do these economies risk becoming ensnared in the middle-income trap? Why is there a backlash against liberal norms in Central and Eastern Europe, but not in older member-states with a history of autocracy, such as Spain and Portugal? And what can the EU do about it?

The first panellist argued that economics do help to explain the illiberal backlash, but that we needed to look beyond the bare numbers. What mattered was the core-periphery dynamic: the CEE economies were now the internal European periphery, with capital flowing 'downhill' to these countries and workers migrating from them to wealthier Western European member-states. The result was that all the key sectors in the CEE region were dominated by Western companies, helping to explain rising economic nationalism. There were only two sectors in which CEE countries had penetrated the West – transport and construction – and in both the EU was making (through tighter controls on posted workers) the single market even more imbalanced in favour of the West. Freedom of movement was not, on the whole, a net loss to CEE countries, but in some sectors there clearly were negative effects, such as in healthcare. The popular perception was that the region's governments were rule-takers, not rule-makers. Net emigration, combined with low birth rates, was leading to rapid population ageing, which was reinforcing conservatism.

The speaker distinguished between three groups of countries: a strong and stable group already in the euro comprising Slovakia and the Baltic states; a weak and stable group comprising Bulgaria, Croatia and Romania, which abided by EU rules; and a strong but unstable group, comprising the Czech Republic, Hungary and Poland. The latter found the EU's rules-based system to be too much of a straight-jacket. For this reason, they were wary of joining the euro. He was sceptical whether attaching greater conditionality – such as rule of law requirements to structural funds – would be effective, because of the need for unanimity and because it would take a long time. The EU needed to develop more soft power in the media and the public sphere more broadly.

The second panellist urged Europe to think strategically about illiberalism. He argued that Macron putting Hungary, Poland and Russia into one basket was a strategic error; illiberalism in CEE countries did not automatically coincide with pro-Russian sentiment. He argued that Europe should recognise the central importance of Poland. If it failed to keep Poland in the European fold, it would have failed the region as a whole. France and Germany should further develop the Weimar triangle format with Poland, and not just regarding defence matters. Europe should ask Poland what it wants the endpoint of its relationship with the EU to be. The EU needed to show the Poles that they can be at the centre of

Europe, and that being in the outer tier would leave them vulnerable to Russian meddling. Poland needed a roadmap for membership of the euro, even if it ultimately chose not to join. Finally, Polish opposition to Russia should not be taken for granted. Warsaw might, at some point, start hedging its bets between Russia and the West. This would have serious security implications.

The third panellist said that joining the EU and NATO had been the central goal of CEE countries, and that the next goal was to reach German living standards. But progress had been slow and had stalled since the financial crisis. The strategy of attracting foreign direct investment (FDI) had worked quite well up to 2008, but since then the limits of this development strategy had been exposed. After the financial crisis, firms' profitability (many of them from Western Europe) had continued to rise, but wages had stagnated. Czech GDP per capita had risen to 45 per cent of the German average (at market exchange rates), but Czech wages were just 25 per cent of the German average. The EU was a useful scapegoat. While Hungarian prime minister Viktor Orbán was more flexible than Poland's Law and Justice party, and would do whatever kept him in power, Poland presented a bigger challenge. It was hard to engage in dialogue with the Polish government, because the person wielding the actual political power was not the (then) prime minister, Beata Maria Szydło, but Jarosław Kaczyński, leader of Law and Justice. He was determined to deepen the divide between conservatives and liberals in the country. In other countries voters had lost faith in the political system. For example, in the Czech Republic just a third of voters supported traditional parties. He argued that the economy did matter, but that the countries in the region needed incomes to converge with the West; GDP was inflated by corporate profits which were then repatriated. The current core-periphery relationship would continue to boost support for populists. CEE governments needed economic strategies to increase the number of high-paying jobs. This meant a focus on encouraging the growth of local firms, less emphasis on manufacturing, and more knowledge and service industries.

The fourth panellist argued that the Washington Consensus had included the view that the embrace of free markets would inevitably lead to democracy. Democracy had been seen to be a one-way street, so little thought had been given to how to consolidate fragile, young democracies. The EU's standard response to illiberal governments was to first ignore the problem, then outsource it to the European Commission, and then sit out the illiberal government's term in office. Over time, illiberal governments undermined democracy, for example through politicising the judiciary and the press, and abusing the electoral system. The situation was now serious. It was threatening police co-operation and the operation of Schengen. More profoundly, the countries of the region were diverging from the values that underpinned the EU. What could the EU do? It was hard to use Article 7 to force change, because this required unanimity, and the Hungarians and Poles would never agree to action being taken against the other. However, there were other options, such as stepping up monitoring through the European semester, setting conditions for the receipt of EU funds, or using the threat of being relegated to a second-tier of member-states as punishment. The EU should also focus on things that fed the illiberal machine, such as fighting corruption and the embezzlement of funds.

The fifth panellist argued that Germany's role was central, even though Germans were reluctant to acknowledge that. Germany had a special responsibility towards the CEE countries, and was increasingly comfortable seeing itself as a geopolitical power. But it had preferred to concentrate on its burgeoning economic ties rather than on the worsening political situation in Hungary and Poland. Illiberal governments were reshaping constitutions in an effort to make them more 'identitarian'. The Polish government, in particular, was doing this with real energy. The Poles and Hungarians were checking out of the obligations of EU membership, but wanted to retain the rights and financial benefits. The major risk was not a formal EU exit, but a de facto exit from the values of the EU, and Russia fully understood that. We should not take for granted that the countries in the region would continue to hold Russia at bay; Slovakia and Hungary were already hedging their bets. The panellist stressed that external threats were increasing the need for closer integration, especially in the foreign policy and security fields, but that foreign policy specialists were ignoring the politics and economics of the key CEE countries.

The discussion initially focused on defining the common elements of populism. For one panellist the common factor was a centre-periphery divide. People felt that they were not part of the decision-making process; that they were being left behind or were at risk of being left behind. The populist base was always a combination of working-class voters and social reactionaries. Several participants commented that the degree of foreign ownership of assets in the CEE economies was a major issue; it reinforced the sense that political sovereignty was illusory. Reform of the 'posted workers directive' was a source of particular resentment, as it undermined CEE firms in one area in which they had succeeded in penetrating Western markets. They also feared that closer eurozone integration would marginalise them further, with the eurozone becoming a market within a market, and resented what they perceived to be an EU *fait accompli* regarding refugees.

For several participants, what was happening in CEE countries was indicative of a global trend. Once the political ideologies of Left and Right had broken down, politicians had to find other ways of motivating people to vote. The rise of populism and suspicion of the EU in the CEE countries would be very difficult to reverse. The countries in question know that they will never join the euro, because they understandably did not want to expose themselves to sanctions: sanctions available to the EU to punish an errant member were weaker than those available to the eurozone. But the decision to stay out of the euro would ultimately come at a high cost. Britain showed that this was a slippery slope to EU exit.

Other participants were less fatalistic. Several argued that Poland was not monolithic. There were huge demonstrations taking place across the country against the government's attacks on the judiciary and the press. The EU needed to attach tighter conditionality to its structural funds. If this failed, there would need to be fines, and ultimately there needed to be the option of expelling countries from the club. This was unnecessary when the EU comprised countries sharing the same values. But failure to take a tougher line would cost the EU its cohesion. Others called for more caution. One stressed that the EU is ignoring illiberal trends in Western European countries, such as surveillance in the UK and Germany, attacks on minorities in Spain and Greece, and the undermining of the independence of the judiciary in Spain. This weakened the EU's credibility in the eyes of CEE governments. One participant picked up on the EU's alleged hypocrisy, arguing that Germany relied on Hungary closing its border to refugees in order to prevent a political crisis in Germany, but then criticised the Hungarian authorities for their action.

Several participants argued there had been substantive economic convergence between the CEE and the EU-15. The pace of that convergence had slowed since the financial crisis but it had not stalled. These countries were becoming progressively more integrated into broader EU supply chains, which would continue to drive productivity growth. One participant went as far as to argue that Central Europe, encompassing Germany, the Benelux, the Nordics, Austria and the CEE, could develop into a more optimal common currency area than the eurozone. The answer was to manage the expectations of CEE workers: it would take many decades to converge on German living standards and may never happen. But the best way of maximising the degree of convergence was greater market integration, which would be facilitated by joining the euro.

Others were more sceptical. The expansion of Western European supply chains into the CEE had brought benefits, but the issue of low wages could not be ignored, and substantive convergence would require different development strategies than greater market integration.

Session 4: Can the euro still be a force for EU integration?

Opinion polls suggest the euro remains popular, notwithstanding the eurozone's poor economic record. Could the single currency yet become a source of support for political integration? The election of a populist government in France or Italy would throw the eurozone into existential crisis. But if populists are defeated, could the present economic upturn provide an opportunity for further political integration? If not, what are the economic conditions needed for political integration to take place?

The first speaker argued that there was no appetite for political and economic union within the eurozone, and that trying to force it would simply feed populism and lead to a backlash against the euro and the EU more generally. The eurozone most needed to integrate monetary and banking policies. The eurozone needed the European Central Bank (ECB) to act like a fully-fledged market-maker and lender of last resort (buying up government debt, as well as assets in other illiquid markets posing systemic risks). This would help ensure there was an adequate supply of European safe assets without having to resort to mutualisation. The second priority was to complete the banking union. Limits on how many of their own government's bonds banks could hold, together with stronger bank regulation, deposit insurance and a proper debt restructuring mechanism, would help break the doom loop between sovereigns and banks. By contrast, the spill-overs from national fiscal policies were very small, so the eurozone should renationalise fiscal policy, which would help contain populism. Fiscal integration should be limited to a small, targeted unemployment insurance scheme. The speaker argued that the eurozone did not need its own parliament, but rather a proper system of committees.

The second panellist took a different line. There needed to be more, not less, conditionality, or there would be political crises in the creditor member-states. There was a debate to be had about what should be done at the level of the EU, the eurozone and that of the member-state, but national governments needed to set the rules of the game, and these rules had to be enforced. The trust and confidence needed to underpin integration was now lacking because of the failure of the EU to enforce the rules. When the Germans had given up the Deutsche Mark they had been promised that this would lead to greater financial stability in neighbouring countries. The Stability and Growth Pact and the Fiscal Compact had failed to enforce fiscal discipline, with the European Commission being too susceptible to government lobbying; this responsibility should pass to the European Stability Mechanism (ESM). Germany had agreed to a banking union, but now there was pressure for an unconditional backstop for eurozone banks. A single supervisor combined with national regulators was unworkable.

The third panellist stressed that while the member-states did not agree about how the eurozone works, the outlook for the currency union would remain uncertain. There were three schools of thought regarding the origins of the crises and hence what was needed to put the currency union on a sound footing. The first was a zero-sum view of the currency union centred on fiscal deficits, and stressing the view that taxpayers in some countries had been forced to bail out profligate governments in others. The second view focused on differences in productivity levels across the currency union, as exemplified by large current-account imbalances. The focus here was again on improving the performance of the weakest member-states. The third view was that the long period of stagnation was the result of the banking crisis, which was handled very poorly, with the debtors being forced to bail out the creditors. This was by far the most convincing explanation for what had happened but it was largely ignored because it was – on the face of it, at least – less political and more technocratic.

The final panellist struck a note of cautious optimism, arguing that the euro was now generating momentum for closer integration. External political developments had also catalysed the resolve of eurozone leaders to find solutions to the currency union's challenges. The ESM would get more responsibility for crisis management. France would get something on the budget, but it would not be big enough to be a significant counter-cyclical force. Political union was impossible, and it was unhelpful to even talk about it; the currency union would remain intergovernmental. The eurozone needed mechanisms to help member-states cope with asymmetric shocks, but this would only be possible if German concerns were met. The Germans were right to fear moral hazard. It was impossible to complete the banking union while some member-states were dragging their feet in cleaning up the non-performing loans in their banking sectors. National regulators were defending their turf; regulation needed to be moved to the eurozone level. The speaker also argued that some members were using the windfall of lower interest rates to engage in pro-cyclical fiscal policy. Germany's current account surplus of 9 per cent of GDP was destabilising – the eurozone needed stronger public spending and inflation in Germany. But there was no way of compelling Germany to act. He finished by saying that the fundamental issue within the eurozone was big differences in labour productivity, which could only be addressed through further market integration.

The discussion initially focused on whether the euro was a force for integration or not. One participant argued it was, citing rising support for the euro among members of the currency union; but while the euro was proving to be a force for integration in the 19 countries that used it, it was a force for disintegration at the EU level. Others were more sceptical. For one, political decision-making at the EU-level was relatively fair, whereas within the eurozone the stronger member-states bullied the weaker ones, which was a poor basis for integration. Another said that strong support for euro membership reflected an awareness of how difficult it was to quit the currency union rather than enthusiasm for the single currency per se. Another argued that the euro could only be a force for integration if it assumed a positive-sum Keynesian logic rather the current zero-sum one, which would always produce losers and hence political strife.

The discussion turned to the issue of debt restructuring. For a number of participants, neither stronger fiscal rules nor fiscal union was the answer to the eurozone's problems. Rather, the currency union required a hardening on the no bail-out rule, with fiscal policy being renationalised and a restructuring mechanism for sovereign debt introduced. At present, Germany and other creditor countries were pushing for tighter fiscal rules while opposing any joint liability. This was unsustainable politically: liability and control had to be aligned. Others were sceptical that sovereign debt restructuring could be undertaken without considerable instability. At the very least, the eurozone would need a sufficient quantity of safe assets, which required the ECB to fully embrace its lender-of-last-resort functions. A further participant questioned whether the markets would discipline national governments. Would investors really believe there would be no bail-outs? Others added that debt restructuring would be very taxing politically and economically: the eurozone still needed institutions to share risk in order to head off the need for restructuring, which should only ever be a last resort. One participant stressed that there was already a contingent transfer union in the form of Target II balances.

Several other participants raised further reservations about the renationalisation of fiscal policy. For one, national fiscal responsibility made the single currency more prone to bank runs, even if the banks were forced to reduce their holdings of sovereign debt. A larger fiscal backstop within the banking union would help, but would it ever be big enough to cope with the collapse of Credit Lyonnais or Unicredit? Also, it was doubtful that the banking union would be able to act quickly enough in a crisis, with fiscally stronger governments able to intervene to rescue national banks, while weaker ones would be unable to. Another speaker stressed that the eurozone needed a unitary fiscal body to provide the fiscal stimulus required to reduce the eurozone's current-account surplus. With 19 separate fiscal bodies, this would not happen, as demonstrated by Germany's refusal to take action to reduce its own surplus. Another concurred, arguing that very low interest rates pointed to the need for more expansionary fiscal policy. And this required a significant eurozone element, as there was no guarantee that national governments would adopt counter-cyclical policies.

Finally, the discussion focused on the roles of the private sector and market integration in stabilising the eurozone. For a number of participants, a big part of the answer to the eurozone's problems lay in encouraging greater market integration, which would boost economic activity (and hence fiscal sustainability), while narrowing the gaps in productivity between the participating countries. For several panellists, capital market integration was especially crucial. The more integrated the ownership of assets, and the bigger the cross-border flows of capital, the more the costs of an asymmetric shock would be spread across the currency union as a whole, rather than being concentrated in the crisis economy. While there was general consensus that capital market integration would help countries cope with asymmetric shocks, there was less agreement that market integration more generally would prove so helpful. For one participant, it might boost productivity overall, but there was no guarantee it would lead to a convergence in productivity levels. For some, it was more likely to widen them as capital and skills became more concentrated in more dynamic regions. This could increase (rather than reduce) the need for transfers to struggling members.

Session 5: Can European identity be reconciled with large-scale migration?

Inflows of migrants and refugees into the EU from Africa and Asia are set to increase further, as income differentials, demographics, conflict and climate change combine to propel people northwards and westwards. Is it possible to forge a more inclusive, civic European identity capable of absorbing these inflows? Does immigration from outside the Union threaten open borders within it? If so, will we see pressures for more EU control of its external borders?

The first panellist pointed out that migration was set to continue, for economic reasons, because of a changing security landscape, and because of climate change. But more diversity was not a challenge to a liberal concept of identity: we all had many overlapping identities. He argued that Orbán's vision was profoundly un-European. Muslims in Europe overwhelmingly held liberal views and wanted to fit in, and illiberal migrants were not a problem as long as they adhered to the rules of the society they now lived in: Europe was about the rule of law, equality before the law, and the protection of minority rights. The biggest threat were illiberal Europeans, who felt threatened by a liberal European identity. The Schengen borders needed to be secure, but offer ways of legal migration into the EU.

The second panellist argued that the empirical evidence on the effects of migration was nuanced. Migration had played a role in widening inequality. There were negative effects on some groups of the native population. It also was not true that Europe needed migrants to fill jobs: Japan had an ageing population and no migration, and still had lettuce in the shops. The beneficial effects on the pension system were often massively overstated. British concerns about their crowded island should not be simply dismissed, as the liberal elite usually did – housing and infrastructure concerns were real. Islam was special in that it had not undergone a process of secularisation as Christianity had, and Islam as practiced in majority Muslim countries was not tolerant of other religions. He added that in the UK, the sympathy for extremist views among Muslims was alarmingly high. He argued that Europe should better manage the economic consequences of migration by responding to potentially adverse distributional consequences; using a robust approach to insist on European values; and setting a cap on numbers of immigrants. But the population explosion in Africa meant that there was no credible case for optimism.

The third panellist said that Europe was discovering a European polity: the realisation that we were sharing a common space. He argued that there were three ways to tackle migration in Europe: go to the source, build a border, or relocate. On the first, Europe was disappointing. On the second, the EU had started to lose its geopolitical innocence. It had beefed up Frontex, closed borders and made "dirty deals" with neighbouring countries, which previously had been done by nation-states. On the third, he argued that the relocation schemes decided in Europe were not a solution, as forcefully distributing refugees touched upon deep issues of identity. The solutions he saw were opening legal ways of migration and linking the costs and benefits of free movement more explicitly.

The fourth panellist focused on the quality of the debate about migration. He argued that Europe could easily digest large-scale migration, but only if the debate was handled better in the future. There was a fear that white majorities were going to be replaced with non-white Muslim communities, and post-industrial towns worried about their irrelevance to metropoles. Currently, the migration numbers were small. Germany and Spain provided examples where the debate was quite different from the rest of Europe, and as a result, policies were different. Conditions for workable migration policies were first that the public needed to have the impression that things were under control; and second, that migration stopped being a proxy for other debates, such as those on demography, the economy or culture. Liberals were dismissive about the concerns of citizens over migration because liberals felt besieged, in part because they were losing the migration debate. But one benefit of free movement that liberals could stress was that people did not have to fear being sent back to their country of origin and therefore did not need to get passports, so it might actually limit permanent migration.

The discussion started with a debate on the proper interpretation of empirical findings around migration. A few pushed back against the claim that migration had some negative effects, pointing out that there was very little evidence for them. For example, the congestion of public services in Britain was entirely a domestic policy failure, but blaming migration was a convenient and successful political strategy. Indeed, another discussant added, the UK faced a higher fiscal deficit in the future because Brexit would lead to lower immigration. The real risk was the nativist right, and pandering to their concerns would not help. Another participant added that large-scale immigration to the UK was a myth; even at its peak, net migration had only increased the population by 0.5 per cent a year. Stagnant wages were a big problem but domestic public policy was at fault, not migration. Another discussant agreed, saying that despite all the complaints by the UK about the negative effects of migration from CEE countries, the British government never made a serious attempt to show these negative effects during the renegotiation of British membership of the EU. Another discussant asked whether the effects of migration on the young or workers were negative, and why the majority of these groups had voted against Brexit.

The first panellist responded that the evidence on migration was indeed positive, and added that this research studied narrow economic relationships: if 'dynamic' effects on long-term productivity could be easily measured, the benefits of migration were likely to be higher than this research suggested. The second panellist, however, insisted that the evidence was not unambiguously positive, that overall GDP measures were useless, GDP per capita showed minimal benefits for the host population, and he was not encouraging nativists by arguing that. The fourth panellist argued that there was no general rule as to who supported migration and who did not. The young, for example, were not in favour of migration everywhere.

The discussion then tackled the question of how the public debate could be improved. A discussant argued that policies to promote assimilation were key to the long-term success of migration. But some were sceptical that the public debate could be improved. One participant argued that restating the empirical evidence was probably the best defence but he favoured teaching secular ethics at school and involving religious institutions in regular dialogues on integration. The fourth panellist added that the reason why the debate in Spain was not a problem was that the framing was different. He pointed to a campaign slogan that said "those who took from you were white and rich, not brown and poor". Another discussant argued that the debate around migration could not be won based on empirical studies alone. It was a problem of control and the impression of a never-ending migration flows, not a problem of long-term absorption capacity. Nor should we confuse migrants and refugees in the debate. One participant thought that the economic evidence did not help much politically; that saying migration is fine was easy from a position of privilege.

For the remainder of the discussion, participants focused on what the EU could do about Africa, and security. One participant wondered why the panellists had said nothing about security concerns and the terrorist threat. He added that migration in West Africa was mostly internal, because the overwhelming majority were too poor to migrate to Europe. With more information, a vibrant trafficking business and increasing living standards, that may well change. Helping Africa to grow economically could mean more, not less migration. Other discussants agreed that migration from Africa in the future posed a massive challenge to Europe.

Another discussant pointed out that Brussels institutions were themselves far from diverse. He argued that the EU saw itself as a Christian club, as Turkey was the only accession country whose people were denied visas to enter the EU as a whole. A discussant responded that the EU was unfairly targeted by populists over the migration issue, as it only made rules but had little say in distributing the benefits of migration. The final discussant argued that it was not just the European identity that policy-makers should consider, but also Europe's soft power in other countries – which nativism could only damage.

January 2018

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