5

Europe in Crisis: More Political Integration in the Eurozone is the Solution

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Introduction

There is no doubt that the world economy has recently faced one of the worst global crises since the Great Depression. It is also quite indisputable that Europe is one of the worst affected areas. Not only do European growth rates tend to be lower than those of the US or emerging economies, but also even the existence of the Eurozone is at risk. The sovereign debt of various European countries, such as Greece and Spain, has come under massive speculative attack on financial markets, despite the fact that other countries are even more indebted. For this reason, several euro members have approved various austerity plans that threaten a double-dip scenario.

The big questions that naturally arise are the following: what accounts for this crisis of the European model, and in particular of the Eurozone, and how to face it? In a recent issue, *The Economist* mentions three alternative stances. The first is the French view, which considers the crisis as due to a lack of political integration which governments should now seek to remedy:

> the chaos, that has spread from Greece to Southern Europe shows the eurozone needs a core of dirigiste powers to run Europe in a more political and less technocratic way. To limit 'unfair' competition, they want things like Europe-wide labour standards and some harmonisation of taxes. They want to oversee transfers of communal cash to the euro's weakest members. (*The Economist*, 2010a: 11)

The second is the German view that regards fiscal indiscipline by a number of southern countries as the key problem for the Eurozone to

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tackle. In order to save the euro, 'Germany wants a harsh system of rules, enshrined by treaty if need be, that would ban countries from spending too much' (*ibid*.). The third is that suggested by most academics and endorsed by *The Economist* itself, according to which Europe's relative lack of flexibility and competition on labour and product markets with respect to other areas turns out to be its main drawback. In this view, a vast menu of liberal reforms is the proper solution: 'The crisis offers the best chance at revival since the 1980s. To rediscover its vigour and boost its economic growth, Europe should free its economy and set up the single market' (*ibid*). However, *The Economist* also realistically recognizes that, in view of the political obstacles to the implemention of such reforms, a suboptimal solution for the Eurozone is likely to emerge after all; namely, it will 'muddle through':[1]

> Tidy minds contemplating the contradictions between the euro's two most important members foresee either integration or collapse. They argue that without a clear political mechanism to cope with wayward countries, the euro is doomed to repeat the sort of crisis it has suffered this year. One day this view may be proved right. But tidy minds underestimate the European art of compromise ... and they overlook the determination in Europe to make the euro stick ... For the moment, therefore, the most likely outcome is neither collapse nor a dash towards integration, but for the eurozone to muddle through. (*Ibid*.)

According to *The Economist*, to 'muddle through' is certainly suboptimal, since it 'avoids problems, it does not solve them' (*ibid*.). In particular, it condemns Europe to experience a relatively slow growth rate for many years to come. I agree. Unlike *The Economist,* however, we suggest that more political integration is the proper, rational way forward, at least for the Eurozone members (for a similar view, see, e.g., Eichengreen, 2010; Krugman, 2010; Soros, 2010; Stiglitz, 2010).[2] But the key issue is: why is this preferred outcome very unlikely to happen and 'muddle through' bound to prevail instead? To answer this question is the aim of this chapter. It attempts to underline the obstacles to political integration, following a research strategy which parallels that pursued by *The Economist*, seeking to explain why its preferred solution (i.e., structural reforms) is not easy to implement in practice.

The main view put forward in the chapter is that mere national interest or 'selfishness', though obviously important, is not the sole obstacle to greater political integration. It interacts with another, more intellectual, obstacle: namely, the conscious or unconscious reliance of most governments, officials, academics and policy-makers alike on the prescriptions of orthodox macroeconomic theory concerning stability and growth issues, a theory which today is labelled as 'New Neo-classical Synthesis' and characterizes most modern textbooks. Indeed, a number of arguments discouraging political integration quite simply follow from the application of this theory to the European case. One can note, for example, that it inspires the pillars of what can be termed as the current 'economic constitution of Europe' linked to the introduction of the euro, namely the Maastricht Treaty and the SGP (Stability and Growth Pact) on the one hand and the one-sided emphasis on structural reforms on the other.[3] These two pillars, which are widely regarded as necessary preconditions for growth, imply that monetary policy and acceptance of strict budget rules are all Eurozone countries need to share; apart from market unification, individual countries' growth is regarded as the product of national factors and policies (such as structural reforms). This framework thus simply dismisses the very possibility of active or discretionary fiscal policy for Europe as a whole, certainly requiring a higher degree of coordination among states, despite the fact that most countries in the world, including the US (which is otherwise taken as the benchmark in many cases), do not hesitate to implement major strategic anti-cyclical plans, such as the Obama plan, when facing serious recession or deflation scenarios as we currently are.

But this is not all. It can be shown that standard theory is ultimately responsible even for the 'muddle through' outcome itself. The point is that its precepts are quite difficult to implement in practice. Thus governments experience a growing sense of frustration and are bound in the end to get stuck out on a limb; as a result, not only do they fail to cooperate more strictly but they also tend to become more suspicious of each other.

The two factors just mentioned are mutually reinforcing: it is because it apparently best suits national interests to leave individual countries alone to pursue growth that the current economic constitution is adopted. The central thesis defended in this chapter is that this circle should be broken. In my view, as Europe's stagnation shows, it is quite wrong to believe that individual countries benefit from this constitution. In principle, they could be much better off under an alternative constitution, one requiring a higher degree of political integration.

The main implication of my view is that any progress towards political integration depends upon individual states understanding the strategic reasons why they could gain from it. This understanding should not be seen as the inevitable outcome of a long historical process of evolution, of the slow maturation of some kind of European identity that will make it almost natural for national governments to accept deferring their prerogatives to some communal entity. Although the *natura non facit saltum* argument is certainly plausible and to a large extent correct, in my view history must be somehow 'guided'. Just as the introduction of the euro was not 'necessary', not somehow written in the genes of Europeans and thus bound to happen anyway, so making the Eurozone work properly calls for lucid determination and strategy. In particular, I suggest that people's eventual understanding that integration is better than the status quo crucially depends upon the existence and popularity of a quite different theoretical framework for stability and growth than the current one, a framework capable of inspiring a different 'economic constitution' for Europe. In other words, greater political integration to this end will occur only if policy-makers in individual countries reject the current macro theories and embrace an alternative one stressing the advantages of political integration.

To discuss such issues this chapter is organized as follows. In the first section, I focus on the arguments against political integration that are somehow justified by standard theory. The second focuses instead on arguments in favour of integration, which derive from an alternative framework broadly inspired by Keynesian theory.

Why is standard macroeconomic theory an obstacle to political integration?

Standard macro theory is a key obstacle to political integration for a number of reasons. Some of these directly follow from its principles (e.g., they influence the key features of the 'economic constitution' of Europe, such as the Maastricht Treaty and the SGP, which implies only a low degree of integration). There are also indirect reasons, however. The point is that such orthodox principles are difficult to implement in practice, so governments are structurally bound to be 'pragmatic' and search for suboptimal compromise solutions within the existing economic constitution: that is, the 'muddle through' outcome described by *The Economist*. The best way to discuss both types of reasons is to analyze the alternative stances expressed in the current political debate about the European crisis, which are all influenced heavily by standard theory.

One major reason why standard theory directly discourages political integration is that it leads governments – like Germany's – to place a major emphasis on fiscal discipline, and more in general tight demand policies, as a precondition for growth. The general idea behind this principle is known as Say's Law, according to which the market system based on rational agents and flexible prices works efficiently so that supply creates its own demand, full employment is the rule and there is no need in principle for any public support to private demand. If governments spend too much, they will simply end up by crowding out private investment and/or generating inflation.

Clearly, this idea inspires the current 'economic constitution' of the Eurozone, which was devised to support the introduction of the euro. Now there is no doubt that this constitution calls for only a relatively modest degree of political integration between the euro members: all they need to share is a unified monetary policy aimed at the strict control of inflation. According to standard theorists, however, this is the maximum achievable degree of unification. Strictly speaking, even a unified monetary policy is too much. As argued, for example, by Tabellini (2010), it is too stringent for some countries (for example, Spain is different from Germany) and certainly there is no need to have also a unified fiscal policy. The only form of 'fiscal' coordination between countries at the European level which is implied by the current constitution is in 'negative' terms, according to which individual countries are obliged to comply with fixed criteria (and even tend to balanced budgets) and, if they fail to do so, they are forced to implement restrictive policies, even in critical periods such as these, in order to avoid sanctions or market punishment.

But fiscal discipline is difficult to implement in practice. The point is that this framework takes stability of the private sector for granted (that is, consumption or investment are seen as responding smoothly to price incentives). It thus leaves governments unarmed when facing serious crises, such as the current one, where demand instability leading to lower income and higher budget deficits (due to lower taxes and higher expenditures) clearly emerges. However, it would be wrong to believe that even in this case the standard framework and the current constitution simply break down and the need for a greater degree of cooperation as well as political integration between Member States becomes self-evident. This is so for at least two reasons. First, recessions are normally seen as temporary and policy-makers concur that they can be dealt with by some flexibility in the timing of fiscal adjustment required by the current constitution, especially if inflation fails to emerge as in the current period. This is one of the main features of the 'muddle through' scenario.

Second, the standard model is the benchmark which people use to assess states of the economy which greatly diverge from the norm even for long periods of time, as in the case of Europe. This means that if the world does not conform to the model, it is not necessarily because demand is low as Keynesians would suggest. It may well be for opposite reasons: namely, because of supply-side problems due to the existence of a number of structural obstacles to the efficient working of markets.

Indeed, this is one the most popular explanations of the European crisis to be found in articles in the academic literature and authoritative publications, such as *The Economist.* They suggest that although Europe does well in certain areas, the success of its economic model is impaired by old structural problems, such as the relative lack of flexibility and competition on labour and product markets with respect to other areas (see, e.g., Steltzer, 2010; *The Economist*, 2010a; 2010b). This basic thesis goes back at least to the 1990s, when Europe started to lag behind the US, and comes in various, not mutually exclusive, versions, ranging from the emphasis on demographic factors (e.g., Europe is 'old', a relatively static society where mobility is scarce and immigration is not sufficient to reinvigorate it: see, e.g., Alesina, 2010; Steltzer, 2010) to that on 'institutional' ones (e.g., Europe is more corporatist than the US and is lagging behind in promoting the institutions of capitalism, e.g., Phelps, 2006). However, the emphasis on the supply-side factors in the crisis of Europe also underlies the views of more heterodox economists when recently claiming that the key problem of the Eurozone is that it fails to be an optimal currency area (e.g., Stiglitz, 2010; Krugman, 2010).

On these grounds, we can now understand the second reason why standard theory directly discourages political integration: it leads governments to place emphasis on structural reforms. Indeed politicians are convinced that this should be the way forward to solve problems.[4] But what is the link between structural reforms and low political integration? To answer this question, we only need to recall that, according to standard theory, the reason why tight demand policies need to be pursued at all costs is that they create the conditions for growth; that is, once price and fiscal stability are achieved, growth can take place almost automatically as it is driven by supply factors. For our purposes, the key point to note is that, when applied to Europe, this framework implies that competitiveness and growth do not need any degree of coordination between countries. Indeed, according to the current economic constitution inspired by the orthodox principles, all the central European authorities should do to favour competitiveness for all Eurozone members, apart from approving regulations to unify markets, is to keep inflation low. For the rest, competitiveness and growth must be pursued by national governments alone in the form of supply-side policies (e.g., labour market policies). Given institutional differences across countries, in these areas competition between countries is better than harmonization (see, e.g., Tabellini, 2010). The following quote from *The Economist* gives a clear idea of the current menu of structural reforms, with an indication of the normative 'division of labour' between central authorities and national governments:

> The single market remains half-built ... the EU is 30% less productive than America in services ... Whole areas, such as health care, are exempted from EU-wide competition. Likewise, some high-tech industries, such as telecoms, have been protected ... the EU has a costly, fragmented patent system ... energy supply has not been properly liberalised; debts are hard to collect across borders ... In Spain and Italy privileged workers are protected ... Europeans retire too early everywhere. (*The Economist*, 2010a: 11)

Again, structural reforms are difficult to implement in practice for a number of reasons. Defenders of this perspective, like *The Economist*, suggest that obstacles are purely political in essence: 'The barrier to reform has always been political, not economic' (*ibid*.). Subscribing to this view, Tabellini suggests, for example, that the actual implementation of the structural reforms project is undermined by the institutional architecture of the Eurozone, which makes the normative division of labour just mentioned quite problematic. In particular, he notes that the 'soft coordination' method, which prevails today among European nations, is responsible for the substantial failure of the Lisbon strategy (see Tabellini, 2010). By placing everything at the same level, this method turns out to be ineffective where strong European intervention is needed and redundant where national government responsibility is needed.[5]

In my view, however, another obstacle is standard theory itself. The point is that this theory regards even recessions as caused essentially by supply-side problems. Although demand shocks may hit a stable economy, it is only when price rigidities or market imperfections impair swift market adjustment that prolonged deviations from the norm occur. This approach leaves governments to seek to follow its precepts relatively unarmed when facing serious crises, such as the current one, due to the prolonged instability of the demand side, induced by factors such as confidence crises, inequitable income distribution, credit crunch and stock market volatility. It is not surprising therefore that, when dealing with such crises, governments become pragmatic: that is, they do the right things without understanding why; they instinctively seek to remedy such effective demand failures rather than insisting on reforms. For this purpose, they discover the virtues of more explicit political coordination. For example, in the recent crisis many countries have been working together to engineer financial intermediaries' bailouts rather than leaving them to go bust (as focusing on 'structural reforms' should have implied). In my view, this gap between actual policy 'forced by events' and wrong economic theory is one of the key explanations for the 'muddle through' scenario. However, once again it should be noted that pragmatism alone does not lead to a change in the current constitution. The latter is meant to apply at least to 'normal times', exceptions being allowed in emergency times only. This is the reason why the structural reform rhetoric accompanied by the fiscal discipline requirement has recently assumed new vigour in the policy agenda of many governments soon after the first signs of recovery in European economies.

It would be wrong to believe, however, that the negative influence of standard theory on political integration follows simply from the two principles just mentioned: that is, the insistence on fiscal discipline and structural reforms combined with the difficulty of implementing them in practice. Another influence results from the fact that standard theory also leads commentators to represent political integration in negative terms: that is, as a 'violation' of the right economic model. It essentially regards it as reflecting dirigisme (that is, an attempt to impose the will of the state over market forces) or protectionism to defend the costly 'European social model'. Indeed, according to *The Economist*, a 'European economic government' within an inner core of Eurozone members:

> means politicians meddling in monetary policy and a system of redistribution from richer to poorer members, via cheaper borrowing for governments through common Eurobonds or outright fiscal transfers ... fiscal and social harmonisation: e.g. curbing competition in corporate tax-rates or labour costs. (*The Economist*, 2010b: 23)

Other elements of this project include: bailout mechanisms as a way to impose the will of the state over 'speculators', protectionism (e.g., French car industry) to keep globalization (especially within Europe's own borders) at bay and, above all, defence of the 'European social model' (old-age pensions and unemployment benefits):

> single nations are too small to maintain high-cost social-welfare models in the face of global competition. But the EU, with its 500m people, is big enough to assert the supremacy of political will over

> market forces. For such politicians, European diversity is a problem because it undermines the most advanced (meaning expensive) social models. Such competition must be curbed with restrictions on labour migration from eastern Europe, subsidies for rich-country production and lots of harmonisation – including ... a European minimum wage. (*Ibid*.: 26)

Clearly, in the light of negative assessments such as these it becomes quite difficult for policy-makers and governments to advocate political union. Once again, it is not surprising that the 'muddle through' scenario emerges as the most likely outcome of the current situation in Europe.

Political union calls for an alternative theoretical perspective

In the previous section, I have suggested that at the roots of the current 'muddle through' scenario, which condemns Europe to relative stagnation, lies the combination between a wrong macroeconomic model inspiring the current economic constitution in the Eurozone and governments' failure to implement the actual policy measures that follow from this model. In this section, I argue instead that to overcome this suboptimal scenario and grow at a more reasonable pace the Eurozone calls for higher political integration. However, for this purpose this area needs to rely on a new economic constitution, based on an alternative theoretical framework, capable of integrating stability and growth issues in a better way than orthodox theory does. The basic idea underlying this framework is to reject the two basic premises of the orthodox policy framework, namely monetary and financial stability, as preconditions for growth and reliance on structural reforms to stimulate growth directly by influencing the supply-side factors. I argue instead that aggregate demand factors represent the 'true' drivers of growth and this idea leads me to draw very different conclusions with respect to standard analysis. A good way to present this alternative framework and its policy implications very briefly is to consider the reasons why the current economic constitution, while apparently favouring the national interest of individual countries, is bound in the end to discourage their growth.

Let me start by noting that, by focusing on inflation control as a precondition for macro stability and growth, this constitution tends to favour export-led growth in countries such as Germany and Italy. A few drawbacks in this model of growth can easily be singled out.

First, such countries tend to experience low internal demand, which many Keynesian economists regard as one major cause of Europe's relative decline (see, e.g., Fitoussi, 2010). In principle, a stronger Union, in which more resources are allocated to central government than is the case today, could more easily address this issue (for example, by using appropriate fiscal tools).

Second, by calling for external engines of growth, such as the US, this model condemns Europe to a certain degree of political minority (as second violin to use Bauman's metaphor: see, e.g., Bauman, 2008, ch. 6). There is little doubt that higher political integration could be a remedy to this state of affairs.

Third, this model rests on the idea that the only weapon to gain competitiveness which is available for individual members of the Eurozone, given the impossibility of devaluating, is to reduce costs. However, this neglects other dimensions of competitiveness, such as quality or identity, which are especially important for Europe in the face of strong globalization trends. German goods are competitive because the 'made in Germany' label guarantees their excellent quality, not because they are cheap. For this reason, aware of their difficulty in competing in terms of costs alone on global markets, the priority of European governments should be to develop more effectively a different model of competitiveness based on innovation and research. Rather than leaving individual countries alone to gain this kind of competitive edge as happens today, a more politically integrated Eurozone would pursue this goal by seeking to promote as added value something like a European identity, 'made in Europe' as a distinct brand, synonymous with high-quality standards, partially overlapping, but not necessarily in conflict with, other existing strong national brands, such as 'made in Germany' or 'made in Italy'.

In the end, the model of growth implied by the current constitution is not internally consistent. The insistence on monetary and fiscal stability as preconditions for growth is certainly aimed at increasing the euro's reputation on financial markets. However, one by-product of this policy is to undermine the very export-led growth in the Eurozone pursued by this constitution: indeed, due to its strong reputation, the euro has been constantly overvalued in recent years with respect to key currencies, such as the dollar or the yuan, thus crowding out those goods which are more exposed to price competition by emerging countries. A higher degree of political integration would perhaps break this vicious circle by changing the source of the euro's reputation. The strength of the euro as a global reserve currency in the international monetary system should derive primarily from political union itself and Europe's ability to grow rather than from the anti-inflationary obsession of the European Central Bank. In my view it is quite wrong to leave the latter alone to fill a political void for one simple reason: low inflation per se is simply not a sufficient condition for growth.

Let us now turn to the second pillar of the current economic constitution, namely the one-sided emphasis on structural reforms as a direct way to stimulate growth. It is sufficient to note here a basic drawback in this approach. In my view, it fails to work not just because of political opposition, but also because it ignores the 'true' drivers of growth. Strictly speaking, I am not claiming that structural reforms and the supply factors are irrelevant for growth, but that they influence outcomes only indirectly through aggregate demand factors. For example, it is misleading to suggest that relative low productivity growth in Europe is simply due to structural factors, such as inefficient labour market, high taxes, bad infrastructure and the inefficiency of the state or technological gap especially in services. It is necessary to recognize that this phenomenon is primarily due to low aggregate demand and that the structural factors just mentioned play a role by undermining the propensity to invest or consume. The key problem of macroeconomics is that the latter are malleable factors; they fail to respond in a mechanical way either to changes in market prices, such as interest rates, or to changing structural factors, such as those mentioned above. In contrast with standard theory, in which such factors exercise a separate, direct influence on productivity growth (as the very notion of the production function implies), in my Keynesian vision they exercise an indirect and 'chemical' influence (that is they do not act separately), especially on investment. But this is not all. If we focus on this variable we can list a vast array of other determinants. Apart from the well-known, key factors, such as psychology, convention and cultural matrix, which are grouped under the 'expectations' label, investment also depends upon a complex and 'chemical' combination of institutional factors including those such as education and public expenditure underlying R&D, which are often labelled as 'the national system of innovation'. It is possible perhaps to summarize all these influences on investment by using the term 'trust'. In this way, we suggest that all the factors mentioned above combine in an unpredictable manner to determine outcomes and a key role in this combination is played by policy. Indeed, 'trust' can be seen as the product of a state's ability to coordinate factors such as education, welfare, cultural resources; these factors do not influence separately income growth as in orthodox stories based on the production function, but in combined form through institutional mediation.

It is important to note a few significant implications of this alternative stance. First, although structural reforms may be important (there is no doubt, for example, that low taxation and good infrastructure may attract investment from abroad), they may fail to stimulate investment in a context in which expectations are depressed and austerity plans are devised, such as the current one. This is the reason why the twin pillars of the current constitution fail to work. Structural reforms and monetary and financial stability are both seen as separate, though complementary, preconditions of growth when in fact they may be in contrast with each other and are, at least partly, the product of growth. For example, higher growth rates make it easier to repay or sustain debt and achieve financial stability (for a similar view, see, e.g., Krugman, 2010).

Second, this approach attributes a positive role to welfare. While the standard model regards welfare as a burden in view of its full employment assumption (as already noted, those like *The Economist* who follow its precepts regard the 'European social model' as too expensive), in my view, instead, welfare is a positive factor for stability and growth because it increases 'trust'. It can be argued, for example, that the problem is not simply to consume more; there is a lack (rather than too much) of public demand especially for relational goods, concerning services, such as assistance, health, culture and education, which may be able to stimulate investment. In this way, my approach seeks to overcome the gap between the economic visions that emphasize the positive role of factors such as culture, welfare and income redistribution (e.g., Sen's capabilities approach) on the one hand and the current macroeconomic paradigms on the other.[6]

In the end, this approach reveals a major weakness in the Eurozone, namely that it lacks trust and trust-generating policies. A stronger form of political union would also remedy this weakness. What I mean by this is that European countries still behave too much as national economies and still fail to coordinate effectively factors such as education, welfare and cultural resources. This is perhaps the main reason behind the failure of the Lisbon strategy, which is a set of goals without the ability to act to pursue them.

In conclusion, it should be noted that by representing economic principles buttressed by law, apparently endowed with higher degree of objectivity, the current constitution itself inevitably favours the status quo and encourages people to regard any deviation from its norm in negative terms. It thus somehow justifies commentators, such as *The Economist*, in describing political integration in the Eurozone as a necessary move towards protectionism or dirigisme, when it actually means instead greater chances to favour growth by allowing active fiscal policy in difficult times such as these, an option which is not available today for individual countries except in negative terms as violation of the SGP.[7] In other words, I suggest that what is missing in Europe today, due to a lack of political integration, is the fiscal counterpart of what already exists at the monetary level – that is, the common currency and monetary policy between a number of countries (for a similar view, see, e.g., Benigno, 2010; Reichlin and Borri, 2010; Soros, 2010; Stiglitz, 2010). It must be noted that what is at stake is not just the possibility to carry out countercyclical plans, such as the Obama plan. Clearly, such plans are costly and Europeans may not be prepared to pay more taxes to allow central government to implement them. However, a stronger form of political union in the Eurozone is desirable even if it does not increase the tax burden for its citizens. For example, debt financing would certainly be much easier and markets could tolerate more European debt than the current sum of individual national debts. It is sufficient to think, for example, that while today the sovereign debt of each Eurozone country is left alone to face markets, common eurobonds representing a cohesive political will should have a much stronger appeal; even if bigger deficits for the Eurozone as a whole are difficult to manage, there is little doubt that eurobonds could be more easily digested by markets than the sum of, say, Greek, Italian and Spanish bonds.

A final remark on the dividends of political integration should be added. The arguments presented so far are clearly quite general. Needless to say, many new problems are raised by a higher degree of integration: for example, how to determine the share of eurobonds that each single country could issue. In principle, only a centralized fiscal authority working under a new constitution appears able to solve this problem. However, it is not a sharp dichotomy between old and new constitution that I ultimately wish to underline. Some positive steps towards a better European cooperation can and have already been taken in the present institutional context, especially when facing exceptional events, such as the Greek crisis. It is important that Member States do not miss further opportunities to move in this direction.

Conclusion

The main conclusion that follows from this chapter is that the key problem of the Eurozone is represented by the insufficient degree of political integration between its members. The chapter also identifies two mutually reinforcing factors that account for this outcome. The first is the traditional concern for narrow national interest, which underlies, for example, the constant political in-fighting between key countries such as France and Germany. The other one is governments' actual reliance upon standard macro theory as a source of inspiration of the current 'economic constitution' and policies such as the recent austerity plans implemented in various European countries when still facing a very uncertain economic scenario. These factors account for the current 'muddle through' scenario which is a suboptimal state halfway between complete deflagration of the Eurozone on the one hand and the economic success which its members hoped for when adhering to the single currency project but has never been achieved on the other.

As a way out of this state of affairs, this chapter concludes that it is important to make people realize: 1. that the current constitution does not serve national interests well since it condemns Eurozone members to slow growth rates; 2. that such interests are best pursued by accepting a higher degree of political integration as the necessary premise for devising a new economic constitution, allowing Eurozone members in particular to carry out a full-blown discretionary fiscal policy like other federal states, such as the US. This chapter has tried to show that this constitution cannot be *ad hoc*, a mere expression of pragmatism, but must rely on an alternative theoretical framework capable of integrating stability and growth issues in a better way than orthodox theory does.

Notes

1. According to the Free Dictionary, which is available on the web, 'muddle through' means 'to manage to get through something awkwardly'.
2. As Krugman puts it, 'So the only way out is forward: to make the euro work, Europe needs to move much further toward political union, so that European nations start to function more like American states' (Krugman, 2010).
3. Indeed 'the single currency was always supposed to drive structural reforms, as once profligate countries were forced by the rules, and their peers, to live within their means' (*The Economist*, 2010b: 24).
4. For example, *The Economist* quotes Juncker, prime minister of Luxembourg, as claiming that 'We all know what to do, but we don't know how to get re-elected once we have done it' (*The Economist*, 2010a: 11).
5. According to Tabellini, stronger European intervention is needed for policies to unify markets, especially in environment, telecoms and information and those providing public goods, such as research and infrastructures, where it is not necessary to deal with other supply-side reforms.
6. This critique applies not just to standard neo-classical theory, unable to accommodate a positive role for welfare in view of its full employment assumption, but also to current versions of the Keynesian paradigm which are

often criticized for neglecting these factors in view of its aggregative nature (see Sen, 2009).

7. This negative bias against European political integration emerges clearly when commentators carry out international comparisons. For example, while the US is widely regarded as the best incarnation of capitalism in line with the neo-classical model, commentators comparing it favourably with the Eurozone tend to forget that it does implement a full-blown discretionary fiscal policy.

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