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## **What was he doing at the Eurogroup?**

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By attending the meeting of ministers of the euro area on Monday 9 July Nicolas Sarkozy was above all making a political statement. This was a 'first', after a decade in which heads of state and government of the euro area have been conspicuous by their absence. They have never met in a euro context, not even at the birth of their common currency. Having taken a momentous decision, they promptly left implementation of the euro to financial technicians. By going to the Eurogroup, Nicolas Sarkozy clearly intended to mark the end of this long absence.

Beyond the symbolism, however, Europe was curious as to his motives and many are worried. Criticised for a fiscal policy which has departed from the agreed objective, was the President of France seeking the consent of partner countries to this departure? Was he launching an offensive designed to dilute the independence of the European Central Bank? And what is this 'economic government' which all the French leaders are calling for but none has pinned down exactly?

Few Frenchmen realise the extent to which the ideas they share may appear odd to their partners. The reason for this is that the euro means different things to different peoples. For some, for example the Netherlands and Austria, it allowed a belated ceding of a sovereignty perceived as existing in name only. They see monetary union as a necessary framework for national economic policy – a little like the gold standard underpinned disciplines in the 19<sup>th</sup> century without implying political affiliation. From this standpoint, the euro needs only an independent central bank and rules governing budgetary discipline.

For Germany, as for France, the single currency has, on the contrary, profound political significance. But not the same one. In the German mind, the euro symbolises a common destiny. Former President of the Bundesbank Hans Tietmeyer liked to say that the currency did not belong to the prince but to the community. A monetary union must therefore be accompanied by political union, federal in nature, which allows the people to accept the rigour of the rules. On the other hand, for the French, a currency remains an attribute of state sovereignty and its transfer to the European level entails the construction of other elements of shared sovereignty. Governance by political decision is what bears witness to the political commitment of the states and what renders a federal construction superfluous.

France under Mitterrand refused both a non-political currency and federalism at Maastricht in 1991. This approach is close to that of the British, probably the partner country with the most similar conception of macroeconomic policy to our own, except that the British have drawn different conclusions. Ever since then, we have been a lone voice pleading the case of the euro as a driver of coordination of national policies.

One can swim against the tide and still make headway. But you need consistency and this is what has been missing. By failing to spell out what exactly it wanted, France has managed to alienate potential supporters. The high priest of policy coordination has, among all governments, been the first to depart from it. In a nutshell, France has not 'walked the talk'. In fact, the already vague notion of 'economic government' has gradually lost its meaning. The provisions of the EU treaty designed to bring it to life have in part fallen into disuse. Optimists see in this a plan in need of focus. Many others see it as a figleaf for ambitions which dare not speak their name.

What remains of the French ideas is the Eurogroup itself, which is appreciated as a body; a political intuition; and a project. The intuition is that it makes little sense to have a common currency and separate economies and that the single currency will not keep its promise without renewed political commitment and ambitious governance. This is a reasonable argument. Some are quick to boil down the euro to a set of fiscal benchmarks. However, the yawning competitiveness gaps in the euro zone do not owe much to the situation of public finances. And with fixed exchange rates the initial years are the easiest. Problems mount as inflation spreads accumulate. Furthermore, few countries have seriously pondered how their economy would react to internal and external shocks without the monetary lever. Few have put in place reforms sufficient to guarantee the necessary flexibility. If handled badly, such problems could handicap the working of the euro area as a whole. These are the problems which collegiate governance is designed to diagnose and treat.

The project is to acquire an external identity which will allow the euro area to box its weight in international money and finance. The need for this project, which has been a hallmark of French initiatives from the outset, is all the more apparent in the present context of rapid change in power relationships. The countries of the euro area are at the same time overrepresented in international organisations and weak in financial negotiations. The debate about the Chinese exchange rate illustrates this well. While the issue is just as important for Europe as for the US, the discussion is essentially a bilateral between Washington and Beijing. What is the point in having one third of the votes in the IMF if the US calls the tune? The emerging countries are calling upon Europe ever more stridently to stop collecting seats everywhere when this does not reflect its economic weight. They are implicitly inviting us to be consistent, unite and exchange numerical weight for real influence.

Heads of state and government would do well to invest in these two areas, because the stakes are far too high for ministers of finance. The latter cannot, alone, pilot the reforms which will make economies more responsive, make clear the implications of the monetary commitment and agree to the ceding of national sovereignty which is needed to gain external influence. It would be worthwhile for the European Council to meet at least once in euro area format.

If this is the meaning of Nicolas Sarkozy's appearance at the Eurogroup, however, he should start by overcoming the credibility gap created by our past behaviour and his own first budgetary decisions.

This of course implies accepting the statutory independence of the ECB and recognising its exchange rate prerogatives.

It also means scotching the ambiguity about the impending enlargement of the euro area. It is fine to intensify cooperation on the currency but it is risky to imply that the door to the club might be closed. Any deepening of the euro will be blocked by the other countries of the Union unless they receive clear assurances on this point.

And lastly it means playing the agreed budgetary discipline game. One cannot at the same time plead for a strengthening of the euro and ignore agreements already reached. It is legitimate to discuss the budgetary cost of reforms designed to boost growth potential and the flexibility of the economy but European budgetary principles rule out completely a country in deficit taking demand-side measures in a boom time, as France has just done. That is a sizable obstacle on the path towards a productive discussion between France and its partners.

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