# The single market and growth for Europe

*Bruegel Debate, 9 November 2011, European Parliament*

UK Deputy Prime Minister Nick Clegg delivered a talk on the topic of the "Single Market and growth for Europe" on the 9th of November, at the European Parliament. The event was chaired by Guntram Wolff, deputy director at Bruegel. Discussants included Benedicta Marzinotto, research fellow at Bruegel, and Andreas Schwab, MEP.

Nick Clegg began his speech by arguing that international focus has now shifted from Athens to Rome and that there is much to be done to ensure stability in the eurozone. He stressed that the UK would support Europe in its endeavour to solve the current problems.

Mr Clegg identified growth as a key weapon against Europe's debt and deficit problems, and argued that while financial and fiscal stability are important in their own right, they do not deliver growth. Europe is currently suffering from a crisis of competitiveness and the demographics are currently against it. The continent is also being side-lined by the economic powers of the East. Furthermore, the Commission's worst case scenario prediction for 1.5 percent growth for the EU, made in March, is close to becoming reality. Unless Europe becomes more competitive, it will find itself in perpetual decline, Mr Clegg argued. Decline is not inevitable however. The resolution of current problems comes down to political will. Europe has some of the best institutional establishments in the world, it has excellent regional cooperation and is already a leader in various industries.

Mr Clegg argued that European integration has always been defined by moments of great upheaval, such as the Second World War, the economic stagnation of the 1970s or the collapse of the Soviet Union. One can indeed learn from such episodes. To succeed, reform is necessary. The Deputy Prime Minister's opinion was strong on this issue: "reform or wither", he told the audience at the European Parliament. Europe needs to change its default response to economic problems, which currently involves implementing treaty changes. This cannot be a surrogate for political will and before original clauses are rewritten, one needs to see if the clauses cannot actually be met via other means.

Mr Clegg then went on to highlight three principles that should guide reform, without appealing to British wisdom and being aware of the fact that the UK is also struggling. For a long time, Mr Clegg argued, European economies were seen as belonging to one of two camps: the Anglo-Saxon camp, with a tolerant approach to risk and flexible labour and product markets, and a mainland camp, taking fewer risks, endorsing a stronger role for the state and placing a smaller emphasis on short run gains. Both have had their shortcomings. The former's attitude to risk lead to huge liabilities, while the latter's rigidity in product and labour markets was problematic. None of the two sides had all the answers and countries could indeed learn from each other.

The first pillar of reform would be unity among European countries. "To retreat from each other now will mean to leave ourselves isolated in extremely tempestuous times," Mr Clegg argued. At the same time, he acknowledged the fact that the EU still has its flaws, and that a lot can be done to deepen the single market, creating an EU wide patent, tackling international crime, energy security issues and climate change. There are also areas where member states are better placed to take the lead. These include the common fisheries policies, youth policy, tourism and culture. There are also policy areas in which the EU has gone beyond setting legitimate standards to protect workers and consumers and promote competition, and has instead imposed "a straitjacket of uniformity" on different sectors. This is a trend that has undermined the ability of

EU states to compete internationally and should be reversed.

He stressed that the UK understands the need to re-regulate financial services. In light of this, the coalition has introduced a bank levy. The UK government however remains against a financial transaction tax, owing both to the disproportional impact it would have on the City of London, as well due to its effect on EU GDP. According to Mr Clegg, the tax completely misses its desired target, as it does not affect the authors of the financial crisis, but it does affect pensioners and businesses that employ thousands of people across Europe.

A second path of reform involves prioritizing growth. The Commission should ensure that all proposals made from now onwards contribute to growth, and that no proposal that undermines Europe's long-term competitiveness is adopted. Mr Clegg further expressed his support of the new growth test. More can be done in this direction however and he suggested that a special session of the council could be in charge of preparing a report card for every European council on the growth impact achieved since it last met. This should praise growth enhancing policies, while also signposting the legislation which has failed the test.

The third pillar of reform would be openness. Mr Clegg called for a stop to protectionism and *beggar-thy-neighbour* policies. Unfortunately, even 20 years after the creation of the single market, the latter is still incomplete, with free trade still obstructed in many ways. Some problems are related to online trade, which remains underexploited. Problems also persist with regards to the recognition of professional qualifications across borders, and with regards to the registration of businesses abroad. The Deputy Prime Minister reiterated the UK's support of the single market act, and the Commission's work, but argued that much more had to be done to modernize and complete the single market by 2015. Some directions for change include fast-tracking the most pro- growth and pro-job areas, liberalizing services, and creating a proper digital single market. These measures alone could add €800 billion to the EU's economy.

Mr Clegg further identified the services sector as a driver of the economy and thus argued that the Services Directive should be implemented in full. He went on to suggest that an ombudsman could be required to work in tandem with the Commission and member states in order to find out first hand where barriers are and how they can be removed.

Clegg concluded by arguing that division between nations has threatened the prosperity and security of European citizens in the past and that much more can be achieved by sticking together.

The first discussant then took over the debate. Andreas Schwab expressed his agreement with the majority of points raised by Mr Clegg. He argued however that not only the services industry is important, but that also more traditional industries can play a crucial role in times of crises and that one shouldn't forget about them. He further expressed his disagreement with the UK view on the financial transactions tax and argued that the tax is not targeted against the City of London and should not be perceived as excessively harmful. Mr Clegg however reiterated his firm disbelief in such a tax, arguing that according to the Commission's own assessment, the tax would destroy half a million jobs. A European financial activities tax or a global financial transactions tax represent more sensible alternatives, he argued.

Benedicta Marzinotto then took over the discussion. She expressed her agreement with the importance of growth as a key tool for addressing structural challenges. "Europe has not grown to its limits and there is a huge potential that needs to be exploited," she argued. She then went on to highlight some of the underlying problems of the Maastricht treaty in relation to growth. The treaty had assumed that stability would lead to growth, which was a mistake. A second mistake was keeping the stability at the macro level and the elimination of barriers at the micro level separate. The crisis taught us that when you have slow growth you have macroeconomic instability, which makes it clear that growth does not play a secondary role. She went on to argue that the single market is an unfinished business, which also reflects unfinished politics.

Talking about the future of European industries, she suggested that services were important, as they made up a large portion of EU value added, but that one should not forget about manufacturing. As a recent Bruegel study on unit labour costs reveals, the huge divergences that exist between costs and price competitiveness, are not due to rigidities in labour markets but to a large extent are due to structural changes in European economies. Changes in unit labour cost have been driven by the downsizing of the manufacturing sector. This in turn raises the question of whether a stronger industrial policy at the EU level is necessary.

Mr Clegg expressed his agreement with these statements, reiterating the fact that the Maastricht Treaty had made a big mistake at the macro level. The belief had been that the euro would put an end to devaluations as a means of escaping economic problems, and would in turn determine EU governments to carry out structural reforms, such as labour and product market liberalization. This did not occur. Instead, credit became cheaper, especially in periphery countries, and an illusion of growth emerged. He further highlighted the British commitment to the manufacturing sector, giving as examples current tax breaks, as well as the opening of technology centres, and the promotion of vocational training in this field.

Guntram Wolff suggested that the fiscal unity of the eurozone is necessary to avoid bank runs which can't be stopped by national fiscal policies. However, once one moves to federal Eurozone fiscal policies of this kind one talks about financial and banking supervision that needs to be much stronger at the eurozone level. He expressed general concerns that "whatever saves the euro" may destroy the EU.

Mr Clegg argued that one could indeed save the euro without destroying the EU. He believes that a total fiscal union would not solve the problem of the banking sector. According to Mr Clegg, the problem is the fact that Europe has banks that are too big to fail. To address this issue, regulatory reforms need to be introduced to make these banks more responsible. There is also a need for rules to avoid sovereign debt problems and perhaps sharing of debt, through means such as Eurobonds, which may be introduced in ten years or so. Mr Clegg ultimately believes in incremental change, which does not involve treaty changes. He thus told the audience at the Parliament that one does not call an architect to discuss the house plans when one's house is on fire. Similarly, Europe needs to develop economic solutions, not legalistic ones.

The last addition to the debate came from Malcolm Harbour, MEP and Chairman of the European Parliament's Internal Market and Consumer Protection Committee. He expressed his concern that the single market is not discussed sufficiently at the moment, particularly in the UK. He further stressed his discontent with the fact that UK businesses are not well informed about the Services Directive, and that other decisions reached by the Committee are not promoted sufficiently.

Clegg appreciated that these were valid concerns, he went on to argue however that not all policies, while important in their own right, promote growth. At the current time however, Europe cannot afford to be even handed anymore. "We have to say that growth has to trump everything else," he concluded. This is the only way one can avoid falling back in a state of economic crisis in the future.