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THE EUROPEAN

The European View

What's in a name?

Merkel/Sarkozy letter: historic steps for the eurozone... but could they spell the death knell of Britain in the EU?

The European Defence Agency: improving European defence capabilities



REGENT'S COLLEGE
LONDON

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The European View

Perhaps the flightless African bird does not deserve the reputation it has acquired but in terms of symbolism at least the British government's reaction to the eurozone crisis resembles a lot the ostrich's alleged tendency to bury its head in the ground when confronted with danger.

Because there is no other way one can describe how Mr Cameron and Mr Osborne have reacted as financial and stock markets seem to implode around them. Even though they have acknowledged the severity of the situation, even though they have admitted that what happens in the eurozone has a direct impact on the UK economy, even though they have gone as far as encouraging their EU partners to adopt the measures necessary to contain the crisis, they have declared, with immense but ill-founded pride, that they are keeping themselves, and the country, away from the decision-making process that aims to resolve the present crisis and put in place the mechanisms that will strengthen the eurozone and safeguard the European economy.

This is where the truly dangerous surrender of national sovereignty lies. When the growth of the British economy depends to such a big degree to the well-being of the eurozone, when billions are wiped off the value of British assets in the London Stock Exchange because of the uncertainty the debt crisis has caused in the financial markets, the British government cannot afford to just stand by idly, inviting others to make decisions that affect the country so profoundly. Whether Mr Cameron and his eurosceptic backbenchers like it or not, the UK is by default part of the eurozone. The British economy is integrated with those of our European partners through the Single Market. The ability of our export sector to generate growth at home depends on the

ability of our European partners to purchase our goods and services. The European financial services sector, with London at its heart, is interconnected through a complex web that links the banks and other financial institutions with something that resembles a stranglehold. Even the cost of our holidays depends on economic conditions in the rest of Europe. Sticking our heads in the ground, like senior Conservatives – in and outside the government – are calling for, pretending that it is up to 'those Europeans' to sort this one out, like we have nothing to do with it, is frankly a clear case of biting one's nose to spite one's face.

But there is a pattern in their madness. Their intention is to present the process of European integration as a speeding train, one that charges towards a certain direction, a train that the UK cannot and should not board. They in fact prefer to encourage members of the eurozone to move forward towards closer economic and fiscal union in the belief that the British electorate will be put off once and for all by the prospect of the European project. Then the government will pursue some kind of marginal role at the periphery of the EU, limited on trade and a couple of other things but staying clear of anything as big as economic, monetary and fiscal union. In effect create a two-speed Europe and relegate Britain to the second tier.

Those two Europes that the Conservatives envision are the eurozone on one side and the non-eurozone EU member states on the other. But of the 10 remaining EU countries that have not joined the single currency yet only the UK and Denmark have an opt-out. All the other member states have declared their wish to eventually join (once they are ready). Even Denmark is in a process of revisiting its opt outs, including euro membership. So sooner than later the UK will find itself all alone, at the outer rim of the EU,

a small island, adrift in the Atlantic, squeezed between two global currencies, the dollar and the euro (not to mention the renminbi). Alienated, without a seat around the table, unable to influence the decisions that affect its economy.

There were two Europes before, during the days when the European Economic Community (that eventually became the European Union) co-existed with the European Free Trade Association (EFTA). What happened then is what will happen with this two-speed Europe. EFTA states, including the UK, quickly realised which was the organisation worth belonging to and eventually drifted into it, in many cases too late to have any influence in the formation of its fundamental structures. What is left of EFTA these days is a tiny grouping, made up of Norway, Iceland, Liechtenstein and in some way and form Switzerland. These remaining EFTA states, reluctant to join the EU but keen to participate in the Single Market, Schengen and other EU policies have to abide to the rules decided by EU member states without having a say in the way those rules are agreed and adopted (while at the same time contributing to the EU budget). Is this the fate the UK would like to reserve for itself? Is this the future the current government is happy to relegate the UK to? One of marginalised insignificance on the sidelines, having to accept the consequences of decisions that affect us but are taken without us?

The eurozone will survive and will continue its successful course through history. Its leaders have demonstrated their commitment and they will do whatever it takes, albeit at a pace different to that the markets, the press and many ambitious integrationists (like yours truly) might desire. It will survive because it possesses the necessary strength, its collective economic fundamentals are solid, it enjoys the confidence of world powers like the US and China and it has at its heart some of the most dynamic and global economies in the world. The question is whether the UK will be part of it or not.

Historians will one day look at what took place at this particular moment of European history. Whether they will acknowledge the UK as a strong and confident nation, at the heart of decisions that formed the future of our continent (and the world) or as a nation that turned inwards, closed itself up and resigned itself to a life of irrelevance in the sidelines will depend on what role Cameron and Co will decide to play from now on. Will they put their chips down, sit around the table and have a say in the hand the EU will play? Or will they leave through the back door while the rest of Europe moves forward?

I guess we will know soon.

Petros Fassoulas

What's in a name?

It is instructive to see how the name of the economic crisis that we have endured since 2008 has changed its name over time - or, rather, had its name changed by media or by vested interests.

Just three years ago, the term **credit crunch** was in vogue, with the focus being on the banking sector turning belly up. Now that the banking sector has managed to offload its debt on to the taxpayer, the term **sovereign debt crisis** is used - at least as regards those countries whose debt level (for that or for other reasons) is excessive. But what is curious is the degree

to which, especially in Britain, the term **euro crisis** has emerged.

After all, the euro as such is NOT in deep crisis. It has strengthened in value on international monetary markets (while the pound and the dollar have plummeted), it has maintained a low and stable inflation rate, the balance of payments of the eurozone is in broad equilibrium, its total public debt level is lower (yes, despite Greece, etc!) than the US or Japan, and the euro is beginning to gain the advantage of being held across the world as an alternative reserve currency to the dollar. Economic growth has returned to the eurozone as a whole (and especially in countries like Germany and France of comparable economic magnitudes to Britain, where growth is still stagnating).

Despite this, there are some interests who want to blame the euro instead of the world-wide downturn.

Yes, some eurozone countries have hit problems of excessive debt - just as have a number of countries outside of the eurozone (such as Iceland, Hungary, Romania, Japan and even the US). Various countries have received loans and this includes three eurozone countries (do the press ever mention any others?). The three eurozone countries in question amount to a total of 6% of the eurozone economy. To characterise the crisis a crisis of the euro as such is misleading - and often deliberately so.

In fact, we would do well to stand back and look at the wider picture. Europe is very much part of the solution, not the cause of the problem. When Europe was hit three years ago by the biggest economic tsunami since the Great Depression, we avoided most of the mistakes that we made in the 1930s.

We avoided protectionism – in no small part thanks to the single European market.

We largely avoided competitive currency devaluations – in no small part thanks to the euro (just imagine for one moment what would have happened if we had still had the French franc, the Spanish peseta, the Italian lira, the German mark, the Belgian franc and so on: there would have been in turmoil on the international currency markets in addition to the turmoil we already had).

So, we did some things right. But Europe does have a number of problems, in which it is not alone. Some are long-term and structural, not least our insufficient economic growth rates when faced with ageing populations, to which the Europe 2020 strategy (focussed on boosting research, investment, education, infrastructure) is intended to respond. Insufficient attention is being paid to it – yet it is fundamental to improving Europe's underlying growth capacity – both for countries inside and outside the euro. A further deepening of the single market – which is, after all the world's largest market – offers further potential, especially for the further integration of service markets.

And, to return to the debt problem, it casts a long shadow. But the risks of spill-over and contagion from indebted countries to others is not actually a simple internal matter for the eurozone. The country whose banks have the third highest level of exposure to Greece is the UK. So, efforts to avoid the Greek defaults are efforts to avoid job losses all across Europe – including Britain. Ditto for assistance to Ireland – and this was recognised by the British government, complementing the eurozone loan with a bilateral loan of its own. The size and importance of the financial sector to the British economy makes it particularly vulnerable to contagion. After all, Britain

had a big enough problem with tiny Iceland (outside the euro) and would certainly be affected should any larger country go belly up.

But at least in the eurozone, efforts are being made to address the issue. The three eurozone countries in question (Greece, Ireland and Portugal) have received loans from their fellow eurozone members. Without these loans, their predicament would be even worse. But, the loans are not technically 'bailouts'. They are not grants or gifts. Nor has there been any assumption of liability for their debts. So it is wrong to say that taxpayers from other countries are having to fork out: the loans even attract interest so, unless there is a default, the lending countries will even gain financially.

The reasons for their excessive debts are diverse: profligacy in the case of Greece, the government

rescuing an overgrown and bankrupt banking sector in the case of Ireland, and so on. Giving the countries concerned time to turn the corner, and preventing contagion, is not without problems nor controversy. Yet it is essential, not just for them, nor just for the stability of the euro, but for the stability of the whole of the European economy and beyond.

It would be a great service to rational debate on these issues if they were characterised as what they are, rather than be hijacked by a eurosceptic agenda seeking to discredit the euro.

Richard Corbett

Former MEP & Member of the European Movement's National Executive

Merkel/Sarkozy letter: historic step for the eurozone... but could they spell the death knell of Britain in the EU?

Though dismissed by most of the English-language media, this letter contains ideas that could well have profound and historic implications. The proposals include: rapid completion of existing economic governance measures; a legally-entrenched balanced budget rule; economic governance by the eurozone Heads of Government, concluding the negotiations for a common tax base for companies; 'enhanced co-operation' in tax co-ordination; sanctioning states by withholding structural funds; Franco-German corporate tax harmonisation and a proposal for a financial transaction tax.

These proposals will ensure fierce debate about the nature of 'Europe' in the next few months. Will EU leaders really have the political courage to implement such ideas? A steady movement in budget deficits along the projected track from 7% of GDP in 2009 to less than 4% next year should revive market confidence as the existing SGP commitments are for a 1.5% of GDP deficit in 2014. An agreement early in 2012 to install a balanced budget regime thereafter should preclude another crisis of this type in the future.

Do the two leaders really mean what they are saying? There is a simple, acid test ahead – for France in particular. The two governments call for the 'rapid completion' of the six-pack of legislation on macro-economic surveillance. This includes the provision of a reverse qualified majority voting for the member states to stop a Commission recommendation for action (and sanctions) against a state that is not

dealing with identified imbalances. Given the steps already agreed, this would be the moment of collective control of an errant state – the final step towards a *de facto* political union (1).

However, there may be a deeper game unfolding: economic governance of the eurozone may be about to turn into economic ‘government’. Instead of a French concept with German content such as the Stability and Growth Pact, this proposal seems to have additional French content such as tax harmonisation and be far more inter-governmental. That would be a fundamental change in German attitudes as, traditionally, Germany has been the defender of the ‘Community method’ where the European Commission is the defender of a Treaty deliberately biased to protect the influence of the smaller states.

It is interesting that France and Germany have sought so strongly in recent months to re-assert their joint leadership role. But who else would be able to? Berlusconi in Italy is widely seen as a spent force, Zapatero in Spain will not be contesting the imminent election and Cameron in Britain has chosen, decisively, not to be involved – and even enacted a ‘referendum lock’ so that any further transfer of significant powers to the EU may have to be submitted to a referendum. Few would expect that to be won, so the UK will not now play any significant role in re-shaping the European Union to deal with this crisis.

The upshot is that France has had the opportunity to propose many of the economic governance ideas that it has long championed and Germany has not felt able to resist the ideas – except for the immediate issue of ‘Eurobonds’. The implications of a split between

France and Germany at this stage scarcely bear thinking about.

It is hardly a year since Chancellor Merkel would not countenance the Heads of Government of the eurozone meeting separately from the European Union Heads. Now she has agreed to a complete institutional framework for the euro area that is separate from that of the European Union:

- Heads of Government meeting twice a year (or more when needed); a President for two and a half year terms (but they have asked Van Rompuy to take this role – otherwise the split from the European Union would be an obvious chasm);
- This body would discipline errant members in breach of the European Union’s SGP;
- It would evaluate the development of competitiveness and act to prevent emergent problems (no mention of the role of the European Commission);
- The Eurogroup of finance ministers would be strengthened.

The thorny issue of tax is now to be tackled – the last taboo for majority voting but the pressure is to be put on to complete the ‘common consolidated corporate tax base’ proposal by end-2012. This author has always argued that would be the natural consequence of the decisions a decade ago to adopt International Accounting Standards for the entire EU – once companies account for their profits in a common format, it is obviously efficient for the tax authorities to use the same calculation.

But the plan goes further and calls for preventing ‘harmful tax practices’ – probably code for Ireland and some others! However, the Franco-German economic union is to take the next step itself and harmonise both their corporate tax base and rate – from 2013.

¹ For full details, see Graham Bishop’s recent book “*EU Fiscal Crisis: Forcing Eurozone Political Union in 2011?*” [link](#)

The gauntlet is powerfully thrown down to challenge the others!

Merkel and Sarkozy were explicit about using Art 136 for the eurozone members to take their own decisions and 'enhanced co-operation' – presumably for the members of the Euro Plus Pact (covering all EU members except Britain, Sweden, Hungary and Czech Republic).

However, France and Germany have decided to push a financial transaction tax very hard. This has been moving up the agenda for some time and the European Commission has made it into a revenue-raising plank of the 2014-20 budget. In principle, this should be agreed by unanimity of the member states in 2012, in good time for the start of the programme. Many financial market participants doubt if significant revenue would ever be collected from such a scheme – but the effort will certainly maximise anti-European feeling in the City of London (and its media friends) as

global financial businesses located in the City will be expected to pay significant revenues direct to the EU. This could trigger the moment of truth for Britain. If the 23 are forced to resort to 'enhanced co-operation' continuously to avoid a British veto by Conservative Party pressure or a referendum decision, then that will become such a norm that Britain could effectively be out of the EU. How long would it be before 'murky protectionism' began to take its toll on British exports to the EU, capital investment slithered away from Britain into the mainland to avoid that protectionism and the British media whipped up an anti-European hysteria that obliged an 'in or out' referendum? The writing is now writ large upon the wall.

Graham Bishop

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The European Defence Agency: improving European defence capabilities

A unique structure

The European Defence Agency (EDA) was established in 2004. It is the only agency mentioned in the EU treaties, and the only one whose Steering Board meets at the level of Defence Ministers (2). This double specificity puts it in a unique institutional position and gives it political impetus at the highest level. The EDA is not a supra-national body. It is intergovernmental: a tool at the service of its shareholders, member states.

² Denmark does not participate

Flexible and compact

EDA is small (fewer than 120 staff) but its expertise is widely acknowledged. It has an annual budget of some 30 million euros. Although this on the face of it is modest, it acts as a powerful lever: the work it launches and manages generates anything between 100 and 250 million euros in ad hoc projects. Its budget should not thus be seen in isolation: in military parlance, it acts as a force multiplier.

EDA's flexibility is also manifested in the configuration of the projects it runs. There are two types of project. Opt-out: all member states participate unless they choose not to; and opt-in: formed by two or more member states. EDA thus works à la carte: depending on their strategic priorities, their operational requirements, or their interest in a specific project,

member states decide the extent to which they wish to participate in the Agency's core work of projects and studies. In other words, EDA is where member states who wish to develop capabilities in cooperation can do so.

The full capability spectrum

EDA covers the full capability spectrum of capability development, from upstream Research & Technology (R&T) to Operational Deployment. In R&T the Agency is working on the technologies that will be required in the defence platforms of tomorrow. It does this either through specific R&T studies, or technology demonstrators. It also works with the European Commission on dual use (civil and military) technologies linked to the fight against Chemical, Biological, Radiological and Nuclear (CBRN) threats, Space, Maritime Surveillance, and Cyber Protection.

Turning to the operational deployment of capabilities, the Agency has trained over 150 helicopter crews, more than half of which have deployed to Afghanistan. In another concrete example – the fight against improvised explosive devices – the Agency has developed a forensic analysis laboratory to counter these weapons that can be so devastating for our armed forces. This laboratory recently deployed to Afghanistan. Two examples of EDA outputs that have been made available to NATO's ISAF operation; and of the close cooperation between EDA and NATO.

These are also concrete manifestations of Pooling & Sharing. But there are others, such as Air Transport, Maritime Surveillance, and Satellite Communications. Pooling & Sharing is not new to the Agency: in a way it has been EDA's modus operandi from the outset. Pooling & Sharing now has top-level impetus: Ministers of Defence discussed the issue at their meetings in the Foreign Affairs Council and the EDA Steering Board on 23 May. They acknowledged the

important contribution by EDA to this initiative and tasked it to submit proposals in the autumn on how it might be best taken forward.

Defence and other EU policies

The strengthening of the European Defence Technological and Industrial Base is a priority for the Agency. It achieves this through a close dialogue with defence ministries and industry: full transparency is the key. The Agency has thus established Codes of Conduct for industry as well as a Code of Conduct on offsets. The Agency is also playing a central role in striving to strike a balance between the single market on the one hand, and the specificities of the defence sector on the other.

EDA is active in maximising civil-military synergies. Its expertise is available to, and utilised by, member states in their consideration of the defence implications of a range of broader EU policies and initiatives, such as Radio Spectrum, Single European Sky, Cyber Defence, Unmanned Aircraft Systems and Space. The Agency is where defence ministries can identify and articulate their interests vis-à-vis these policies, as they did most recently at their Steering Board meeting on 23 May.

EDA and partners

The Agency does not live in a bubble. Relationships with the broader defence community are vital. In the same way that EDA is developing its relationship with other EU institutions such as the Commission, it is also working with third parties. It already has an Administrative Arrangement with Norway, which facilitates close practical cooperation. We signed a similar Arrangement with the European Space Agency on 20 June at Le Bourget. An Arrangement with Switzerland is also in preparation. The Agency has an excellent working relationship with NATO. And a number of other third states, such as the US, Ukraine

and Russia, also have dialogue and cooperation with the Agency.

Challenges

The EU faces three key challenges:

- The current climate of austerity which has led to dramatic cuts in European defence budgets;
- The lessons from the Libya operation;
- Political will.

Defence budgets across the EU have reduced by 15% over the last decade. But the demands placed on our armed forces have not reduced. If anything, the opposite is true. So, how to square the circle?

European defence is necessary, as shown by the lessons from Bosnia and Kosovo in the 90s and Libya today.

We therefore need to preserve and develop the European ability to act on the international stage. We must not put our credibility at risk. Europe cannot afford to become a second-tier player on the international scene. Moreover, as Robert Gates said in a recent speech in Brussels, Europe should not count on the US to do the heavy-lifting in the future. In other words, Europe needs to demonstrate its commitment and willingness to share the burden more equitably in order to preserve its vital relationship with the US.

The strategic challenge for Europe is to reconcile significant defence cuts with the need to provide a robust and credible defence capability.

This is a risk. But it is also an opportunity. It offers a chance to reform, and to launch a new dynamic. Cooperation is no longer simply an option: it has become a necessity. The cost of not cooperating would be significant: a decreasing spiral of reduced

capabilities, a negative effect on technological and industrial base, and a culture of demilitarisation.

Critically, however, this opportunity can only be realised if it is backed by strong political will.

The EDA is ideally placed to help. It has been described as the hub for European cooperation. EDA is the natural place to promote more cooperation in Europe in a flexible way. It was designed for this very purpose back in 2004. Now is the time to use it.

How?

- *By preparing the future together:* investment in research and technology is key to ensure the right capabilities of tomorrow.
- *By promoting more cooperation:* EDA is there to align the requirements among member states – preparing for joint projects and programmes and thereby achieving economies of scale. In other words, promoting coherence in place of fragmentation.
- *By pooling and sharing critical capabilities in Europe:* the examples of helicopters and counter-IED. Maritime Surveillance and Satellite Communications have been mentioned already. But this is not just about capabilities. EDA can help by promoting best practice, as well as the idea of ‘save and reinvest’: the savings achieved through pooling and sharing – which could amount to 30% - should be reinvested in defence. This is vital if Europe is to preserve the right investment for the capabilities that will be needed tomorrow.
- *By ensuring complementarity of work with NATO through transparency and dialogue:* The EU and NATO have 21 members in common. Dialogue and cooperation between the two organisations is thus a sine qua non. Despite the political difficulties which have been well-documented, EDA and NATO, notably Allied Command

Transformation (ACT), have established and continue to develop a close working relationship. This is vital if we are to avoid unnecessary duplication, as well as gaps.

- *By connecting civilian and military spheres to foster synergies:* there are many examples of dual-use technology. Space is one; maritime surveillance is another. The EDA acts as a bridge between Defence Ministries and the European Commission in order to maximise the potential of dual-use and to foster cooperation. This is a potential win-win situation.
- *By strengthening the European Defence Technological and Industrial Base:* A robust, competent and competitive European Defence Industrial Base is a prerequisite to improving the EU's defence capabilities, to satisfying the military capability needs of our Armed Forces and supporting the CSDP. Without a strong defence

industry, efforts to improve and sustain sovereign European military capabilities will fail.

Ambitious? Undoubtedly. But the EDA is ideally placed to support member states individually and collectively to acquire more with less. We will continue to fulfil this challenging mandate so that cooperation becomes the norm rather than the exception.

Claude-France Arnould

Chief Executive, European Defence Agency

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