

# EU and European Disintegration: A House of Horrors

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# Overview

- 2016 was a tough year for the European economy overall – but not in Germany: Falling unemployment, rising employment, steady growth...
- But then *Brexit* happened. What was that all about?
- The very real possibility of the collapse of the EU: A summary
- Constant theme: The increasing rejection of „globalization“ in political discourse, even in the USA
- Three Ghosts of European Past are coming back to haunt us
- Possible ways out of the house of horrors

# The Problem

- My bachelor course at the Humboldt University sees European economic integration as a consequence of inexorable forces:
  - „home-grown“ capital accumulation á la Solow/Swan
  - capital mobility / foreign direct investment
  - labor mobility
  - trade in goods and services
  - convergence of institutions, rule of law, macroeconomic shocks and policies
  - general political convergence, free exchange of ideas
- These forces are no longer inexorable – in fact they have been set in reverse in the past two years!

# What happened?

- These are the same forces that drive globalization – the increasing economic integration of the world's economies.
- Trade in particular, but also the movement of capital and people are essential components.
- Until recently there was consensus that globalization is good for you: Letting China produce our clothes, let Germany produce our cars, let the US produce our mobile telephones... (or not)
- Lower prices for all
- A great application of the principle of comparative advantage, which was given to us by the great economist David Ricardo

# What happened?

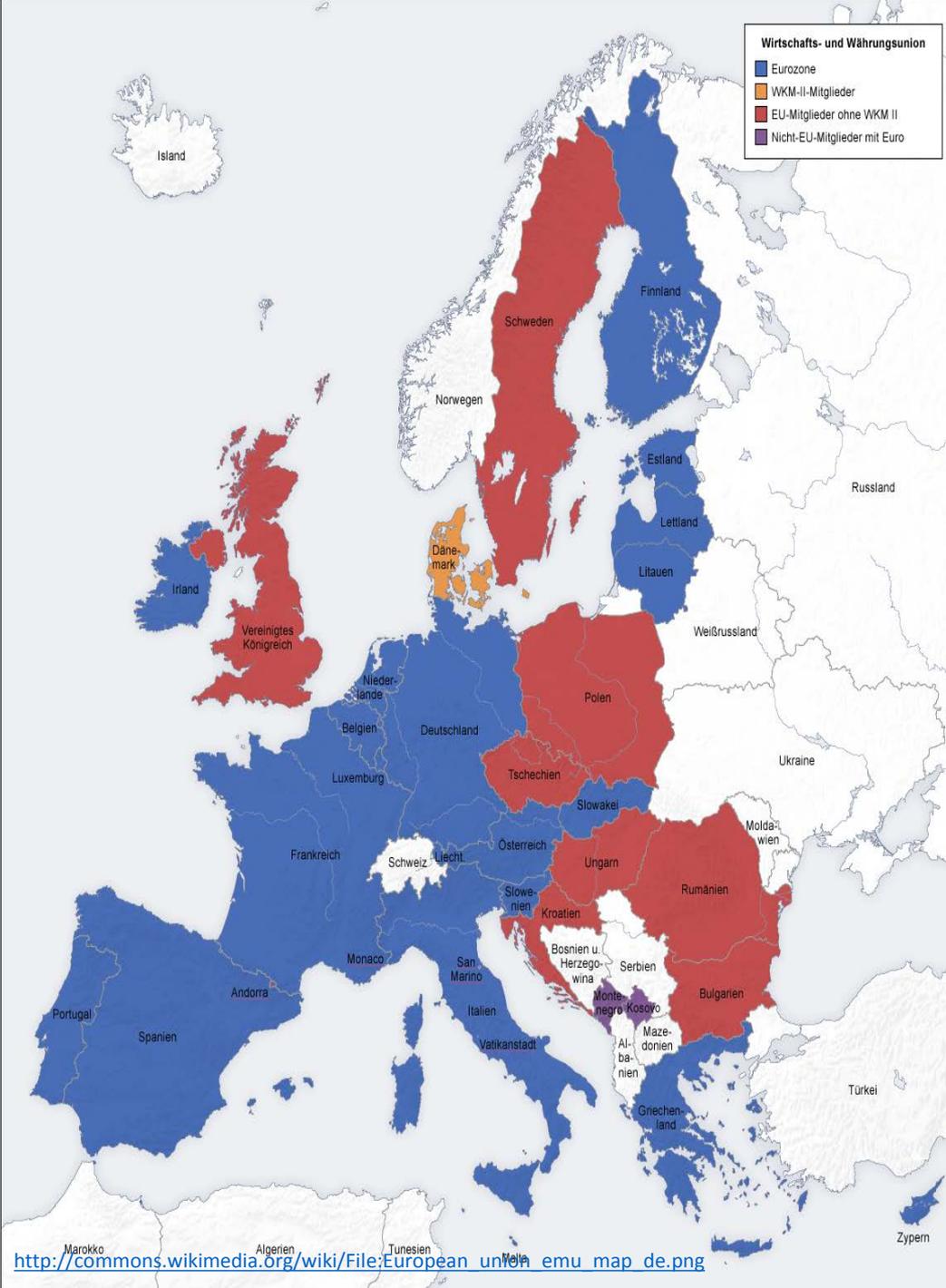
Recent years challenge this logic. In particular there's a *perception* that:

- globalization has led to loss of traditional industries
- gains from globalization are unevenly distributed
- familiar common places – main street, the malls, downtown – don't look quite the way they used to
- truth is relative – and in social media you can find „evidence“ for any position, some which are nonsense (e.g. „Make America great again“)
- experts (especially economists) advocate self-serving positions
- those in power („elites“) don't care about the little guy anymore.

# What happened?

- Nowhere is as vulnerable to this perception as *Europe* : A mosaic of nations all huddled together on a land mass much smaller than the US.
- Many (28) countries = many elections = rapid and frequent feedback
- Many economic interactions = interdependencies
- A history of duking it out at every opportunity
- That's why the EU exists

# EU in 2016



*Population:*  
510.3m

*Land mass:*  
4.38m km<sup>2</sup>

*Population density:*  
116 persons/km<sup>2</sup>

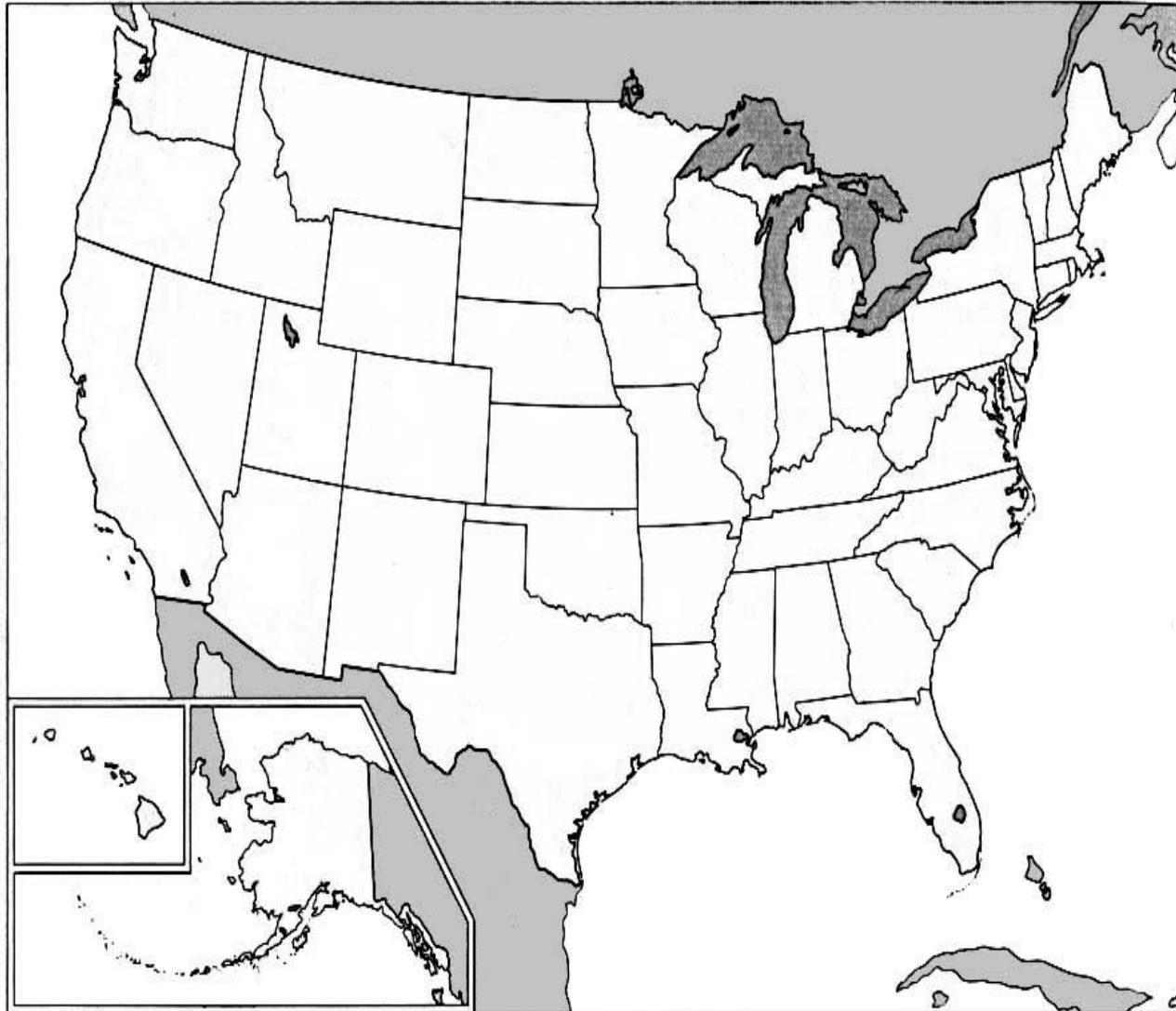
*GDP:* € 14.82 t

*GDP per capita:*  
€ 29,040

*Employment:*  
232m (45.5%)

*GDP / employed:*  
€ 63,880

# USA in 2016



*Population:*  
322.3m

*Land mass:*  
9.83m km<sup>2</sup>

*Population density:*  
33 persons/km<sup>2</sup>

*GDP:* € 16.87 t

*GDP per capita:*  
€ 52,300

*Employment:*  
154m (47,8%)

*GDP / employed:*  
€ 109,500

[https://www.lib.utexas.edu/maps/united\\_states/usa\\_blank.jpg](https://www.lib.utexas.edu/maps/united_states/usa_blank.jpg)

# Eurozone in 2016



*Population:*  
338.5m

*Surface area:*  
2.61m km<sup>2</sup>

*Population density:*  
130 persons/km<sup>2</sup>

*GDP:* €10.73 t

*GDP/capita:*  
€31,700

*Employment:*  
152m (44.9%)

*GDP / Employed :*  
€70,600



# Brexit: The background

- On June 23 2016, UK citizens voted in a referendum to leave the European Union (EU)
- The UK joined the EU in 1973 – after two failed attempts in the 1960s (due to French resistance). Joining was endorsed by a *63% majority* in 1975
- In 2016, the UK's elites – politicians, media, business executives – were convinced that Brexit would be rejected
- But in the run-up to that day, many undecided voters became supporters of Brexit. The final result: 51.9 to 48.1%

# Brexit: It will happen

- Despite the close vote and unclear nature of what they voted for, „Brexit,“ is going to happen:
  - Parliament passed the **European Union (Notification of Withdrawal) Act 2017**
  - the government of Theresa May will soon invoke Article 50 of the Treaty on European Union, after which the exit must be negotiated and concluded – *within two years*.
  - Great Britain devolves to minimum WTO member status with no trade preferences. This would be a disaster
  - Some form of Norway’s status (European Economic Area) seems likely, but UK would have to pay through the nose. For what?

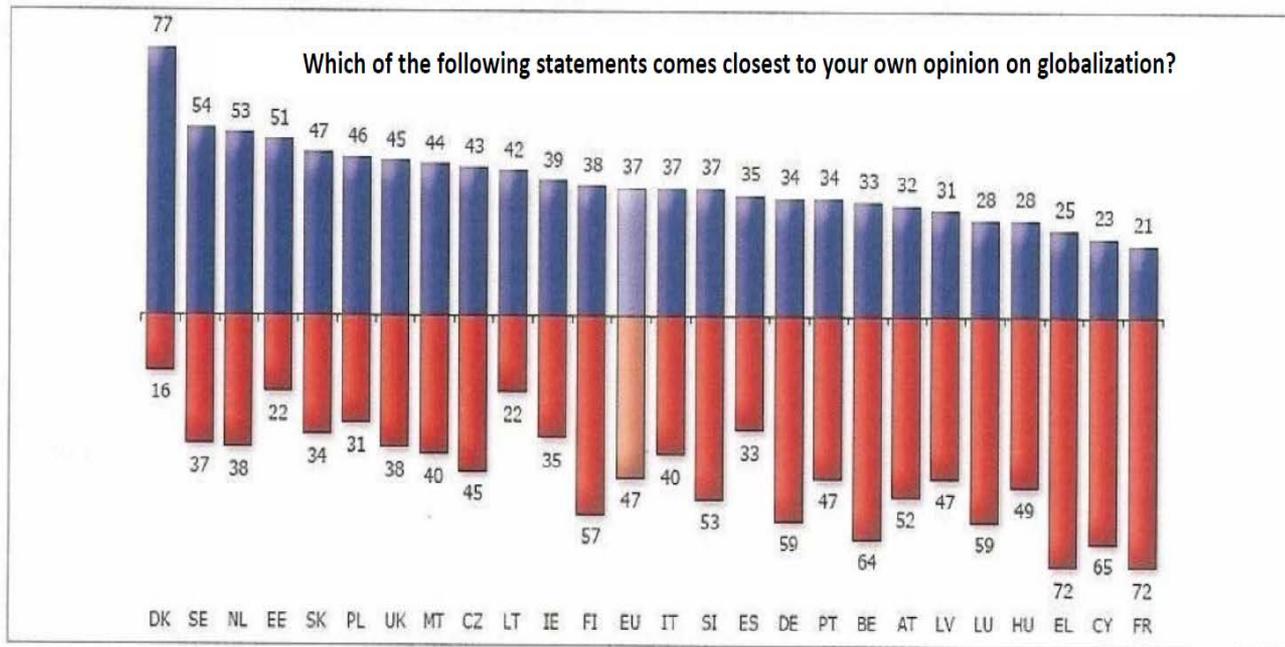
# Brexit: Why?

- It is complicated.
- Public rejection of the EU was a by-product of globalization for those who did not benefit or even lost as a result...
- ...as well as poor marketing by the EU and outright lying - „alternative facts“ and misuse of the EU as a scapegoat
- There was no plan for Brexit – Premier Cameron called the referendum in order to placate the right wing of the Tory Party
- Now the lawyers and negotiators are in charge – and tens of billions are at stake

# Brexit: Why?

- Brexit is a symptom of the EU's more fundamental problems:
  - The advantages of *further* integration are not evident to average people
  - The flood of refugees couldn't have come at a less favorable moment for most of Europe (Germany excepted)
  - A general perception of a democracy deficit in those countries where the losers are prevalent
- Since the Great Recession, integration has been moving backwards
- The „four freedoms“ anchored in the Maastricht Treaty are now being challenged
- Great deal of diversity in the EU on the question of free trade, or more generally globalization

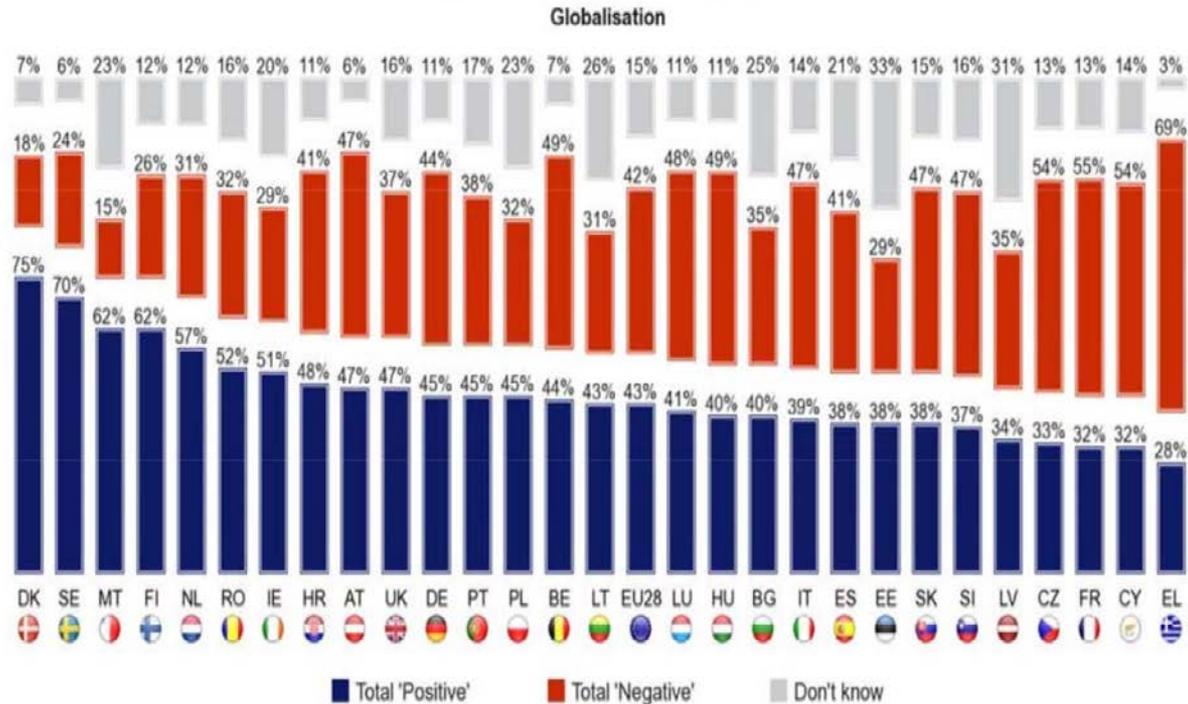
# Public opinion on globalization (2007)



- Globalization offers opportunities for the companies in my country
- Globalization is a threat to employment in the companies in my country

# Public opinion on globalization (2014)

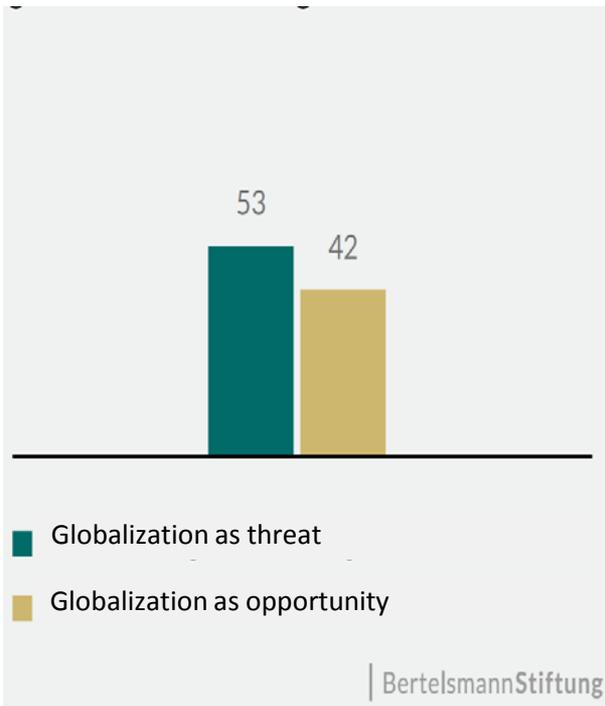
QA10.7. Could you please tell me for each of the following, whether the term brings to mind something very positive, fairly positive, fairly negative or very negative.



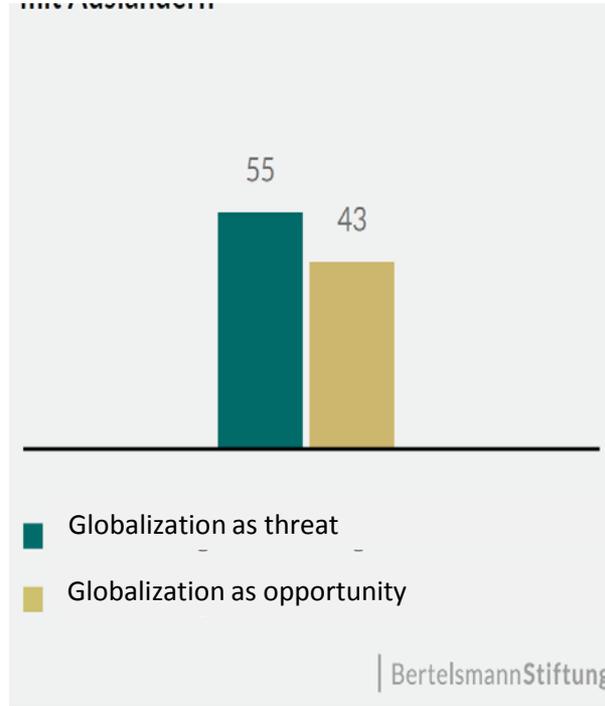
Source: European Commission (2014) PUBLIC OPINION IN THE EUROPEAN UNION, Standard Eurobarometer 82 Autumn 2014

# Bertelsmann Study (2017)

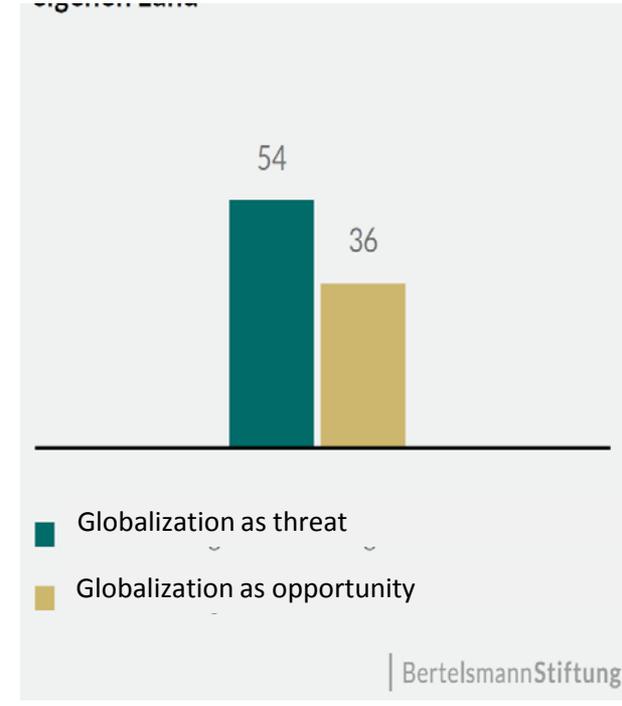
Those who consider migration to be a serious challenge for society see...



Those who have little or no contact with foreigners see...



Those who feel alienated or estranged in the own country see...



Source: Bertelsmann Foundation

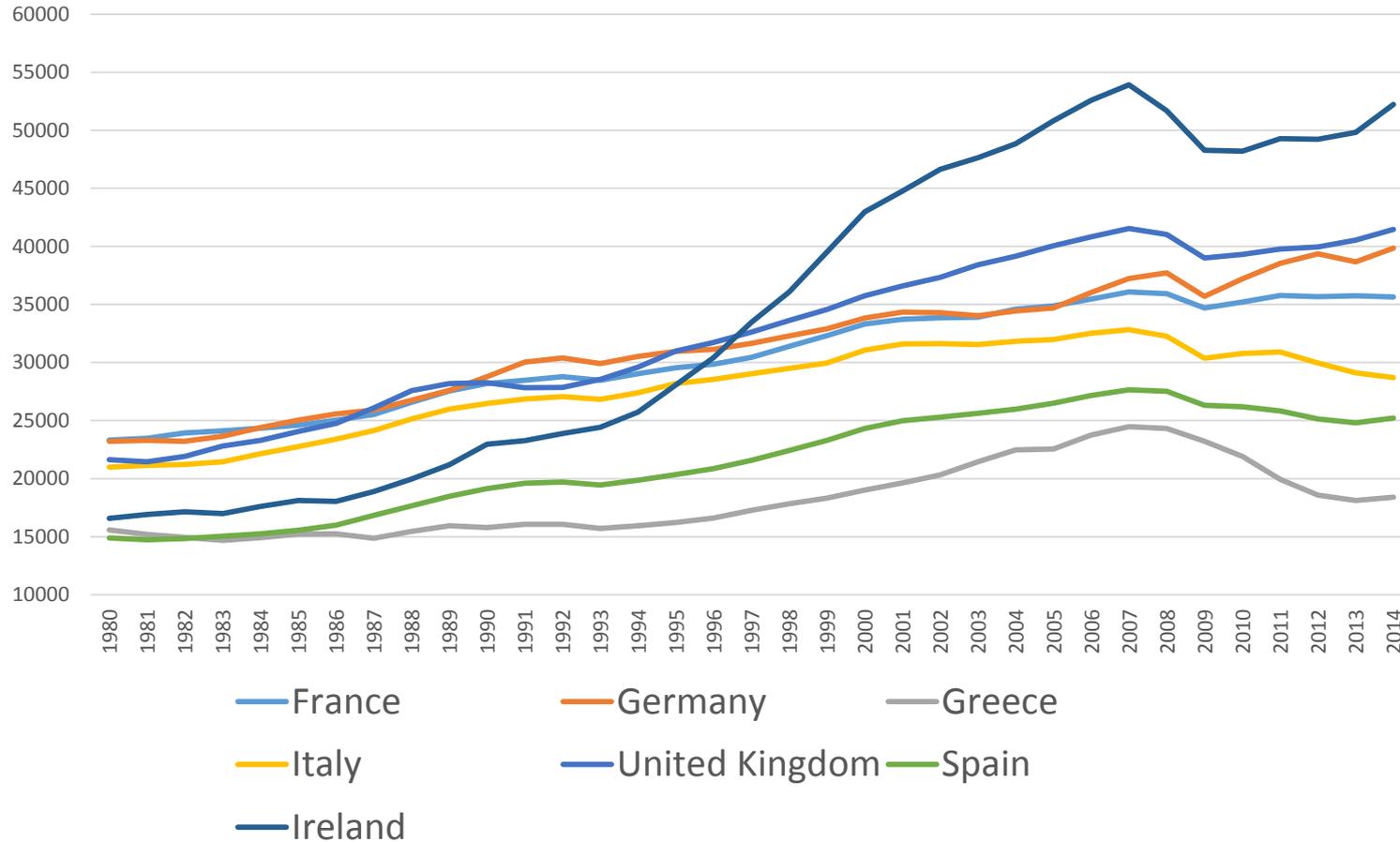
# The drivers of economic disintegration

## *Flagging economic growth:*

- Never so low for such a long time **Germany: 2015: 1.5%**
- Reflects a general development, even in fast-growing economies
- Never so divergent for so long (2015)
  - Italy **0.8%**
  - France **1.1%**
  - Greece **-0.2%**
  - Germany **1.5%**
  - Spain **3.2%**
  - Ireland **7.8%**
- Deadly in a monetary union – a chronic problem

# European divergence

GDP per capita (levels), USD of 2005

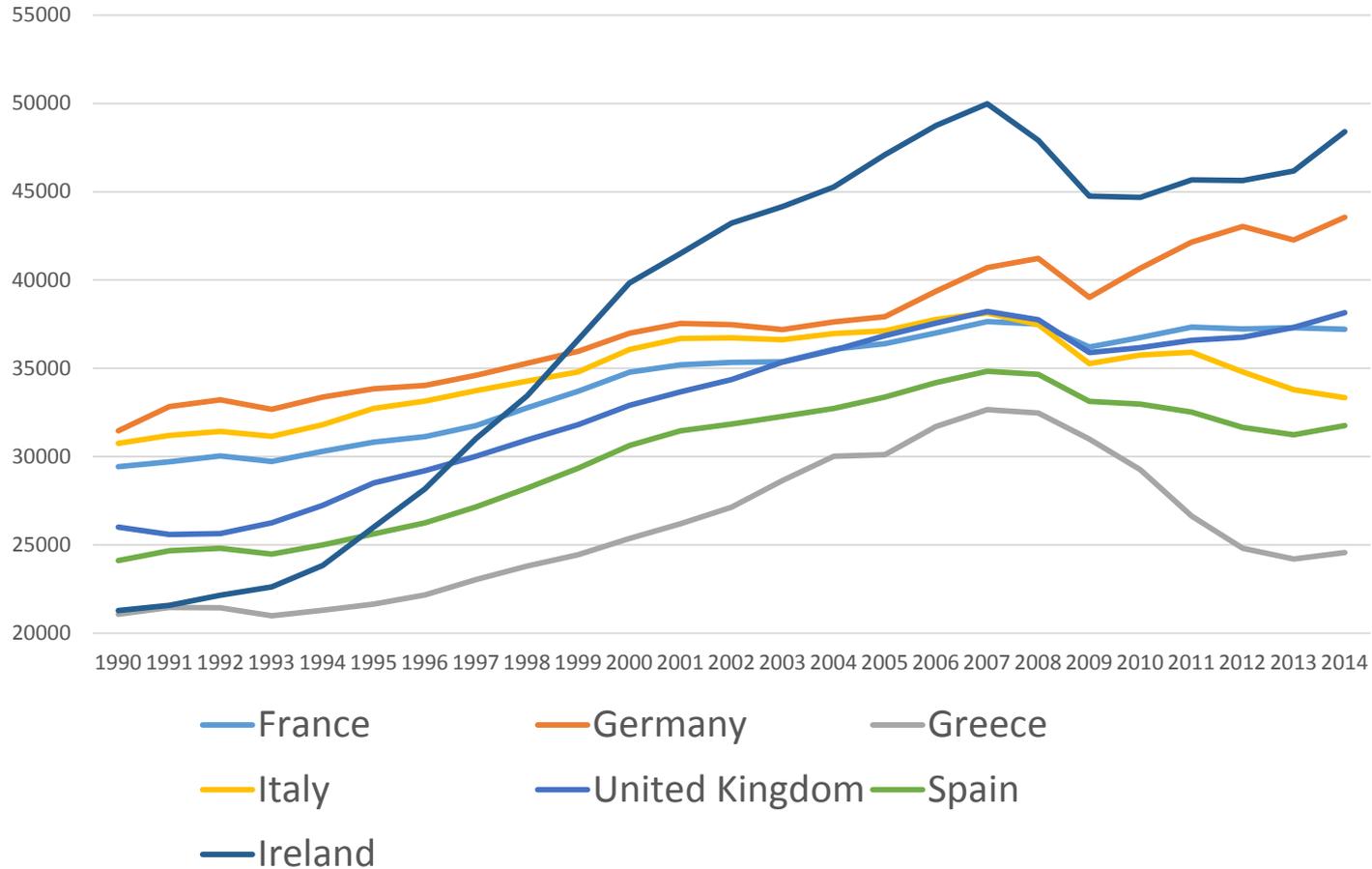


Source: World Bank



# European divergence

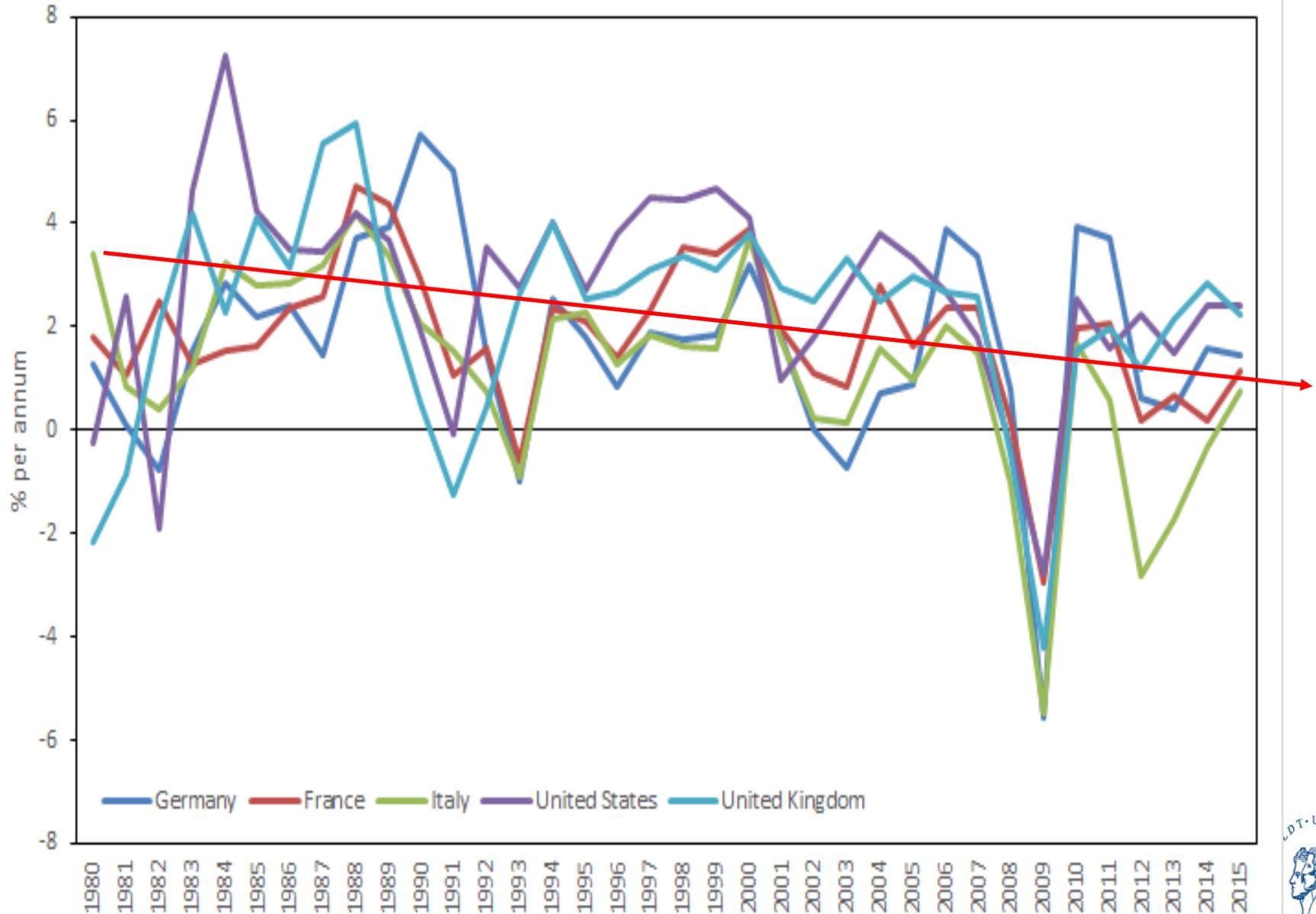
GDP per capita (levels), international dollars of 2011



Source: World Bank



# Per-capita-GDP growth 1980-2015



# The drivers of economic disintegration

## *Labor mobility under siege:*

- Complicated! Schengen was designed to encourage free movement of labor
- Germans shut out the Poles for 8 years, who then went to UK and Sweden instead
- But now, after more than a million refugees came to Germany many are questioning this policy – especially the Scandinavians
- The integration of Syrian refugees has proceeded very slowly

# The drivers of economic disintegration

## *Capital mobility in trouble:*

- The sovereign debt crisis in southern Europe and Ireland caused a reassessment of „joint liability“- many peripheral countries are candidates for transfers, which is politically unacceptable
- Capital flight from the crisis countries has made it worse
- European capital markets union a non-starter, unfortunately
- National resistance to foreign ownership of productive capital is becoming an issue for populists (ghost of the past!)

# The drivers of economic disintegration

## *Trade:*

- The European sovereign debt crisis led to a general decline in trade
- Voices of protectionism are getting louder – TTIP is dead
- The exit of the UK will increase pressure on continental European politicians to follow suit
- Terrorist attacks as in France Belgium and elsewhere hurt free trade indirectly

# The drivers of economic disintegration

## *Convergence of institutions and policy:*

- The Euro-Sovereign debt crisis left many southern European countries indebted and hamstrung
- Facts: Government budget surplus (consolidated), **2014** (% of GDP)

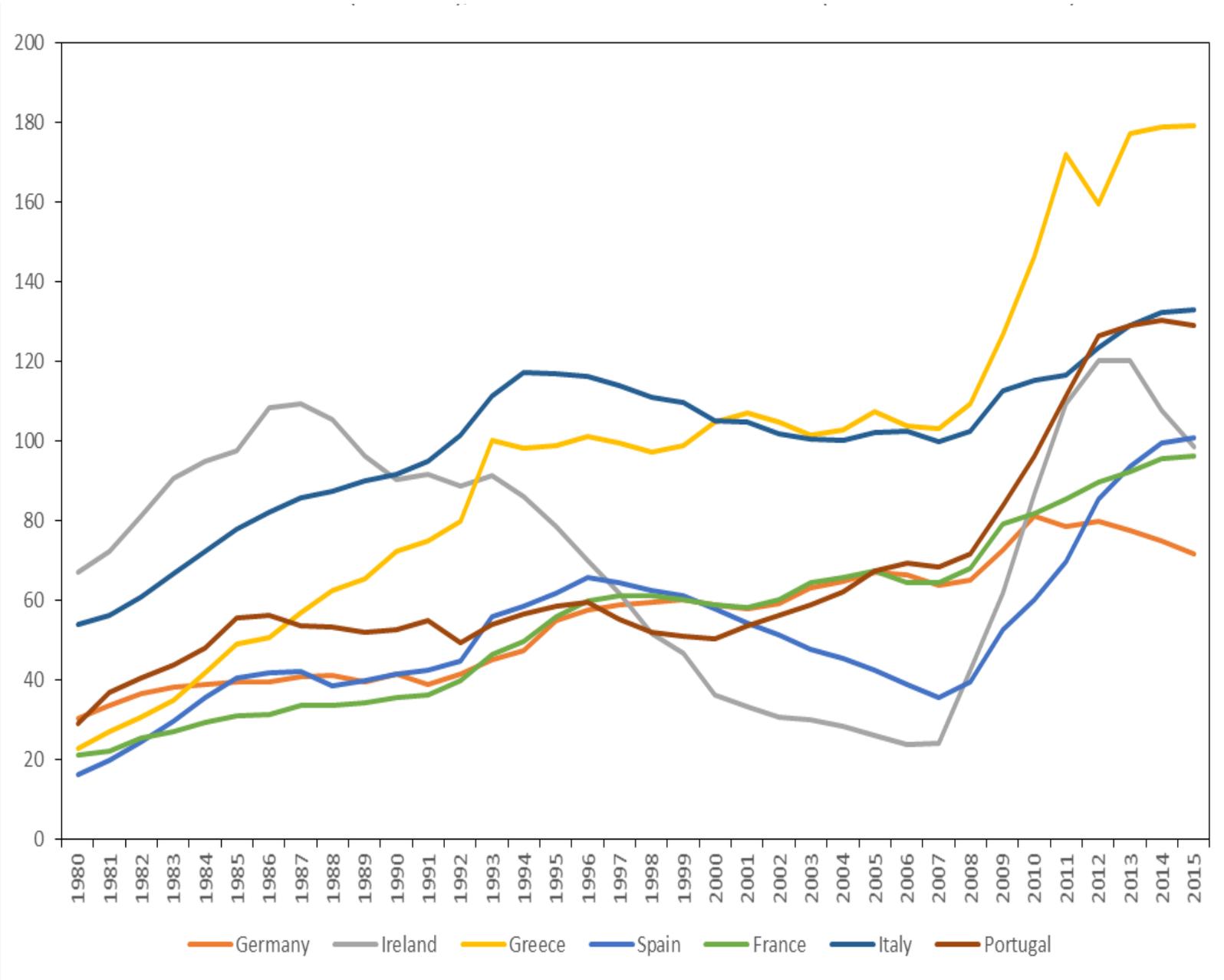
Country	Overall surplus	Interest expense	Primary surplus	Debt
D	0,3	1,4	1,7	74,0
F	-3,9	2,0	-1,9	95,6
PL	-3,3	1,9	-1,4	51,6
GR	-3,9	3,9	0,0	178,4
IRL	-3,9	3,5	-0,4	107,5

Source: IW Köln



# Sovereign debt, Euro countries (ESA95 Basis)

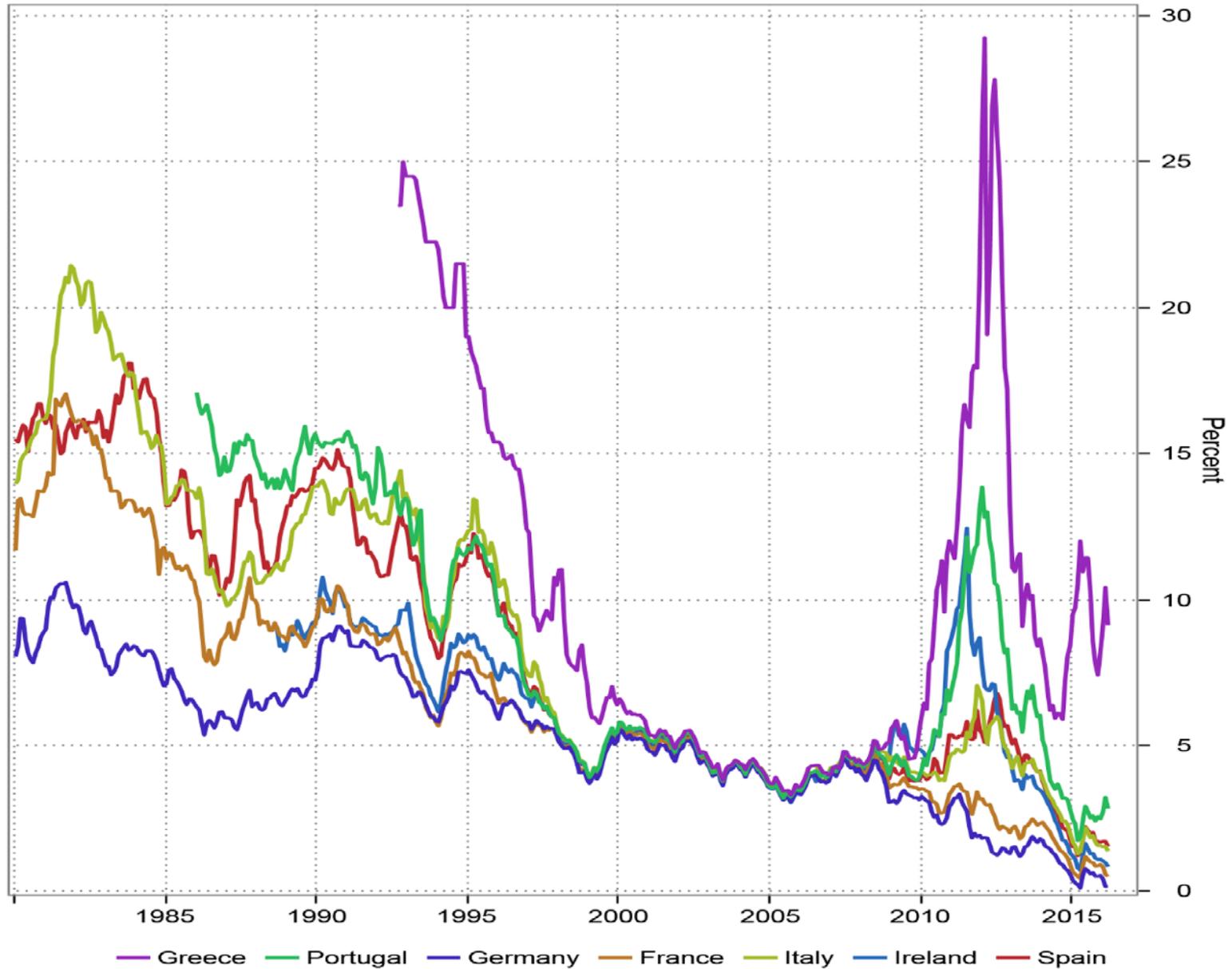
% of GDP, 1990-2015



# Yields on sovereign debt, Euro countries

10 year bonds, % p.a., 1990-2016

Government Benchmarks, Eurostat, Government Bond, 10 Year, Yield





# The Ghosts of European Past

- The title of this talk comes from European history
- Since Roman times, European integration has come in cycles – rising and falling tides of centrifugal and centripetal forces
- We are possibly experiencing the end of a grand cycle of opening, world trade, enlightenment and political integration
- Which ghosts?

# A house of horrors

- The ghost of the *Grandes Alliances* - „Europe of multiple speeds“ – involving coalitions concerned with national interests, european solidarity or regional concerns...
- The ghost of tribal go-it-alone: A European house of horrors with an erosion of consensus of solidarity, European ideals, and peace on the continent...
- The ghost of the „strong man“ – kings, emperors, extreme nationalism, national socialism, fascism, and communism

# Solutions?

- These ghosts are perennial European classics!
- Lacking the ability to redistribute the gains from globalization, Europe needs more growth, especially productivity growth
- But how do that when the whole world is slowing down?
- Europe needs a project – common defense, external borders, infrastructure program, educational excellence
- But Europe also needs to focus on local democratic forces – bottom up, based on common European values

# Solutions?

- There is a generalized lack of patriotism among Europeans – no feeling that the EU represents a positive force their daily lives
- This is a pity, because there is much to be proud of and to promote
- Junkers: Infrastructure? Education? Erasmus?
- Maybe it would be smarter to go halfway with the Britons – concessions might save a very important trading relationship
- It might even be worth sacrificing one of the vaunted „Four Freedoms“ as the price of saving the (priceless) customs union

# Conclusion

- The motto of the European Union?  
*„In varietate concordia“* („united in diversity“)
- It is time for Europeans to step up to the plate and respect and honor these values...
- ...with subsidiarity and autonomy for member nations...
- ...and with a new EU constitution that enshrines European principles of diversity, tolerance, and respect for human rights.
- Insisting on the advantages of durable peace, open exchange of goods and ideas is essential for exorcising the ghosts of the European past.

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