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If Not Now, Then When?

Using Europe 2020 to Move from Crisis Management to Restoring Confidence and Growth

By Ann Mettler

Ann Mettler is executive director of the Lisbon Council.

'Greece Passes Tough Austerity Measures,' 'Spain and Portugal Accelerate Cuts,' 'Debt-Heavy Rome Reins in Spendthrift Regions,' 'German Plan for Heavy Cuts Sets Example for EU,' 'France Poised to Raise Retirement Age'

For all the Europe-bashing in recent months, with markets jittery about unsustainable sovereign debt and lagging competitiveness in large parts of the European Union, it is tempting to overlook that real and profound changes are underway.[1] The headlines above would have been unimaginable as little as half a year ago. For sure, the Greek crisis could not have come at a more inopportune moment, with Europe crawling out of recession and trying to restore fragile growth.[2] But it is likely that history will remember this as the moment when Europe finally mustered the courage to confront the unsustainable nature that lies at the heart of its societal model in the absence of reform; when it learned that past performance is not a free ride for future prosperity; when it experienced the limits of a state that had taken on more and more obligations over the decades without making adequate provisions on how to pay for them down the road. Many countries across Europe are now learning the hard way that if you don't reform during the good times, you have to do it during the bad times. Undoubtedly, there are many today who wish that they had taken the Lisbon Agenda, Europe's reform programme of the past decade, more seriously and had acted earlier on the many warning shots that had been fired from Brussels and elsewhere.

This moment of truth must not be squandered for it represents the first – and perhaps the last – opportunity in many years not only to bring about cosmetic, superficial changes in a member state here and there, but also to launch a paradigmatic change in how Europe operates, how it conducts its business and how it will lay the foundation for future growth and prosperity. Against this backdrop, it is deeply disturbing that Europe's leaders increasingly come across as perennial crisis managers who excessively focus on short-term remedies to problems that have built up over many years, if not decades. Even though ostensibly the first two European Councils of 2010 (the Informal European Council of 11 February and the spring European Council of 25-26

1. The author would like to thank Paul Hofheinz and Stéphanie Lepczynski of the Lisbon Council for their comments on and editorial assistance with an early draft of this e-brief. As always, any errors of fact or judgment are the sole responsibility of the author.

2. Alessandro Leipold, "Preventing Greek Tragedy from Becoming a Eurozone Disaster: Lessons from IMF Crisis Lending – and the Challenges Ahead," Lisbon Council e-brief 06/2010.

> ‘Recent months have demonstrated that the key driver of structural reform is the threat of state default and loss of economic sovereignty.’

March) should have been devoted to Europe 2020, the EU’s blueprint for future-oriented policy making and smarter, greener and more inclusive growth, the reality is that this important agenda was cast aside to produce make-shift pledges of support for Greece which in reality shattered market confidence and ultimately did nothing to prevent the need for a subsequent bail-out which was agreed only weeks later, on 02 May 2010. And while some countries did take important first steps in getting a grip on their public finances, austerity packages alone are too simplistic a response to the profound challenges awaiting these countries. For the truth is that simply cutting expenditure or raising taxes is no convincing recipe for sustaining prosperity in the long run, nor are they the way to lay the foundations for future growth. If anything, this should be a time of investment – investment in areas that we know are crucial to future success, such as education, innovation, science, information and communication technologies, as well as the larger transformation of the state itself, which after all accounts for 40-50% of gross domestic product in most EU member states.

Public Finances Will Be Europe’s Driver of Structural Reform

Recent months have demonstrated that the key driver of structural reform is the threat of state default and loss of economic sovereignty. In that sense, having Greece as a real life example of what economic experts had hitherto only been able to forecast to happen sometime in the distant future was a healthy wake-up call. It has spurred unprecedented precautionary action across the EU and has finally removed the treacherous “safety valve” of piling up ever greater debt in order to spare the public from “cuts” they were told would be painful, when in reality the postponement of reforms only exponentially increased the overall pain and cowardly shifted responsibility to a future government or the next generation. In reality, what today is called “austerity” is perhaps nothing more than at last making an effort to live within our means – which in the case of Greece will nonetheless lead to an overall rise of debt to GDP level from 113% in 2009 to 150% in 2014, despite the massive austerity package and related €110 billion bailout for the country.[3] The second key driver of structural reform is the insistence of German Chancellor Angela Merkel – pushed through at the spring European Council 2010 – that any rescue package involve the International Monetary Fund. Even though her decision has been sharply criticised, it turned out that it was the prospect of losing economic sovereignty to an institution that is recognised for playing hard ball (unlike the European Union, which to date never had the courage to punish violations of the Stability and Growth Pact) and being unrelenting in its demands for conditionality, that would kick-start member states into action. No one fancies repeating the humiliating Greek experience and any cost of an action imposed today pales in comparison to the alternative, namely an EU/IMF-led bailout with stringent conditionality requirements.

3. Kerin Hope, “EU Puts Positive Spin on Greek Rescue,” *Financial Times*, 02 May 2010.

‘Implementing austerity measures and negotiating an economic governance framework will in and of itself do nothing to spur growth, innovation and employment.’

Observing what so clearly works today goes a long way to explain what so clearly did not work in the past. Taking the Lisbon Agenda as an example, it is now obvious why it could never be the driver of structural reform that many had hoped it would be. For one, the agenda was for all practical purposes de-coupled from public finances, apart from its (unfulfilled) plea to spend 3% of GDP on research and development. Secondly, it had no teeth. Compare the Open Method of Coordination, a harmless peer review that usually elicits neither media attention nor public interest, to the threat of having to invite the IMF to vet your books, examine the quality of your public coffers and monitor progress in implementing reforms.

These lessons of the real drivers behind structural reform – the threat of sovereign default and loss of economic sovereignty – need to become part and parcel of EU policy making henceforth, meaning this approach should become a pillar of the economic governance that European leaders are contemplating and will present at the June and October European Councils, as well as a hallmark of the Europe 2020 strategy.

Do We Still Need a Europe 2020 Strategy?

Knowing that the EU’s reform programmes – whether it’s the Lisbon Agenda or the new Europe 2020 strategy – do not have the political gravitas to drive forward structural reform, do we need them in the first place?[4] The answer is of course yes, because implementing austerity measures and negotiating an economic governance framework will in and of itself do nothing to spur growth, innovation and employment. This is why the Europe 2020 programme should be positioned and perceived as an important accompanying policy process that will help political leaders, as well as the public at large, to focus on a medium- to long-term development strategy. In addition, it has the potential to go a long way to reassuring the investment community and global partners that Europe has an actionable and credible plan for its future, and is capable of breaking out of its institutional naval gazing, which most recently started with the Lisbon Treaty and is now continuing in discussions over economic governance, as well as its perennial crisis mode, which has overshadowed and unilaterally dominated recent European Council meetings. By themselves, these actions do nothing to create a dynamic business environment, an efficient and well-functioning state or a world-class innovation and education system, all of which are prerequisites for future growth, employment and prosperity.

The fact that the Europe 2020 strategy – despite being announced with much fanfare last autumn – has even less of a profile and public recognition than the Lisbon Agenda is an embarrassment for the European Commission, as well as the member states. Such a timid and modest start for what is supposed to be a flagship of the Barroso II Commission, as well as European Council President Herman van Rompuy,

4. For more on the Europe 2020 proposals, visit Europe 2020 – A New Economic Strategy on the European Commission’s website.

> **'Hard-hitting future-oriented policy prescriptions and convincing strategic guidance could go a long way to refocus attention on the larger transformation of the European economy.'**

neither instills confidence nor demonstrates that our leadership is prepared to assume the opportunity presented by the beginning of a new decade in the midst of such a profound crisis. In fairness, both President Barroso and President van Rompuy are ultimately dependent on EU member states to support and agree on Europe 2020, but it is unlikely that the member states will raise their game if they feel so little energy coming from Brussels, particularly at a moment when national leaders are all distracted by the crisis and face difficulty focusing on anything other than domestic austerity packages and interest group battles. Hard-hitting future-oriented policy prescriptions and convincing strategic guidance could go a long way to refocus attention on the larger transformation of the European economy that must occur before sustainable growth can resume, employment levels be increased and credibility in the global economy be restored.

For sure, the time to kick-start a strong and lasting policy blueprint in the form of Europe 2020 is running out. Two opportunities, namely European Councils that should have enacted Europe 2020, have already been squandered. While individual flagship programmes of Europe 2020, such as the Digital Agenda, are moving forward, they are largely doing so without being formulated and positioned in the larger policy framework for which Europe 2020 was established in the first place. As such, these policy initiatives appear as *ad hoc*, uncoordinated and isolated, rather than as important components of a larger strategy aimed to prepare Europe's economy for the future.

In order to regain the initiative and demonstrate to Europe and the world that the EU can play offense, and not only defense, the following 10 urgent steps must be taken:

1) Use the June European Council to Make a Public and Lasting Commitment to the Europe 2020 Agenda

If the EU will assemble its entire leadership once again merely to respond to market pressures with yet more bailout or austerity plans – or succumb to the temptation to sell greater coordination as a credible recovery strategy – the summit will fail to restore confidence, calm markets or give the impression that our leadership knows how to handle this crisis.

2) Realise that Greater Coordination and Economic Governance Will Not be the Drivers of Growth

Much of the recent debates in Brussels about the need for economic governance – some even go so far as to call it economic government – are strangely reminiscent of the past haggling over the Lisbon Treaty. At the end of the day, it's more about the distribution of power between Brussels and the member states, as well as the creation of new institutions (i.e. a permanent secretariat for the Eurogroup or the creation of a European Monetary Fund) than

‘Our leaders do a real disservice to their citizens if they use populist rhetoric and easy excuses, for it only makes it harder to accept the necessary changes.’

5. Standard & Poor’s, *Global Graying: Aging Societies and Sovereign Ratings* (27 June 2006).

about the substance itself, namely Europe’s anemic growth prospects, high unemployment, unsustainable social security systems, lack of future-oriented strategies and lagging global competitiveness. Europe must break out of the cycle of endless internal deliberations, which granted are important but are not an end in and of themselves.

3) Don’t Blame the Crisis and Subsequent Reforms on Markets and Speculators Alone

Without a doubt, the global financial crisis accelerated and exacerbated Europe’s recent economic woes but it is a grave mistake – as well as a gross misinterpretation of the facts – to maintain that markets and speculators are solely to blame.Europe’s problems are for the most part entirely home-grown and are the result of politically inept leadership which failed to reform countries during the good times, knowing fully well of the unsustainable nature of public finances, demographic outlook and economies that relied more on past glory than future-oriented investment and strategies. Despite the barrage of criticism of rating agencies, it was no other than Standard & Poor’s which published the following statement in 2006: “Certain continental European countries including France and Italy would post debt burdens well above 200% of GDP by 2050…The Czech Republic and Hungary could face net debt equivalent to more than 400% of their output by 2050, similar to levels in Portugal and Greece…The consequence of this hypothetical fiscal outcome would be inconsistent with the current high level of ratings on sovereigns... Using budget balance trends as empirical long-term proxies for sovereign creditworthiness, a collective slide down the ratings scale would commence early in the next decade. Its initial gentle decline would accelerate by 2015 and continue until the mid-2030s, by which time the vast majority of countries would display characteristics that today are associated with speculative-grade sovereigns.”[5]

And it was not only Standard & Poor’s that had these insights well before the financial crisis ever hit. Analysts and experts had been warning for years about the risk of excessive government debt and the threat of prospective insolvency. It is now time to finally take responsibility for our own actions – past and present – and not blame markets, speculators or globalisation (the previous scapegoat popular during the first decade of the 21st century) for our plight. Our leaders do a real disservice to their citizens if they use such populist rhetoric and easy excuses, for it only makes it harder to accept the necessary changes. Does anyone need to retire later because the market commands it or is it really because our social model needs to be made sustainable for our children and grandchildren? Do citizens want a more flexible labour market to appease speculators or can they be made to accept and understand that more dynamic systems have better social outcomes, both before and during the crisis (compare unemployment rates in the Netherlands and Denmark with those of Spain, for instance)?

'Greece is the most extreme case but across the EU, states are in urgent need of modernisation and reform.'

4) Modernise the State

One of the single biggest omissions in the current Europe 2020 strategy is the careful and no doubt purposeful omission of what in many member states is the single biggest part of the economy, namely the state. Apart from a few words on e-government, one would be hard pressed to find any reference to the larger issue of state transformation and reform. Seemingly oblivious to the fact that the crisis in Greece was largely triggered by an inefficient, overcommitted and bloated state – or that recent election campaigns in the United Kingdom and the Netherlands were dominated by the question of state reform – the Europe 2020 strategy will be rightfully marginalised if it fails to accompany member states in what is undoubtedly the single biggest challenge in the foreseeable future, namely how to cope with increased demand for public services at a moment when budgets are tight and states can no longer afford to be the drivers of growth and employment that they had hitherto been (See the box on State Transformation on Page 11 for more]. The Europe 2020 strategy, as it is conceived now, would have no answers or solutions to offer to a country like Greece, which does not first and foremost need targets for R&D, or greater commitment to "Digital Europe," or a "Youth on the Move" programme, but a wholesale reform of how the state operates and meets its commitments and obligations vis-à-vis its citizens. Granted, Greece is the most extreme case, but across the EU states are in urgent need of modernisation and reform. What is largely overlooked in the debate about the economic success of Scandinavia is the large contribution that an efficient, reform-oriented public sector has played. For instance, Greece has four times as many teachers as Finland, but with dramatically poorer educational outcomes.[6] So the question is not necessarily about "big" versus "small" but more about "quality" versus "quantity." In order to assess these questions, it will be imperative to create new benchmarks and performance indicators and allow for greater transparency in how governments work and operate, both areas where the EU could make profound and lasting contributions.[7]

5) The EU's Litmus Test: Financial Perspective after 2013

After a white paper on the next financial perspective that was launched in the final days of the Barroso I Commission was derided by the EU's biggest beneficiaries – regions and farmers – there has been a stunning silence surrounding the important issue of budgetary reform. Given that the EU budget is a topic that is no longer only about how money is spent, but is now of a much greater magnitude, which threatens the overall credibility of the European Union, it urgently needs to be put back on the political agenda. Political leaders never seem to tire of speaking of the importance of innovation, growth, employment and sustainability – but in the same breath they will staunchly defend that the lion's share of the EU's budget be allocated to agriculture – a pre-industrial sector accounting for some 1.6% of the European economy and some 4.7% of EU jobs (2.8% in the EU-15).[8]

6. David Gardner, "Nation With a Pantheon of Problems," *Financial Times*, 15 May 2010.

7. For an excellent discussion of state transformation and public-sector innovation, see forthcoming Christian Bason, *Leading Public-Sector Innovation: Co-Creating for a Better Society*, (Bristol: Policy Press, 2010).

8. Eurostat, *Statistics in Focus*, 18/2010.

‘If the next financial perspective will closely resemble the last one, the EU should drop its pretense of wanting to be an “Innovation Union” and instead rename itself the “Agro Union.”’

This kind of political inconsistency used to be mildly annoying and confusing, but against the severity of the economic crisis in Europe, it is now downright irresponsible and actively undermines the EU’s global credibility.[9] And it makes the EU itself come across as a hostage to pressure groups, in violation of the interests of the broad population which would like to see the money going towards growth and employment[10]. If the next financial perspective will closely resemble the last one, i.e. with the lion’s share going to agriculture, the EU should drop its pretense of wanting to be an “Innovation Union” and instead rename itself the “Agro Union”, which would be more suitable given the fact that agriculture would then remain the overwhelming political priority of the EU, judging from the way it spends its money. A political priority which is not a budgetary priority is not a political priority, no matter how much our leaders try to convince themselves otherwise. Allocating some €25 million to the newly established European Institute of Technology, set up to supposedly rival the world-class Massachusetts Institute of Technology, while channeling €40 billion a year into agriculture, speaks for itself and of Europe’s true priorities.

6) From Subsidies to Strategic Investment

Along with the need to shift priorities in the EU budget should come a new understanding of what financial resources are for. Should they be permanent financial allocations, making entire sectors of the economy permanently dependent on politically motivated handouts, rather than focusing on building up competitive enterprises that strive to deliver better quality to the consumers they serve? Should they be permanent life support for lagging regions, which are financially incentivised to sustain their status because any rise in performance would threaten to cut off the money supply from Brussels? With enormous pressures on public budgets across the EU, including in Brussels, there is an urgent need to redesign financial assistance programmes from an emphasis on subsidies to an emphasis on strategic and smart investments. These strategic investments should be made where a good return can be expected – be it in growth, employment, innovation – and should be of limited duration in order not to breed dependency and foster political patronage.[11] The focus on strategic investments should be accompanied by a larger debate about quality of public finances. There is a real risk that in the midst of Europe’s austerity drive, political leaders only focus on cutting expenditure, rather than shifting, even raising, expenditure in areas that will be critical to stimulate growth, such as innovation, education and research. In an effort to focus the public discussion on quality of public finances, governments, the European Commission and other pertinent bodies, such as the OECD, should spearhead a drive to bring complete transparency to government finances, so that citizens can see first-hand how much is spent on key budgetary items, such as debt servicing, defense, social expenditure, infrastructure, and education.[12]

9. See forthcoming Philippe Legrain, *The CAP Post-2013* (Brussels: The Lisbon Council, fall 2010).

10; According to a 2008 Eurobarometer survey, 38% and 36% of respondents wanted the EU budget to be spent on economic growth and employment and social affairs respectively. Only 14% wanted the EU budget to be spent on agriculture and rural development. European Commission, *Standard Eurobarometer 70: Public Opinion in the European Union* (December 2008).

11. German Economics Minister Rainer Brüderle recently announced that subsidies should be paid for a limited time only and should not be extended indefinitely. Die Welt, *“Steinkohle – Brüderle will an die Subventionen,”* 06 June 2010.

12. Ann Mettler, *Innovating Indicators: Choosing the Right Targets for Europe 2020* (Brussels: The Lisbon Council, 2009).

‘The overriding priority must be to change the narrative and demonstrate that Europe and the member states can pro-actively shape and develop policy agendas.’

7) Kick-Start Confidence Measures at EU Level

In addition to austerity measures, there is an urgent need to demonstrate that additional action is taken in key areas that are considered ripe for reform and further development. These include but are not limited to: completion and strengthening of the internal market,[13] particularly in energy, services and ICT/digital products and services; reforming the EU budget towards future-oriented priorities and growth- and employment-generating areas; demonstrating commitment to global trade, for instance by breathing new life into the Doha Development round; continued support for building a low-carbon economy in the run-up to the Cancun UNFCCC; supporting and assisting member states’ efforts to reform labour markets; and accompanying the larger process of state transformation that will occur in coming years, making the transformation a European issue, not only a national one. There are countless other areas that need urgent attention but the overriding priority must be to change the narrative and demonstrate that Europe and the member states can pro-actively shape and develop policy agendas rather than only formulate rushed and defensive responses in reaction to their own shortcomings, be it lax fiscal management, stalled reforms or overstretched and overcommitted states.

8) Build on European Synergies and the Value-Added of Integration

In times of stretched budgets and Europe’s shrinking share in the global economy, does it really make sense to have 27 national energy markets, research policies, telecommunication regimes, etc? While in all of these areas, there is a European dimension and moves to streamline policies with the aim of greater integration, it is fair to say that we are far from having a truly European response. While the Lisbon Agenda very much counted on reviews of national strategies, with the aim to highlight best practices, the Europe 2020 strategy should focus more on articulating and implementing European governance systems and policy strategies to drive forward key policy areas that are known to be important for growth and employment: energy, innovation, research, ICT, education, skills, etc. So rather than admiring the high level of R&D in Sweden and Finland and using it as an example of best practice, are there binding European strategies that can be developed to pro-actively help national policies to converge, build on European synergies and raise everyone’s performance and standards of excellence? Such moves would signal a fundamental shift in the governance structure in Europe 2020, from a non-binding focus on exchange of national best practices (in the old Lisbon Agenda) to binding, Europe-wide policy responses in key areas that have hitherto been the exclusive domain of member states.[14] For sure, such a profound shift in governance would present a quantum leap but one that would signal that this time around Europe is ready to embrace a modernisation and reform agenda that is worthy of the name. For more, see Chart 1: Acting Together Pays Off on Page 9.

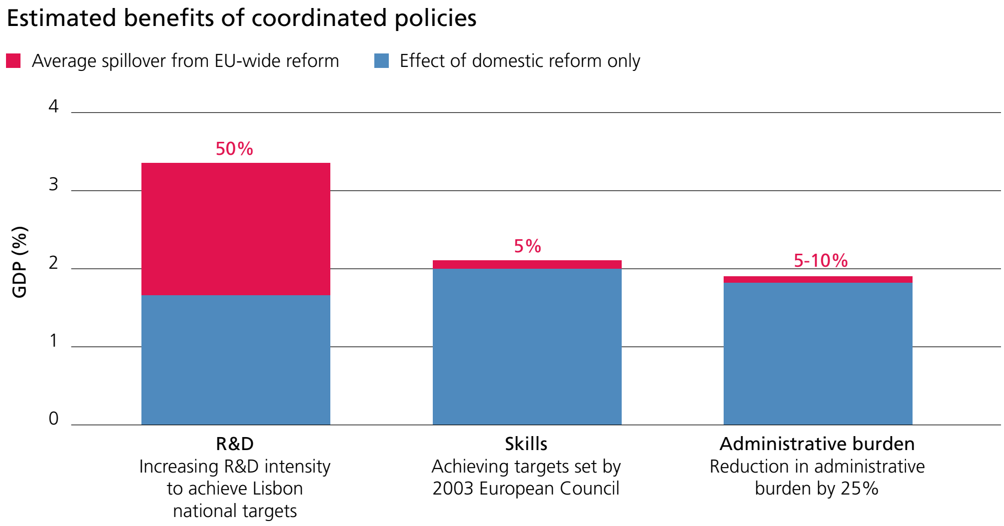
13. Mario Monti, *A New Strategy for the Single Market: At the Service of Europe’s Economy and Society* (Brussels: Report to the President of the European Commission, May 2009).

14. A proponent of a greater “community” approach to the Europe 2020 strategy versus the previous intergovernmental approach is Guy Verhofstadt, leader of the liberal group in the European Parliament. He argues that if Europe 2020 applies the same governance structure as the previous Lisbon Agenda, it is doomed to fail. Euractiv, *“Parliament Threatens to Block ‘Europe 2020’ Plan,”* 07 June 2010.

'Given Europe's demographic outlook – coupled with a state of public finances which will place unprecedented burdens on future tax payers – it is long overdue to highlight the need for greater sustainability.'

15. For a good review of how young people expect to interact with government, see Anthony D. Williams, *Wikinomics and the Era of Openness: European Innovation at a Crossroads* (Brussels: The Lisbon Council, 2010).

Chart 1: Acting Together Pays Off



Model simulations show that there are important benefits of undertaking structural reforms in a coordinated manner: R&D policy spillovers can range between 20 to 50% of the overall impact; for other reforms spillovers account for 5 to 10%.

Source: European Commission

9) Make Intergenerational Equity and Fairness a New Social Paradigm

The traditional and well-established and organised tension in European society is between capital and labour, with both sides boasting well-known arguments, organised interest groups and permanent institutional arrangements. This tension is certainly still present and deserves to be continued and fostered. However, alongside we are witnessing a new emerging tension between the generations, which is much less understood, for all practical purposes not organised and has no institutional foundation which could serve as a platform to highlight the cause or facilitate medium- and long-term solutions. Given Europe's demographic outlook – coupled with a state of public finances which will place unprecedented burdens on future tax payers – it is long overdue to highlight the need for greater sustainability and responsibility in all areas of governance, particularly with regard to future-oriented investment (i.e. education, innovation and more); overall government debt and future debt servicing; outlook and durability of social security systems, particularly pensions; labour market policies which currently lead to an unemployment rate among young people that is twice as high as among the general population; and a larger reinvention of the state itself, which a generation of "digital natives" will expect to become more user-centric, interactive and agile in meeting citizens' needs.[15]

‘No one seems to be prepared to take the political heat one is inevitably confronted with when trying to bring about change and reform.’

16. Lorenzo Bini Smaghi, "Saving the Young from the Burden of Pensions," *Financial Times*, 17 October 2006.

10) Good Reforms are About Persuasion, Not Coercion: New Voices are Needed

Many of the traditional pressure groups have failed to stop – or even raise attention – to the irresponsible handling of public finances in recent decades and have not been able to lend the popular support that would have been necessary for our political establishment to drive forward the necessary reforms. And political leaders themselves, even though well aware of the unsustainable nature of public finances and social security systems, have for the most part proven utterly inept at either acknowledging these facts or having the political stamina to see reforms through. With the benefit of hindsight, one can draw two conclusions: our political classes will not tell citizens the truth about future challenges and the current set of interest representatives will not either. No one seems to be prepared to take the political heat one is inevitably confronted with when trying to bring about change and reform. This sad fact leads to a style of governing and governance in which change can hardly ever be pro-actively initiated at an early stage, when negative externalities could be limited and overall damage contained. Instead – as seen in the aftermath of the fallout over the Greek crisis – action is usually only taken when it is almost too late, when all alternatives have been exhausted and political room to maneuver is at a minimum. That is neither a mature style of governing for advanced democracies, nor does it bode well for the future, when problems of the kind we are experiencing today will exponentially increase in view of Europe's declining importance in the global economy, its extraordinarily challenging demographic outlook and its declining trend growth. The task at hand now is to identify and build up voices which can warn of future dangers, much like environmental groups raised alarm bells for years before climate change and global warming became hot-button political issues. In the absence of recognising and empowering new interest groups which could facilitate a better, more informed exchange about future challenges, another option could be to enshrine fiscal discipline in national and EU policy, so that today's efforts to make public finances sustainable cannot be reversed once the immediate urgency for austerity is over. This could be modeled for instance after the German "debt break", or *Schuldenbremse*, a constitutional provision the German government imposed last year which forces the government to limit its debts to a maximum of 0.35% of GDP. Another proposal comes from Lorenzo Bini-Smaghi, member of the European Central Bank's executive board, who already in 2006 proposed the establishment of independent commissions in EU member states, charged with setting a retirement age that guarantees intergenerational equality.[16] Decisions by these bodies would be shielded from political interference – by being modeled after central banks – and would be taken on the basis of available scientific data on demographics and life expectancy. Enshrining provisions to ensure fiscal sustainability in constitutions or creating new independent bodies would go a long way to restoring Europe's battered credibility, for it would demonstrate that there is a long-term, binding commitment to sound public finances.

> 'Enshrining provisions to ensure fiscal sustainability in constitutions or creating new independent bodies would go a long way to restoring Europe's battered credibility.'

This is necessary because there still seems to be an underlying assumption that things can go back to "normal" – i.e. that the reckless handling of public finances can continue once the immediate crisis is over and markets have calmed down. Not only is this not an option but political leaders should for once have the courage to say so.

Europe is at a Crossroads

The coming months will decide if Europe can regain the momentum and act pro-actively to shape its future, or whether we will continue to be on-call crisis managers, frantically trying to fix past mistakes and cobble up make-shift solutions to calm the markets for a few days. The verdict is still out on whether Europe 2020 will suffer the fate of its predecessor, the Lisbon Agenda, or whether it can be an actionable, useful and widely accepted policy blueprint for a sustainable, inclusive and smart future. Despite Europe 2020's low-key start, it is not too late to signal to European citizens and the world at large that the EU is still in business, capable of reform and embraces the once-in-a-generation opportunity for transformative change that the current moment provides.

Experiencing the Limits of the State is a Sobering Process

Political leaders are using the crisis to finally drive forward the need for greater fiscal sustainability. However, they remain remarkably silent and timid about the underlying problems that have gotten us into this situation in the first place, as well as the long-term challenges awaiting us. While it is convenient to blame the crisis on speculators and the inability of banks to manage risk, the truth is that for years prior to the events unfolding in 2008 and 2009, analysts had warned that many European countries had no underlying economic growth model which could sustain their large state nor their comparatively high standard of living. The difficulty now is that at exactly the moment when governments could really make a contribution to restoring growth by spending more, we have run out of room to maneuver. Let the fact that the toughest austerity measures in Europe are spearheaded by socialist governments in Greece, Portugal and Spain, speak for itself. These are administrations that have neither the ideological conviction nor the historical track-record of implementing cuts to government expenditures. The fact that they are pursuing them nonetheless tells us a lot about the severity of the situation. We live in thriving democracies which in principle should offer political choices. But the power of democratically chosen governments to allocate and distribute resources has been dramatically reduced due to our irresponsible handling of public finances in previous years and decades. This is not an empowering moment, neither for governments nor their

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electorates, but it is something that the current generation of leaders was prepared to impose on future generations, burdening them with so much debt and a demographic problem to be reckoned with, that political room to maneuver would be reduced to a minimum. Perhaps if nothing else, this crisis forces us to treat the interests of future generations more seriously.

This crisis of confidence in the power of the state is understandably traumatic for Europeans. Unlike the United States with its deep belief in limited government, Europe has a proud tradition of a comprehensive and interventionist state. While there are nuances of support for government, there is a broad political and cultural consensus for a "European social model" that includes universal health care, minimum pension provisions, the fight against exclusion and poverty, etc. For generations of Europeans, a job with the state was desirable because it was considered "safe." While those in the private sector may have some fears about their future pension, people working for the state never doubted its ability to pay, either for salaries, benefits or pensions. The growing feeling that the state will not be able to meet its future obligations, particularly vis-à-vis those whom it employs and those who are dependent on it, i.e. pensioners, is a traumatic prospect which elicits widespread fear and anxiety – not to mention that it shatters firmly held beliefs and convictions. The European crisis of the state is perhaps the psychological equivalent of what Americans must have felt when "Wall Street capitalism" was shaken to its core in the aftermath of the financial crisis of 2008. It's not only an ostensible crisis, with rising unemployment and market turmoil, but something much larger – a crisis of confidence that challenges cultural mores and traditions.

Time for the State to Reinvent Itself and Come Clean with the People of Europe

The worst thing that can happen now would be that governments produce only two responses to the crisis: raising taxes and cutting expenditure. While both are likely outcomes, they are neither enough to produce new growth – in fact they are more likely to stifle it in the short-term – nor are they enough to give people a sense of purpose as a society or instill faith in the future. That is why it is imperative that the state reinvents itself, that it becomes a driver of change, a body that not only asks sacrifices of others but that is prepared to make them as well, an apparatus that is not attached to preserving itself but to serving its citizens. If the state will not manage this crisis responsibly, capable of imposing high standards of conduct on itself, demonstrating that the actions taken lead to more sustainable governance that citizens can once again trust, it will have

> ‘The difficulty now is that at exactly the moment when governments could really make a contribution to restoring growth by spending more, we have run out of room to maneuver.’

profound ramifications for the cohesion of European society. Citizens may no longer be willing to contribute to public pension funds if trust erodes that these will be sustainable over time; others may shirk taxes if they believe that public services are either too poor in quality or not available at all when they need them; young people may not want to work for the state because it is seen as a relic of the past, incapable of innovation and renewal.

How the state behaves in coming months and years will decide its future fate. And while it might be tempting for political leaders to continue the politics of deception, of telling citizens that their system can be sustained with only minor reforms necessary, they should instead use this moment to come clean with their citizenry and voters. The politics of truth must prevail. Citizens deserve to be told about future challenges, such as unsustainable pension obligations, so that they can make adequate and informed judgments as well as take actions today that can prevent crises tomorrow.

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