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International Spillover of EU Disintegration

The Western European message of the 1960s, 1970s, 1980s and 1990s was fairly clear: More regional economic integration and the building of joint institutions is good for the European Union and could serve as a model for other regions in the world economy that are interested in higher economic growth and more politico-economic stability. The ASEAN countries in Asia, the Mercosur countries in South America and many other regional integration schemes were interested in EU integration dynamics: A typical question raised at many international economic conferences was about what one could learn from Europe, and in several Asian countries leading universities offered master programs in “European Studies” which attracted many brilliant applicants from which the respective university could choose the best students. Since 2013/2014/2015 the situation has changed considerably: a much lower number of applications and students in this field clearly indicates that the attractiveness of EU integration dynamics has started to lose much of its previous shine.

The EU in 2008-2015 has indeed exhibited large inconsistencies and experienced policy pitfalls – its previous integration dynamics have been lost and it looks increasingly weak; it could even be on the way towards disintegration. What were the key problems in the EU?

- When the Transatlantic Banking Crisis emerged it took the European Parliament and national parliaments in major EU countries many years to sort out the problems and respond with major reforms – these reforms were so much slower in coming and so much weaker in practice than in the US that the delayed and lacking reaction explains much of the 10% growth gap vis-à-vis the US in 2008-2015: standing for an income gap of € 3000 per capita in the euro zone and the EU, respectively.
- When the Transatlantic Banking Crisis fully erupted in mid-September 2008 – with the collapse of the US investment bank Lehman Brothers – it was immediately clear that the international risk appetite of investors would dramatically shrink and that the first victims of this regime shift would be countries with high debt-GDP ratios and high deficit-GDP ratios and/or high foreign indebtedness. So this author wrote at the end of October, in the manuscript of a book on the banking crisis, about a scenario in which Greece, Spain and Italy could face a major refinancing crisis for sovereign debt (at that time I was not aware of the incredible problems in Ireland, i.e. the total absence of any serious prudential supervision and massive corruption, so that my book Transatlantische Bankenkrise/Transatlantic Banking Crisis had a small blind spot in terms of the description of the upcoming crisis in Europe).

- Under the weight of the banking crisis, the EU member countries decided – largely following British pressure – that the EU's government expenditures should be cut in a period of tightening budget constraints: from 1.24% of GDP to 1%, which is absolutely the wrong decision. While the US, a top political player, spends about 9% on federal government expenditures relative to GDP and another 11% on federal social security expenditures, the EU stands for almost nothing. This implies that the EU fiscal policy is largely inefficient and the IMF has argued that a 1% GDP reduction – a standard shock to the economy – will reduce the EU's consumption-GDP ratio by roughly three times as much as in the US. Part of this bad result is due to the homeopathic expenditure-GDP ratio in Brussels. Infrastructure expenditures and military expenditures plus short-term unemployment benefits should be financed via Brussels, in doing so the overall tax rate in the EU should reduce by about 1%. Political competition in the European elections would increase massively if the economic and political role of the EU could be reinforced: More intensive political competition – with a stronger European Parliament (and the Commission no longer playing a twin role as both legislative and executive body) – would reinforce the efficiency of the EU and the EU's spending of taxpayers' money. The role of radical small populist parties would be strongly reduced and this would bring more stability for Europe.
- As regards monetary union and the creation of a single EU currency, there is a lack of consistent rules and in this perspective there is the problem of a missing political union. The Eurozone could have major benefits – more than 0.5% of GDP - if the euro remains a strong international reserve currency. The enormous privilege of being a reserve currency is an important benefit of the dollar and the euro. If the euro countries are not willing to establish a political union, the Eurozone will disintegrate.
- If the EU or the Eurozone should disintegrate, there will be strong economic disadvantages and in Europe military expenditures relative to GDP would rise from about 1.5% of GDP to about 4% - as in the decade before World War I. The risk for economic and political stability and peace would be enormous. Other regional integration schemes in the world economy also could become rather unstable.
- The problems in the EU, and in Germany and France etc., could certainly be solved, but the current policy of merely muddling-through is poor – better concepts and more professional economic policy are urgently needed. If the EU should disintegrate, this would stimulate the disintegration of regional integration clubs worldwide and thus contribute to international economic instability.

The EU has only a few short years remaining to sort out its problems. So far, the German government – under Chancellor Merkel – has not given many impulses for a strong Europe, rather the poor political management of the refugee wave of 2015 and the euro crisis have served only to destabilize the EU further. The TTIP project (EU-US regional economic integration) offers new prospects for higher economic growth, but again the political management in the EU is rather weak. In a period in which the US political attention increasingly is focusing on Asia – this reduces the relative weight of EU-US economic cooperation – a successful TTIP project would be a crucial for element for better EU-US cooperation.

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