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TO EXIT OR NOT TO EXIT (FROM THE EMU)?

ABSTRACT

We discuss the main alternatives open to the Union, from its break-up to exit of some countries and radical changes in its institutional set-up. The pros and the cons of a possible exit are thus assessed with respect to these alternatives. The prospect of political and institutional changes that reinforce the existing structure, in particular with reference to solutions for overcoming its democratic deficit, are finally outlined.

Keywords: Monetary Union, Exit, Institutions, Democratic Governance
JEL Classification: E42, F00

RIASSUNTO

Uscire o non uscire (dall'UME)?

In questo lavoro discutiamo le principali alternative aperte all'Unione, che vanno dalla sua disintegrazione all'uscita di alcuni paesi e all'introduzione di cambiamenti radicali nelle sue istituzioni. È così possibile valutare gli aspetti favorevoli e quelli contrari all'uscita alla luce di queste alternative. Si delineano infine le prospettive dei mutamenti istituzionali e politici necessari per rafforzare la struttura esistente, in particolare con riferimento alle soluzioni capaci di superare il deficit democratico esistente.

1. INTRODUCTION

In the worst days of the Greek crisis, the exit of this country, possibly followed by others, was a likely prospect. By contrast with the diffuse skepticism of the 1990s, after the first decade of functioning of the EMU optimistic views prevailed also among economists. Eichengreen (2010a), in a paper originally written before the Great recession, suggested that the rumors of some years earlier about the possibility of one or more members of the Euro Area leaving it in the next ten years were largely unfounded and that its break up was even more unlikely.

However, Nordvig (2014) rightly speaks of a (premature) celebration, as the fathers of the Euro did not realize that the shaky institutional foundations of the Euro Area would soon lead to sustained 'homegrown' instability. The crisis soon showed the sad reality and skepticism came back. In fact, after 2009, numerous authors, policymakers or political parties have advocated exit of peripheral countries from the monetary union, especially as an effect of the policies implemented in order to tame the crisis. A debate on the various prospects open – and, in particular, of the pros and cons for exit, together with the discussion of the different ways to implement it – has then arisen, involving economists, politologists, political parties and laymen. After a few years, populism and nationalism seem to suggest again a similar issue or – at least – the prospect of a different structure of the EMU. These political waves contribute to reduce the enthusiasm for the introduction of the euro of the first decade on the occasion of the celebrations for its second decade.

We discuss the main alternatives in section 2. Radical changes in the structure of the EMU, including the possibility of its break up and the pros and the cons of a possible exit. Section 3 presents a summing up of the various solutions. Section 4 concludes, outlining the prospect of political and institutional changes that reinforce the existing structure, in particular with reference to solutions for overcoming its democratic deficit.

2. The main alternatives: a break up, exit of some countries, a many-speed Union, or structural reforms?

As an effect of negatively assessing not only the competitive position of some countries in the EMU, but also the performance of the whole Union, the prospect of a future crisis looming arises. Four possibilities are open: 1) a breakup of the Union; 2) exit of less competitive countries; 3) internal changes to the monetary union that take account of the different speed of the various countries; 4) adoption of structural reforms, particularly in peripheral countries. Let us deal with these different options in turn.

2.1. A *break-up*, even more than exit of one or a few countries, can occur in an orderly or a more or less chaotic way. A break up of the Union might derive from exit of a country (either a weak or a strong country), especially following a crisis of the kind of the Great Recession. This can cause

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a domino effect on others in a similar position that can practically be forced to follow the first country, by speculation or other factors. A break up was a rather likely outcome in the worst days of the Greek crisis, which could have reduced the Euro-area to a handful of countries.

To avoid the prospect of a chaotic break-up, plans must be prepared in advance, as we will say in more detail with reference to simple exit. This can explain the usefulness of discussing this topic also in the case of countries belonging to the core, not to the periphery, of the EMU[1]. Belke and Verheyen (2013) describe both the genesis of a doomsday scenario and its impact on domestic debt, the domestic banking sector, EU membership, the freedom of trade as well as the social and political costs of the social disorder that would follow.

2.2. *Exit* from the Euro-area of a less competitive country can be the result of a unilateral decision of one country. It can derive from some kind of speculative attack or be prepared in normal contingencies as a result of a reflection about its benefits and costs.

An automatic exit is suggested by Ritzen and Haas (2016), who, while criticizing the Five Presidents Report as based on unrealistic assumptions, suggest a New Deal between the highly indebted countries of the Euro Area and the other Euro Area countries. This would mutualize debt, but also lead to automatic exit in case of non-compliance with the agreed rules. Analysis of the pros and cons of exit, together with a discussion of the path to follow, is the object of the remaining part of this sub-section.

The Pros and the Cons of Exit

The difficulties in building the Euro-zone with the contribution of countries having different institutions and histories – or even countries that had been engaged in some cases in ferocious conflicts and wars – have been enormous. These differences certainly had an influence on the attempts to cope with the crisis. The different course of the crisis in the various countries, with a high price paid by the periphery in terms of GDP, employment and debt burden, has implied understandable requests of exit from the Euro-area. But doubts have also been raised as to its benefits and costs mainly with reference to the effects of exit on competitiveness and the path

[1] Exit of more competitive countries is in any way a possibility suggested by some authors and politicians.

that would follow from exit, given some crucial features of the economies of peripheral countries. We deal with both in turn[2].

Exit is advocated with many justifications. First, it has been argued that the economic advantages from participation to the monetary union have been meagre. Some authors have noted a negative impact of the financial crisis on the members of the Eurozone, due to fixed exchange rates, which tend to accentuate the negative effects of the crisis (Bohl *et al.*, 2016). In exiting, a country would regain control over monetary and fiscal policy and be freed of the constraints on their use deriving from the reduced inflation target, the SGP and the fiscal compact limiting it when being a member of the EMU. It would thus have the possibility to cope with asymmetric shocks and its specific problems, such as a high debt burden. In addition, by exiting it would (re)gain control also on the exchange rate as a way to improve its competitiveness. Countries no longer tied to the euro would adopt a flexible or fixed (but adjustable) exchange rate, allowing for a depreciation or a devaluation of their new currency (Feldstein, 2012)[3]. In fact, an increase in competitiveness would ensue from that, and the country would bridge the gap with Germany, which enjoys an advantage deriving from the undervaluation of its real exchange rate – of the order of about 20-24 per cent with respect to Italy (Sapir, 2017)[4]. According to this author, there is no other alternative open to France, Italy and Spain and permanence in the EMU would mean the death of the economy, due to impoverishment and deindustrialization. Bagnai *et al.*'s (2017) stochastic simulations show that, after some initial stress in terms of their balance of payments, appropriate countercyclical policy measures could make growth of Italy to resume in five years' time, 'at a reasonable pace', with lower unemployment and a reduced public debt-to-GDP ratio. Apart from the nominal adjustment channel, the persistence of real exchange rate misalignments would be reduced by an improvement in the quality of regulation and institutions.

Critics of exit remark that the relief deriving from exit would be of short duration, as the external depreciation would fuel wage and price inflation. The inflationary process could be so high as to have a negative impact on distribution and social cohesion, as happened in the past when

[2] These are different according to whether there is a 'disorderly' or an 'orderly' and consensual exit.
[3] Obviously, in the event of exit of a hard-currency country, the problems could be opposite.
[4] The order of magnitude of the devaluation is debated, as some authors think that it can be rather low, while others hold that it can reach a peak of 60 per cent, at least at the beginning. Obviously, it depends on a number of factors referred to the country involved, such as its financial and real exchanges reserves as well as the degree of overvaluation of its real exchange rate with respect to the rest of the EMU, the secrecy of preparation of exit and the time required for the new payment system to be implemented.

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national currencies were either tied by adjustable fixed exchange rates or not pegged at all as an effect of some international agreement (e.g., the EMS, especially before 1985-7 and after 1992, for the Italian lira)[5]. Moreover, Eichengreen (2010a) notes that a country would experience a significant rise in interest rate spreads and debt-servicing costs as an effect of its departure from the Euro Area. The public and private debt that are euro-denominated would increase in terms of the new local currency. Credits towards foreigners could instead appreciate in terms of the new currency. If the *lex monetae* – whereby a sovereign state can decide the currency of denomination of its debts – is called into question, there will be no such appreciation, unless the Collective Agreement Clause (CAC) is to be applied, which is the case for the majority of government bonds, as from 2017 on. In 2022 almost all these bonds will be under CAC, whereas almost none were at the end of 2013, which would imply a net loss of €381bn, assuming a 30% devaluation of the new currency (see Figure 1).

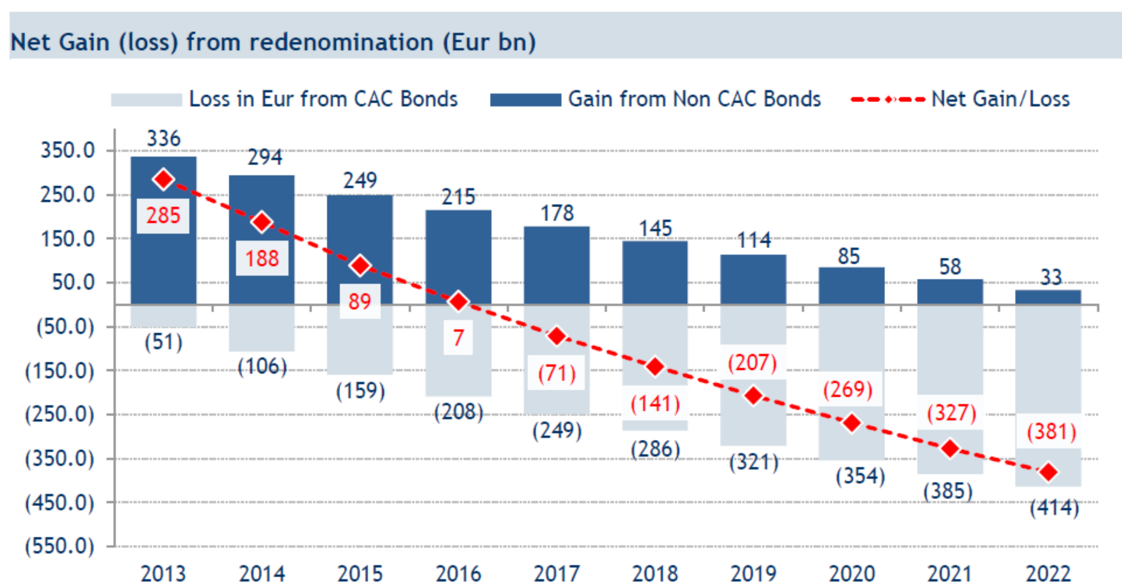
As to private debt, the prevailing interpretation is that it cannot be redenominated in the new currency, which would imply a loss related to the devaluation of the new currency. Most likely, it would be firms to be hit by this loss. The balance could then show that the costs from the devaluation would prevail. All in all, there could be a fall in GDP, which is estimated – possibly overestimated – as 40-50 per cent high by Deo *et al.* (2011), for the first year after exit. Even if this estimate is 'greatly exaggerated', various famous economists have written against exit (see, e.g., Feldstein, 2017).

Really, an analysis of the effects could be superficial and lead to prescriptions of a dubious foundation, if not complemented by a study of the determinants of the scarce competitiveness. Only the latter could indicate the true roots of imbalances and give advice on how to avoid them. These roots can originate not only in the low productivity profile (ascribable – in turn – to different growth models, private and public sector inefficiencies, and a different stage of development), but also in the austerity and stagnation imposed by the EMU institutions and policies, which act differently, given such diversity. To the latter determinant one should add the negative impact on resource allocation and productivity of the low real interest rates existing in the EMU as an effect of expansionary monetary policy after 2010, which has been found by

[5] In the case of Italy, it was only the extreme cooperative attitude of social partners that allowed putting a halt to depreciation.

Gopinath *et al.* (2015) and Cette *et al.* (2016)[6]. As one can see, there are cases of a low competitiveness endogenous to the participation of a country to the monetary union. Obviously, they would be removed in case of exit. Coping with factors of backwardness or slow growth of peripheral countries not endogenous to their participation to the EMU would entirely remain on the shoulders of the exiting country, which should weigh its chances to effectively steer its economy. After the exit in any case, use of available instruments for coping with low competitiveness will be effective only in the medium- long-term, which implies the need for the country to reduce the remaining short term negative effects, such as inflation, redistribution and unemployment.

FIGURE 1 - *Net Gains from CAC in Government Bonds*



Source: Guglielmi *et al.* (2017).

In addition to the pros and the cons of exit for the exiting country, an issue of the beneficial or costly consequences for the remaining countries arise. As an example, the latter would enjoy a benefit (cost) in terms of higher (in)stability, in case of exit of a peripheral (core) country. Most likely, all countries, those exiting and the remaining ones, would suffer from a financial turmoil,

[6] According to Gopinath *et al.*, firms with a higher net worth increase their capital in response to the decrease in the real interest rate, thus lowering their marginal productivity of capital, while more productive firms with lower net worth remain financially constrained. A lower sectoral fall in total factor productivity ensues.

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if the exiting countries are not small ones and if there is no preliminary agreement for exit[7].

Going to the path that peripheral economies would follow for the exit, one may first ask whether exit is the real target to pursue, given a positive balance of its benefits vs costs or whether it is simply a threat to other countries directed at pursuing other benefits through some kind of concession. If the latter is the case, the threat, even if not desired *per se*, should be credible. This requires in any case a favourable review of benefits and costs. In addition, exit should be carefully prepared. Many authors have noticed that it could be particularly disruptive, as speculative capital outflows would arise even before exit, due to expectations. This can even happen when simple fears of exit – not followed by it – arise in a country, as it happened after 2010. Bank failures could follow from capital outflows. Certainly, capital controls (notably, under the form of taxes on foreign capital) could be implemented, but one can doubt of their effectiveness when adopted by countries having an inefficient public administration and in an era where electronic money and transfers are available. In any case, capital controls have not only direct effects (i.e., those due to taxes), but also indirect effects that influence investors by signaling the likelihood of future policies, especially action that will negatively affect their investment[8].

The need for keeping secret plans for exit would thus arise and this way of implementing exit is advocated by many authors. However, it seems difficult to do this, not only for possible malfunctions in the administrative path to follow, but also because exit would imply complex accomplishments for converting means of payments from the euro to the new money. To reduce the associated costs it could be useful to prepare a kind of back-up domestic payment system,

'using as an argument the eminently sensible (and truthful) need for national economic security' (Malinen *et al.*, 2017: 14).

In addition, the possibility of capital flights and speculation arises, since financial integration is extensive and controls would be scarcely effective even in well-organised countries. An even more powerful argument against secrecy in the preparation of exit is the need for democratic

[7] In the case of the Euro Area it would be difficult to repeat the positive experience of the numerous cases of exit from currency unions, almost exclusively LDCs.
[8] These conclusions refer to cases of capital controls in a different political and economic environment as that of Brazil's tax on capital inflows implemented from 2006 to 2013. Thus, they can only be indicative of some indirect effects of such measures that are not easy to devise and assess.

control over government decisions by the Parliament, in addition to the need for informing the governments of other countries and the EA institutions. Thus, also counterarguments to secrecy are relevant or even more relevant than those in favour.

In addition to these possible outcomes, one should consider that exit from the monetary union might require exit from the EU. Some authors think it possible to exit only from the EMU, without this implying exit also from the EU (Marelli, Signorelli, 2017). Cooperation with European institutions, like the ECB, EBA and the European Commission is important in case of exit as it can decrease its costs, e.g., in terms of the extent and length of the capital controls and the costs of economic and political retaliation by other member countries (Malinen et al, 2017). If exit from the EMU also needs exit from the EU, an unclear and potentially complex process would be required (as the case of Brexit teaches us). In addition, exit from the EU is not really desired by some of those who favour exit from the Eurozone. Permanence in the EU, even in case of exit from the Eurozone, could be sought not only for political, but also for economic, considerations. Remaining only on the economic ground, Dreyer and Schmid (2016) empirically find positive effects on growth from the EU membership, but not from the Eurozone, during the first 15 years of the Euro.

2.3. Various forms of *differentiated integration* are already in existence or can be devised. They aim at introducing elements of flexibility that try to reconcile heterogeneity within the EU and may involve the EMU too. There are many classifications of differentiated integration, according to the principle inspiring them.

From the point of view of its pace, the main types of differentiated integration are: i) variable-geometry integration, which is already a reality now, as almost one third of the EU members have not joined the Euro Area and some of them do not take part to Schengen Agreements or to a series of intergovernmental agreements; ii) *à-la-carte* integration, such as the permanent right given to Denmark and the UK to remain outside the EMU; iii) multi-speed integration, such as provision of transition periods and temporary derogations from formally-accepted common objectives; iv) multi-speed integration with 'parallel currencies', such as a new drachma or a new lira. With specific reference to this latter type, a proposal of a two-speed EMU has also been suggested, starting from the consideration that a number of different euros circulate now in the Union. The two-speed union would acknowledge this situation, while ensuring stability to the

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Euro Area. Each country would reintroduce its former currency for its domestic payments and the euro could circulate as a truly international currency.

With respect to the primary law from which differentiation derives, two kinds of it have been indicated by Schimmelfennig, Winzen (2014): ‘instrumental’ and ‘constitutional’ differentiation. With the former, originating from the EU treaties, the new Member States are temporarily excluded from some policy areas, for two reasons: the fear by old members of some kind of competition from the new members or the (in)ability of the latter to meet some policy requirements.

Here we are interested in constitutional differentiation, originating from the revision of the EU treaties. It transfers new competences to the Union, thus ‘deepening’ the process of integration in some areas. This has already developed to some extent through the instrument of intergovernmental cooperation. The need for closer co-operation, but also for the policy differentiation that it can involve, first arose with the Treaty of Amsterdam in 1997, which introduced this kind of cooperation, a deliberate legitimatization of variable geometry.

Among the most relevant recent steps, we should mention:

- the Rome Declaration, signed by the leaders of 27 EU member states (absent the UK) on March 25, 2017, on the occasion of the 60th anniversary of the Common Market and the Rome Treaty, stating that they

‘will act together, at different paces and intensity where necessary, while moving in the same direction’ (European Commission, 2017);

- the agreement of June 2017 reached by the EU Council of Bruxelles to set up Permanent Structured Cooperation in defense;
- the proposal in September 2017 by the EU Commission President to create a EU minister of finance and economy as well as a EU monetary fund, by ‘graduating’ the existing European Stabilisation Mechanism.

Differentiated integration seems in any case to pursue different strategies for different countries. It is a pragmatic way to integration, which can really lead to widening the current differences. It could indeed turn into exit of some countries from the EMU, the topic of the next

sub-section. Independently of this prospect, it is a way to integration that negates the possibility of devising a common growth strategy.

2.4. The need for *reforms* in the EU derives from persisting structural divergences and aims, compounded by new divergences originating not so much from its enlargement, but mainly from the financial crisis.

Policies can be imagined that do not imply exit or the other alternatives indicated at the beginning of this section. The policy most favoured by some researchers and countries could derive from an internal devaluation strategy in peripheral countries, implying deflation of wages and prices. Apart from considerations of fairness, this might not be an easy way out, however. The simple prospect of price deflation would create a 'fundamental contradiction' that would make the internal devaluation strategy impossible or very hard to pursue. In fact, the more countries reduce wages and costs, the heavier their debt load inherited from the past becomes. And, as the debt burden becomes heavier, public spending must be cut further and taxes increased to service' the debt of the government. Banks can be in a situation similar to the government.

'This, in turn, creates the need for more internal devaluation, further heightening the debt burden, and so on, in a vicious spiral downward into depression' (Eichengreen, 2010b).

One way out would be debt haircut or restructuring of debt, e.g., conversion of bank debts into equity or their writing off, if banks are insolvent. Similar haircuts or restructuring or a prolongation of maturity might be necessary for public debt. However, also this route would not be an easy one. As an effect of such operations being implemented in a country, a contagion to other countries being in a similar position – or, by contrast, a flight to 'quality' or 'safety' – could ensue. While contagion is certainly dangerous, flight to quality would mainly benefit the country towards which investors direct their capital, by relieving its public debt financing. This country, however, could be endangered by the reduction of exports to the country experiencing a crisis.

Other policies could be devised that can, instead, consolidate the Union. Rather than deflationary policies by peripheral countries, expansionary ones could be implemented in core countries. In addition, fully implementing the banking union, enacting fiscal union and introducing Eurobonds or similar common financing instruments could help in avoiding exit or the other policy options mentioned at the beginning. All these policies would require the assent

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of core countries acting as hegemon or leaders. German leaders should convince their constituents that these policies can be in their longer-run interests. In fact, these could even be a premise to more cooperative policies, leading to a completion of the union and uniform and more rapid growth. In a similar way argues Rodrik (2015).

Finally, also structural policies should be considered. From the point of view of the latter, the EU Commission President, Jean-Claude Juncker, in September 2017 has proposed to double the EU budget for structural reforms, which appears to be a very promising prospect.

3. A SUMMING-UP

All countries should make a benefit-cost analysis, albeit a difficult one, in order to evaluate both the short- and long-run implications of any action (implementing structural reforms, exiting or staying within the union, implementing one or another policy, favouring or hampering other countries' action). In many cases, such an analysis would lead to a cooperative attitude. However, a main obstacle can arise. In fact, the short- and long-run costs and benefits deriving from the various alternatives are unevenly distributed. In many cases, the alternatives most profitable in the longer run imply also higher short run costs. In addition, costs and benefits are also unevenly distributed across the various sections of the constituency in each country. Time preferences of different people and, in any case, of each country's governing body are then different. This compounds the difficulty of finding a common position of the governing body in each country. Divergences in the positions within the EMU will thus emerge.

The opinions on the future of the Euro-zone widely differ. Gros (2017) is optimistic on the outlook of the European economy, as this appears to be exiting the crisis with fundamentals better than other countries, especially in terms of the debt/GDP ratio. By contrast, De Grauwe (2017) judges that a budgetary and political union in Europe would be needed, but are far away, since the willingness to move today in this direction is simply non-existent, which will continue to make the Eurozone a fragile institution. One could add that this prediction derives from the persistence of asymmetries and imbalances inside the Euro Area, which, together with weaker institutions and policies, could imply a sinking of the whole boat, due to the specific faults of its stern (i.e., peripheral countries).

4. For a democratic EMU not prone to country or sectional interests

An important preliminary clarification is needed about the meaning of the term *democratic* institution. Democracy can be seen from a 'collective' or an 'egalitarian' perspective. The former emphasizes the possibility for a people – in this case, the entire Euro Area constituency - to elect its governing institutions. The latter is less demanding, as it preserves self-government of countries, but also suggests integration of policies and accountability of international institutions. The EU is now only a union of peoples, which can become more democratic, even if it cannot become a democracy. If in the short run we can accept this position, it must be said that the dream of the founding fathers of Europe tended certainly more to the goal of a European people. This dream can require time, but it is important to have in mind some kind of path that can lead to its implementation.

The EU Commission has introduced a system of contacts with various stakeholders, trying to develop a method of consensus. However, this has involved mainly the élites and has not ensured the necessary transparency. Majone (2014) speaks of a kind of 'democratic default' in the Union, which arose over time, starting with the failure of the CAP, continuing with that of the Lisbon Strategy and ending with the misconduct of the EMU governing bodies in the prevention of, and response to, the financial crisis. Then the issue arises of how to combine democracy with other requirements of a heterogeneous Europe and the different positions and abilities of each country. Only from solutions respecting all these requirements can a viable and democratic Europe spring.

It must be said that responding to the demands of people and countries has become very difficult in Europe after the crisis, as this has implied a return of the primacy of narrow economic interests in the European governance, together with a good dose of confusion. In the words of De Wilde *et al.* (2016: 15), now

> 'different "Europes" are demanded by different people, in different settings, different countries and even by the same people at different times'.

In any case, democracy would require less involvement in policy decisions and in the ability to punish of unelected people, such as those governing the EU Commission and the ECB, and markets (De Grauwe, 2009). It is true that the European Parliament has some powers in

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nominating the European Commission, but this does not put these institutions in the same position as national parliaments and governments. De Grauwe (2009) notes:

'(w)hen the Commission starts an excessive deficit procedure which aims at forcing national governments to cut spending and/or increase taxes, it bears no political responsibility for these decisions. In fact, the national governments do. When these follow up on the Commission's procedure and cut spending and raise taxes they are the ones who will be judged by their national electorates, and who face the threat of being punished by the voters at home. In contrast, the European Commission at no time faces the prospect of being voted away. Thus from a political point of view, the European Commission, which initiates the control and sanctioning procedure of the SGP, lacks democratic legitimacy, because there is no mechanism to make the Commission accountable before an electorate for its actions.'[9]

De Grauwe (2011) says that

'(n)either the European Commission nor the other members of the Council face political sanctions for the measures they impose on one member country. The principle of "no taxation without representation" lies at the heart of democracy. The SGP has been an attempt to short-circuit this principle, by giving powers to individuals and institutions that do not face the political consequences of their actions. Such an attempt has to fail and happily so'.

As to the ECB, there are some differences with the status of other central banks, such as the Fed, that aggravate the democratic deficit of an institution that is independent from the democratic institutions of the government. Finally, as to markets, their power to punish, to favour or in any case to indicate directions to follow – also through the pressures that the financial markets exert on the EU governance – should be more decisively balanced by fiscal responsibility (on this see also Bénassy-Quéré *et al.*, 2016).

Also according to Schelkle, there are issues of democracy in the EU. In fact, against the position that has led to

'keeping politicization out' there are good arguments in favour of 'bringing politics back in', as this would 'halt growing apathy or outright hostility towards the emerging European polity' (Schelkle, 2006: 681)

[9] This can be partially tempered by the possibility of voting against some policies required by the Commission on the occasion of the EU Parliament polls.

or, at least, contribute to that. Schelkle's reasoning seems to be even more relevant facing the growing populism in European countries. To overcome apathy and populism also more transparency of the process leading to decisions is needed.

In sketching the lines of a democratic reform of Europe's institutions, some kind of 'deliberative supranationalism'[10] (at least in the transitional phase before a federation or the goal of a European people can be established) would be required in order to face conflicts between countries. In fact, both country and sectional (often conflicting) interests play now a relevant role in EU governance. Policymakers' personal preferences or the sectoral interests influencing them fill in the space between input participation by the people and output, in terms of policy effects in favour of people. This can be hindered by people's participation to governance, which can ensure transparency, accountability and inclusiveness, thus contributing to a better outcome (Schmidt, 2013). However, in the words of Nicoli (2017: 399), the EU misses the necessary 'convergence of identities'.

This generates a number of problems of governance in the Euro Area, which are at the root of the pains related to the crisis. In a nutshell, the missing 'convergence of identities' makes it difficult to build a federal entity[11]. Almost as a reflection of this, the Union

'is ... not equipped with a government, but with a series of partial powers' (Pisani-Ferry, 2014: 165)[12],

the ECB, the EU Commission, more or less powerful national governments, ... and markets. And the more recent steps for reforms have aggravated the deficit, by creating a number of intergovernmental bodies and strengthening the role of the Eurogroup, the Economic and Social Committee and, in some cases, the European Council. As to country interests, one case may be of particular significance:

[10] This is the application of the concept of deliberative democracy to the EU case. Deliberative democracy holds that a democratic decision is legitimate, if it is preceded by authentic deliberation, not merely the aggregation of preferences obtained by voting, keeping aside the distortions deriving from unequal political power deriving from economic wealth or the support of interest groups.
[11] Absence of a convergence of European identities is documented by Alesina *et al.* (2017: 206), even before the financial crisis, as most Europeans '*became prouder of their national identities*' between 1980 and 2009. In the absence of this convergence, '*the EU risks facing the emergence of a dysfunctional system, hostage of minority blockages in national or even regional parliaments and characterised by recurrent instability on the financial markets. Ultimately, such sub-optimal solutions may not be sustainable and also may end up provoking the collapse of the EMU*' (Nicoli, 2017: 401).
[12] According to Pisani-Ferry, Europe, is '*reminiscent of Blaise Pascal's definition of the universe: "a sphere whose centre is everywhere*": (Pisany-Ferry, 2014: 166), except, perhaps – we can add – under the command of a European people.

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‘(w)hile EMU’s domestic demand-led models are forced to pursue painful austerity measures that have reduced inflation and increased unemployment, no attempt has been made to correct the excessive levels of wage moderation in the EMU north, specifically Germany, which undermined the periphery’s lack of competitiveness in the euro’s first decade. The result of the EU’s policy response, which has been shaped in the shadow of German hierarchy, has been to establish an asymmetric low-growth equilibrium within Europe that exclusively penalizes its southern rim’ (Johnston and Regan, 2016: 333).

The different size of countries and the asymmetry of power between ‘creditor’ and ‘debtor’ countries in the management of the Euro Area crisis as well as the ongoing institutional reform process of EMU have brought the issue of German dominance in Europe back to the forefront of scholarly debate. Germany has pursued the interests of its savers by shifting on debtor countries the burden of adjustment deriving from the financial crisis, as is clear from the policies imposed on Greece. Also in the case of the policies to relieve the Euro Area from the ensuing recession, the Bundesbank and, to some extent, the German government have pushed against unconventional policies, expansionary fiscal policy and rising inflation, in order to protect the interests of German savers. In this circumstance, the ECB has taken a firm position, favoured by its independence. However, this situation is no longer tolerable and a more balanced governance should be implemented. Creating a common finance minister for the whole Euro Area could to some extent increase the coordination of macroeconomic policies, even if institutional issues would arise. One of these refers to the powers of such a minister and the goals to pursue. In our opinion, this minister should have, in addition to the general task of better coordinating country policies, the authority to declare the existence of the exceptional circumstances that allow the possibility to make available to member states some flexibility in their budget policies. Alternatively, a Fiscal Council could be charged with the task (see more in Pisani-Ferry, 2014), but it should be reminded that such a Council should not have the task to undertake decisions that in their essence are of a political nature.

Some steps for pursuing not only economic and political goals, but also democratic accountability and effective governance over the next years are indicated in the paper recently prepared by the EU Commission (see EU Commission, 2017). It covers issues such as banking and capital markets unification, economic and social convergence, preparation of the new Multiannual financial framework, the fiscal stabilization function, in addition to those of accountability and effective governance. There are different projects for the periods 2017-2019

and 2020-2025.

Cramme and Binzer Hobolt (2015) call for proper solutions to the democratic deficit of the EU[13]. The situation could be improved by implementing some minimal rules, such as more transparency about the motivations and effects of decisions, with specific reference to the categories of people that would benefit and those that would be hit. Hix (2015) suggests a range of reforms oscillating between a minimalist and a maximalist perspective. To exemplify, let us refer first to governing bodies. The European Commission could be elected either indirectly via the European Parliament or directly by the EU citizens. As to the ECB, in confirming its independence one can think of subjecting it to oversight, either by the EU Parliament and the EuroGroup and/or also by national parliaments of member countries. Finally, bailout funds and austerity programs can be subject to approval and scrutiny by national parliaments or referendums ratifying them.

A solution to the democratic deficit would thus require not only a change in the orientation and the modes of current decisions, but also and mainly a radical change in the institutional setting of the EMU (Pisani-Ferry, 2014). This would be difficult to implement in the absence of a process of

're-envisioning of the EU's socio-economic policy, ... in concert with the people, through pluralist processes, and by the representatives of the people at both national and EU level, through more politics ... In addition to the political and economic reforms, ... the EU needs to re-envision its identity and change its decision rules ... [in particular] by eliminating the unanimity rule' (Schmidt, 2009: 38).

Alesina *et al.* (2017: 207) also suggest searching for institutions in charge of European policymaking in a way that can make them accountable and

'accelerate the formation of European identities and the emergence of a European (as opposed to national) public forum, where European policy issues are discussed in a European perspective'.

A democratic state must respect the will of its citizens, but also be efficient. From this point of view, a number of reforms of the Euro Area are also in order. A number or reforms are suggested

[13] Moravcsik (2002) finds little evidence in favour of the existence of a democratic deficit in a comparative perspective. Only the ECB looks like somewhat departing from the case of other countries, but this is justified by its position of particularly pronounced independence. However, the warning by Follesdal and Hix (2006) about the need for more democracy is still valid at present, even after some small improvements.

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in Acocella (2020: chapters 8-11) from which we have also drawn some pages for this article. From a methodological point of view, a starting point is offered by existing institutions, in the process to changing them in the directions we have traced. Key elements can be reinvigorating the Broad Economic Policy Guidelines and the framework that guides economic policy. Horn and Watt (2017) suggest also to extend the EU Macroeconomic Dialogue, in particular by setting up meetings at the Euro Area level, by involving the Eurogroup, the peak European social partner organisations, and – at the level of Member States – the participation of national central banks, fiscal authorities and national social partners.

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