

Asan Special Lecture Series

“European Union and the Eurozone Crisis”

Guy Sorman

Economist, Philosopher, noted Author

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The Asan Institute for Policy Studies

Dr. Guy Sorman, celebrated French economist and philosopher, presented the *Asan Special Lecture* titled “**European Union and Eurozone Crisis**” on July 12, 2012 at the Asan Institute for Policy Studies. Dr. Sorman highlighted the European Union’s successes and failures across its 60 years of development and proposed solutions for how to adapt to the new world economy. He remains optimistic about its future, stating that it represents more than just economic and political cooperation, but a new identity for Europe as a whole.

How fragile is the European Union?

The foundation of the European Union (EU) was built 60 years ago at a time of extremely high growth in Europe. At that time, competition from emerging markets was extremely low and the EU’s institutions were not designed to handle it. In the years since, fierce competition has emerged and a failure to adapt has resulted in crisis. This crisis is not just of economics and finance, but one that seems to threaten the very Union itself.

It is largely believed outside of Europe that the EU reflects merely economic and political integration, but what is misunderstood is that for many of its citizens it reflects a new identity. Many identify themselves as European before their own nationality, which is less tangible but still important evidence of the EU’s strength. Furthermore, there are a great many countries such as Poland, Turkey, the Ukraine, Belarus and others which are actively seeking to join the Union. This is evidence of its future viability. The UK, which may soon leave the Union, stands as an exception to this rule. But Dr. Sorman feels this will help distill the EU’s committed core rather than irreparably fracture its membership.

Finally, an examination of debt yields some dissonance in the perceived fragility of the EU and its member states. Belgium has large amounts of debt but it is not disparaged in the same way as Greece and Italy. Similarly, comparisons with the US reveal comparable levels of debt and growth, yet the United States is perceived as being much more stable.

Institutional reform and the way forward

The European Union and Eurozone face a great many problems, but the solution is to focus on the right problem. Dr. Sorman identifies the obsolescence of the EU's institutions as the true cause of the crisis. First among them are the strong welfare systems built by several countries during past periods of high growth. In 1974, recession nearly broke the welfare states but the governments opted for deficit spending in place of reform, leaving their flaws in place. At the time, low competition and the relative ease of borrowing allowed such a strategy to work, but recently the market has grown more volatile. Many emerging markets have ceased buying bonds from European states, creating a debt crunch.

The second institutional failure is European aversion to unregulated markets. Emerging markets can now out-compete Europe by creating higher quality products at a lower cost, partially because their markets are less regulated. Indeed, the most labor-regulated countries in Europe are those with the highest unemployment. Countries such as Austria, Germany, and the Netherlands deregulated parts of their economies in the 1980s and have weathered the crisis much better, but there is still more to be done to fully adapt them to the new global system.

Finally, there remains the issue of those countries with crippling high interest rates on borrowing. They are the result of accumulated debt from 30 years of bad policy. The solution, then, is to fix the bad policies by deregulating labor markets and scaling back welfare states. Dr. Sorman sees a growing consensus among governments towards taking this path, giving him cause for optimism that EU countries can reduce their deficits and bring capital back to private investment.

The beneficiaries of the European system remain an obstacle. When French President Nicholas Sarkozy changed the retirement age to 62, France, "nearly had a revolution." This resistance comes from a lack of understanding and the failure of governments to adequately explain why reform is necessary. Furthermore, certain political parties seek to exploit popular

dissatisfaction. While these parties remain on the fringe, they disrupt the path toward a rational solution.

The costs and benefits of EU membership

It is often proposed that the EU's implementation of a common currency without proper economic coordination was foolish. Dr. Sorman contends that there actually was coordination. For example, each nation was expected to keep a deficit limit set at 3% of GDP. This rule went ignored and a lack of an oversight authority prevented enforcement. The new system will be designed to prevent abuse in the future. This new system consists of a central bank that will support banks in countries that obey the deficit limit as long as they follow transparency rules. It will employ sanctions and incentives, create a treasury system within five years, and issue Euro bonds in the place of individual bonds.

These changes will not fix the problem of rich countries paying for poor countries, which Sorman views as the price to pay for being in the EU. In return, the Union guarantees for its members peace, welfare, and prosperity. Peace remains the number one priority for its member countries, which until recently were in a state of seemingly constant war with each other. In this respect the EU has been remarkably successful, creating an atmosphere in which citizens can no longer imagine going to war with their neighbors. It has also brought trade and open borders. As each member joins it receives support from the wealthier members. Sorman describes this as all part of the contract, and that bailouts are also an important part of the agreement.

A brighter outlook for the EU's future

The crisis today is not significantly different from crises in the past. Sorman dismisses the Euro's detractors who claim it is doomed, asserting that if that were the case a collapse would have already happened. While it's true the Euro has lost a significant amount of its value over the last 2 years, one cannot ignore the fact that the market continues to buy Euros. He predicts that the EU will be very different in the near future – the admission of new members such as Turkey and the withdrawal of old ones such as the UK. The new financial institutions being developed in response to the current crisis will make the future EU more stable and help provide responsible government. He concludes that these changes are the best solution to the crisis, and that they are indeed what the people want.