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Taking back control of globalisation: Sovereignty through European integration

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There has been a backlash against globalisation and international cooperation in recent years[2]. In Europe, Brexit and Euroscepticism have challenged the notion of the European Union (EU) as a political construct based on shared sovereignty, freedom of movement across borders and economic integration under a common legislative framework. In the United States, meanwhile, the benefits of free trade have been openly called into question. Europe was generally believed to be under the greatest threat from this trend. Even if the United States were to retreat from globalisation, that would not undermine the integrity of the country itself. In the case of Europe, however, the EU and the commitment to shared values and an open society are in many ways inseparable.

More recently, stronger growth and falling unemployment have supported an improvement in attitudes towards the EU. According to the latest Eurobarometer survey,[3] seven out of ten Europeans now regard themselves as citizens of the EU – the highest level ever recorded for this indicator. What is more, three out of four euro area citizens now support the euro – the highest level since 2004. Meanwhile, an increasing number of Europeans are optimistic about the future of the EU, and the percentage of respondents who regard the EU as "a place of stability in a troubled world" now stands at 71% – up 5 percentage points since 2016.

We need to take advantage of this opportunity and help Europe to make further progress. If we do not, the European project could end up at risk again sooner or later. The reason for acting is obvious: people's basic fears about the risks of openness have not really receded. Improved economic prospects can help to soothe such worries, but they will resurface in difficult times. Still, the EU can provide a lasting answer to those fears. Indeed, just as the EU is under threat from the backlash against globalisation, it can provide a way to manage globalisation. This is, after all, not the first time that globalisation has been on trial: the period between the First and Second World Wars showed that unregulated global markets are liable to descend into protectionism and nationalism. The lesson here is that cross-border integration is only sustainable if it is regulated and organised by institutions that safeguard the stability of the economic and financial system, ensure a level playing field, settle disputes and contribute to solidarity among members. This is what the EU gives to the people of Europe: a way of sustaining an open international order while also bending its outcomes to their will.

TAKING CONCERNS ABOUT GLOBALISATION SERIOUSLY

There are four basic reasons why people in Europe and beyond are worried about globalisation and open markets.

The first concern relates to stability – i.e. the question of whether globalisation has made countries more vulnerable to harmful spillovers from abroad and to international crises. This applies in areas such as agriculture, medicines and biotechnology, but it is perhaps much more visible in the case of international capital flows (i.e. financial globalisation). From the Asian financial crisis of the late 1990s to the global financial crisis of the late 2000s and the euro area sovereign debt crisis of the early 2010s, international financial integration has consistently triggered and amplified

1. Chopin, T. and Foucher M. (eds.), Schuman Report on Europe, State of the Union 2018, Editions Marie B, coll. "Lignes de repères", 2018

2. I would like to thank Jean-François Jamet, Jonathan Yiangou and Sander Tordoir for their contributions to this article. I remain solely responsible for the opinions contained herein.

3. See Standard Eurobarometer 88, which was carried out by the European Commission between 5 and 19 November 2017.

shocks. Indeed, between 1945 and 1980 an average of one in a hundred countries worldwide experienced a banking crisis in any given year, while between 1980 and 2008 – a period in which international financial integration increased considerably – the equivalent figure was one in five.[4]

The second concern is about fairness – i.e. the question of whether all countries abide by the same rules and standards. This is evident at global level in relation to accusations of currency manipulation or dumping practices, or in fears of a "race to the bottom" in terms of environmental and social standards. Similar worries have emerged within Europe in relation to free movement of people and posted workers.

The third concern relates to inequality. Many people believe that open markets have favoured capitalists and the rich at the expense of workers and the poor. Global value chains (i.e. supply chains spread across a number of countries) are thought to have reduced workers' bargaining power. There is also empirical evidence that financial globalisation has been associated with increases in income inequality within individual countries.[5] OECD data show that the labour compensation of the bottom 99% of earners, measured as a fraction of national income, has declined over the last 20 years in rich countries, while the labour compensation of the top 1%, measured as a fraction of national income, has increased by 20%.[6] Likewise, global integration has made it easier for companies and individuals to avoid taxation by exploiting international loopholes. Corporate tax bases have been eroded owing to transfer prices within value chains, and tax competition between countries has led to a race to the bottom in terms of tax rates.[7] A debate is currently raging between economists as to whether all of the unequal gains resulting from international trade can be addressed using social transfers, or whether changes need to be made to the rules of the global game.[8] However, all would agree that the revenue which has been lost as a result of tax avoidance and tax optimisation would have helped governments to at least mitigate the adverse distributional effects of globalisation.[9]

Finally, the fourth concern is about democracy. Many people are concerned as to whether the open market is truly subject to democratic control. As international markets extend further beyond the borders of nation states, it becomes less clear who governs them. Some people fear that openness has resulted in elected authorities ceding sovereignty to international investors or multinational corporations – e.g. via investor-state dispute settlement mechanisms. International cooperation between elected governments has been rekindled following the global financial crisis (particularly in the context of the G20), but beyond efforts to tackle immediate crises, the effective remit of such cooperation has largely been confined to financial regulation (and, more recently, tax cooperation). Even in the presence of clear structures allowing democratic control (as in the case of the EU), some politicians have succeeded in suggesting that those structures are too remote from the lives of voters and successfully played on the idea of taking back control by promising to repatriate powers to the national level.

Some of these concerns are based more on perception than on fact. For example, increased sensitivity to financial shocks and widening income gaps could be attributable to a number of other factors, including technological change,[10] and the two processes are increasingly interrelated.[11] Still, just as it is important not to overreact to criticism of globalisation, it is equally important to retain a sense of humility – to acknowledge that globalisation raises profound questions about fairness, stability, equity and democracy, which need to be properly debated and, where necessary, answered by means of effective public policies.

REGAINING SOVEREIGNTY

Some suggest that the solution is to withdraw within national borders. This option is destined to fail for two reasons. First, it deprives people of the economic advantages that trade and integration bring. According to one estimate, the EU's GDP per capita would be as much as one-fifth lower if no integration had taken place since 1950.[12] More than 30 million jobs in the EU (i.e. a total of one in seven) are dependent on exports to the rest of the world.[13] Second, the act of renationalising policies will not allow a country to evade global competition: isolating itself from global

4. See Reinhart, C. and Rogoff, K. (2009), This Time Is Different: Eight Centuries of Financial Folly, Princeton University Press.

5. See Jaumotte, F. et al. (2013), "Rising Income Inequality: Technology, or Trade and Financial Globalization?", IMF Economic Review, Vol. 61(2), pp. 271-309.

6. See OECD (2012), Employment Outlook 2012.

7. See Devereux, M. et al. (2008), "Do countries compete over corporate tax rates?", Journal of Public Economics, Vol. 92(5-6), pp. 1210-1235.

8. The former represents a textbook view of international trade, whereby gains from trade are unevenly distributed (e.g. between skilled and unskilled workers) but can be fully equalised by means of lump sum transfers. For an example of the latter view, see Rodrik, D. (2017), "Too late to compensate free trade's losers", Project Syndicate, 11 April.

9. See also Bourguignon, F. (2016), "Inequality and Globalization", Foreign Affairs, January/February, pp. 11-15.

10. See Jaumotte, F. et al. (2013), op. cit.

11. See Baldwin, R. (2016), The Great Convergence: Information Technology and the New Globalization, Belknap Press: An Imprint of Harvard University Press.

12. See Badinger, H. (2005), "Growth Effects of Economic Integration: Evidence from the EU Member States", Review of World Economics, Vol. 141, No 1, pp. 50-78.

13. See Rueda-Cantuche, J.M. and Sousa, N. (2016), "EU Exports to the World: Overview of Effects on Employment and Income", DG Trade Chief Economist Notes, Issue 1, European Commission, February.

value chains will raise input prices, make its exports less competitive and make the country less attractive to investors, ultimately weakening the economy on both the supply and the demand side. Similarly, retreating from international cooperation will not allow a country to escape tax competition and is likely to make it less effective at fighting tax evasion.

History suggests that there is only one solution. Whenever globalisation has led to excesses and retreated into protectionism in the past, the lesson we have learned is that globalisation is not sustainable without strong institutions. The United Nations and its offspring (such as the International Monetary Fund (IMF), the World Bank and the General Agreement on Tariffs and Trade) were a direct response to the descent into protectionism that was observed during the interwar years. Similarly, the G5 was born of the 1970s oil crisis, while the G20 was born of the Asian financial crisis in the 1990s and was given a new role in safeguarding world trade and strengthening the global financial architecture in the aftermath of the collapse of Lehman Brothers. However, by far the most advanced and successful political construct in terms of managing globalisation has been the European Union.

The EU's founding fathers devised a means of collectively managing the challenges thrown up by open markets without retreating behind national borders. They gave its Member States a unique platform for recovering some of the state functions that had been eroded by globalisation. Rather than having to choose between openness and sovereignty, sharing sovereignty within European institutions has allowed countries to regain sovereignty.[14] In other words, the EU provides a regional answer to the "political trilemma" popularised by economist Dani Rodrik,[15] according to which it is not possible to pursue democracy, national sovereignty and global economic integration at the same time.

This is not to say that the EU is perfect. The multiple crises that it has faced in recent years highlighted many issues that need to be addressed in terms of its effectiveness and its legitimacy. However, the EU has sustained an open order across the European continent for over 60 years. Since 1960, cumulative growth in real GDP per capita has been one-third higher in western Europe than in the United States. Europe has also accumulated greater wealth as a percentage of annual income than the United States (more than 500%, compared with 400% on the other side of the Atlantic).[16] At the same time, it has also demonstrated greater awareness of sustainability concerns – e.g. through its leading role in brokering international agreements on climate change in the context of the UN, from the Kyoto Protocol to the Paris Agreement. Thus, where pitfalls are encountered, we should not seek to unravel the EU and its many achievements, but strive to build better political institutions at European level that directly address the concerns of EU citizens and deliver the kind of managed globalisation that they desire, on the basis of the four considerations detailed above.

RECONCILING ECONOMIC INTEGRATION WITH FAIRNESS

The EU has probably been most successful in its efforts to make economic integration fair – i.e. ensure that everyone abides by the same rules and standards. Here, the fundamental factor is the level playing field established by EU legislation and the EU institutions responsible for its enforcement, particularly the Court of Justice of the European Union. This provides the strongest possible assurance that fair competition and consumer protection will not be undermined by openness. Moreover, the obligation for companies to respect EU standards when exporting products to the EU, combined with the size of the European market (with the EU representing the number one trading partner of no fewer than 80 countries), mean that the EU tends to influence standards elsewhere – the so-called "Brussels Effect".[17] Rather than allowing globalisation to become an inevitable race to the bottom, the EU can, with its regulatory power, actually trigger a global race to the top. This can only be good for globalisation in the long run.

There has been growing criticism of the fairness of competition in relation to the free movement of labour. But here, too, the EU has established a framework – on which it can build further – aimed at reconciling mobility with fairness. Safeguards central to the European social

14. See Chopin, T. (2017), "Defending Europe to defend real sovereignty", Policy Paper No 194, Notre Europe – Jacques Delors Institute and Robert Schuman Foundation, 25 April.
15. See Rodrik, D. (2011), The Globalization Paradox: Democracy and the Future of the World Economy, W.W. Norton.
16. Source: World Wealth and Income Database.
17. See Bradford, A. (2012), "The Brussels Effect", Northwestern University Law Review, Vol. 107(10), pp. 1-63.

model have progressively been embedded in European law, notably through the Charter of Fundamental Rights. And where there is more subtle undercutting of wages, the EU framework allows national authorities to set their own minimum wages and limits on working hours. Moreover, where there have been controversies (e.g. regarding posted workers), EU legislation has been amended following intense political debate.

Fair trade in Europe has also been supported by the single currency, which has reinforced the framework governing fair competition by removing the possibility of repeated cycles of competitive devaluations of national currencies. This has eliminated fears of currency manipulation, reduced protectionist temptations and supported the Single Market. Now that devaluation is not an option, euro area countries have to address the real root causes of any competitiveness problems that they may suffer.

This is sometimes seen as harsh medicine, since such adjustments may require a subtler form of devaluation through wage restraint. Many euro area countries adopted this approach in seeking to restore cost competitiveness following the global financial crisis, and most of those countries have now fully recovered. However, further thought could be given to the question of how European instruments could be developed in order to ensure that social safety nets prevent such adjustments from increasing poverty and undermining long-term growth. This will, contribute to support for the European project in countries undergoing such adjustments – particularly in the context of financial assistance programmes. Europe's crisis-fighting toolbox is now greatly improved thanks to the establishment of the European Stability Mechanism (ESM), but significant gaps remain in the absence of a grant instrument supporting social safety nets in programme countries or an option to redirect substantial funds from the EU budget.

PROTECTING EUROPEANS FROM INSTABILITY

When it comes to goods and services, the EU has contributed hugely to ensuring that economic integration is perceived as safe, and therefore sustainable. Regulatory convergence in product and services standards, coupled with a common approach for market surveillance, has underpinned trust in open markets within Europe, as has the ability of the EU to respond quickly to emerging threats to consumer protection. For example, the internal market for frozen foods was able to survive the mis-selling scandal of 2013, when horsemeat was sold as beef, in large part because it was met with an improved food labelling and EU-wide inspection regime that restored trust. By contrast, a perceived lack of regulatory convergence between the EU and third countries, especially regarding food safety, is one reason for opposition to preferential trade agreements, such as the TTIP.

When it comes to finance, until recently, the EU had less to offer in terms of making integration stable. Indeed, we learned the hard way that an incomplete monetary union, as well as integrated capital markets without similarly integrated financial regulation and supervision, can create their own forms of instability. But Europe has made important progress in this area in recent years. It has established the ESM, which has a lending capacity of €500 billion – not far short of the IMF's lending capacity for the whole world – and can come to the rescue when Member States face liquidity constraints. Equally far-reaching has been the decision to establish a banking union in order to mitigate the risk of systemic banking crises. 80% of all banking assets in the euro area are now supervised at European level, and there is a single mechanism for resolving failing banks. For the first time ever, we have genuinely supranational governance of the banking sector, based on a single rulebook. This ensures that there will be no regulatory race to the bottom.

However, there is no room for complacency in this regard. Risks to financial stability, including new risks such as cybersecurity threats, require continuous attention. The process of establishing a capital markets union remains in its infancy and faces a number of daunting legal challenges, which will need to be overcome (e.g. as regards harmonising – if not unifying – national insolvency laws). Moreover, the banking union needs to be completed by ensuring that fully robust European lines of defence are put in place to protect taxpayers, customers and depositors. There are also discussions about giving the euro area a budgetary capacity, with varying views as to whether it should primarily act as a backstop and instrument for investment protection in times of crisis, focus on stabilising the business cycle or finance the provision of public goods on a permanent basis, as well as a debate regarding the appropriate way of ensuring democratic accountability. While it is important to get this right and ensure that it is accompanied by efforts to restore fiscal buffers at national level, progress towards more central fiscal stabilisation should not be deferred indefinitely.[18]

The robustness of our crisis resolution framework will not be truly tested until the next major crisis, but we have already seen encouraging signs in this regard. Europe's financial system successfully weathered the turbulence that was observed in global financial markets in 2015 and early 2016, and the shock of the Brexit vote came and went without visible damage. More fundamentally, the path that Europe has embarked on represents the most advanced attempt yet to reconcile the benefits of cross-border financial integration – in terms of risk-sharing and access to finance – with its potential pitfalls.

PROMOTING EQUITABLE INTEGRATION

In the third area – making integration equitable – there has been less emphasis on policies at EU level thus far. To a large extent, this is because EU Member States already have the most comprehensive welfare systems in the world at national level. As Chancellor Merkel has often noted, Europe has 7% of the world's population, 25% of its GDP and 50% of its welfare spending. Welfare systems need to be adjusted in many ways if they are to be financially sustainable, but they provide a strong basis for protecting people who lose out as a result of globalisation. Indeed, history shows that making globalisation sustainable has often depended on strengthening the welfare state.

The erosion of the tax base and the shifting of corporate profits are severely challenging Member States' ability to engineer redistribution, but the EU has considerable latent potential in this regard, because no large corporation – not even Apple – can threaten to completely turn its back on the world's largest market.

Indeed, the European Commission is already using competition tools to address possible tax arbitrage by multinational corporations, while the proposed Common Consolidated Corporate Tax Base has the capacity to eliminate opportunities for tax avoidance through profit shifting within Europe. In both areas, European institutions can establish leverage over large corporations in a way that individual countries cannot.

A key issue for the EU as time goes by will be the extent to which its direct redistributional role should increase. The European Globalisation Adjustment Fund, which was established in 2007, was set up in order to help workers and companies with the transition process, but its resources remain far too limited and its procedures too heavy. The European Social Fund has much greater resources at its disposal and has proved to be effective at helping people to get back into employment. There is an argument for expanding these two programmes further, both in scale and in scope.[19]

ENSURING DEMOCRATIC LEGITIMACY

In many ways, the EU gives its citizens more democratic control over globalisation than is afforded to people in other countries. Indeed, it is far more advanced than other trade areas in terms of its political structure: decisions affecting the EU as a whole are taken jointly by nationally elected representatives sitting together in the Council of the European Union and by the directly elected European Parliament. And through the powers it has over competition and financial regulation, the EU gives its citizens greater control over multinational companies and financial markets. A united Europe, speaking with one voice at global level, also helps to communicate European preferences on trade, as well as on financial, tax, social and environmental standards.

However, governance and democratic legitimacy need to be strengthened further. For example, the ESM and decisions on financial assistance programmes are based on intergovernmental arrangements that fall outside the European Parliament's accountability remit. This may give the impression that powers have been transferred to the European level, when in fact they continue to be exercised largely by Member States.

__18.__ See Cœuré, B. (2016), "A budgetary capacity for the euro area", introductory remarks at a public hearing before the European Parliament, Brussels, 2 March.

__19.__ See Bénassy-Quéré, A. (2017), "Jobs Union", in Bénassy-Quéré, A. and Giavazzi, F. (eds.), Europe's Political Spring: Fixing the Eurozone and Beyond, Vox EU eBook, 31 May.

Thus, intergovernmental institutions such as the ESM need, eventually, to be integrated into the EU's treaties in order to improve both democratic control and the means and perception of joint ownership and decision-making. Otherwise, we risk a situation where common challenges are continually seen through a national lens, which inevitably fragments Europe's democratic debate and fuels divisions that undermine efforts to implement effective European policies.[20]

All of this is made more challenging by the fact that there is not yet a meaningful European public space. And yet here, ironically, globalisation could actually come to the EU's aid. The spread of digital technology, especially among younger people, could ultimately lead to a different, less nation-centric debate about the role of Europe.

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The EU's challenge is to preserve social contracts within countries in the face of globalisation – which effectively requires a social contract across countries. This is what the EU provides at European level, through its legislative, executive and judicial powers. If those powers are well used, and if economic, social and legal frameworks are also improved at national level, the EU can make a decisive contribution to making globalisation sustainable, both in Europe and beyond.

In so doing, the EU could also go a long way towards addressing its own challenges in terms of popular legitimacy. If it can better advertise its capacity to harness globalisation to the popular will, and if it can be reformed in order to achieve its full potential, there is no reason why some of the negative perceptions that surround the EU today cannot rapidly be dispelled. It is encouraging to see European leaders working to define a vision for further integration with a view to tackling common global challenges. Despite everything we hear from the various doomsayers and naysayers, this could be Europe's moment. We need to seize this opportunity – and do it soon.

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20. See Cœuré, B. (2015), "Drawing lessons from the crisis for the future of the euro area", speech in the context of "Ambassadors' Week", Paris, 27 August.