

Fiscal policy-making in EMU

Empirical question and theoretical background

The dissertation seeks to explain the emergence of the mechanisms for fiscal policy-making in European Monetary Union (EMU) and to analyse their functioning and development in the first two and a half years of their existence. The last point includes the question in how far we can observe any dynamic which has led or may lead to change in the initial setting and discusses suggestions for institutional and procedural amendments put forward by politics and the academia.

Explaining the emergence of the mechanisms implies firstly an analysis of its political and economic logic (i.e. the political logic of the status quo reflecting the results of national interests and bargaining and the normative assumptions on economic policy making which led to the particular setting). Then, the complex and interacting levels, actors and procedures of fiscal policy-making as part of overall macro-economic policy-coordination are analysed in order to be able to judge the impact of EU-level co-ordination on national policy making. This then leads to the discussion, in how far actors' preferences are met, violated or have changed – the key to answer the question, whether the current set-up creates any impulse for change, i.e. further institutional development or even the danger to break apart.

Political relevance and policy significance

EMU is unique in the way it combines a single monetary policy with national economic and fiscal policies. Strong interdependencies among monetary and fiscal policies have led to some degree of policy coordination. Yet, the unwillingness to surrender further parts of national sovereignty to the EU-level, has produced an outcome which does not measure up with the economic policy-making setting within nation states: the single monetary policy is not matched by a unitary economic or fiscal policy. The various procedures and processes have created a complex setting of actors and their respective objectives which has been criticised - not only from the economists' point of view, but also from perspectives considering democracy, transparency and legitimacy. The former e.g. see potential risks in the EMU-arrangements, as they may not be able to deal with e.g. external shocks, given the political constraints on joint action. Reasons for this view are e.g. the absence of transfer mechanisms, a weak attitude towards economic solidarity which could lead to a collapse of the Stability and Growth Pact or hinder enhanced co-operation as soon as national constraints influence individual governments' behaviour in a way that they pursue national objectives regardless of the euro-zone targets, etc. Various approaches to accommodate shocks and manage crises have been

suggested. However, given the role of tax and expenditure for national sovereignty, they are far from being achieved, as the limits to public debt and deficit touch on one of the key elements of national sovereignty.

Political scientists have worked on the explanation, why and how EMU emerged. Yet only few studies include the mechanism for fiscal policy co-ordination. This is a gap the study seeks to fill: too give an account and explanation of the emergence of the mechanisms for fiscal policy making in EMU. Hopefully, the analysis then provides insights into the stability and weaknesses of the current setting and nourishes the debate on alternative models for fiscal policy-making in EMU from a political scientist's point of view, as existing suggestions are evaluated e.g. regarding the likeliness for the actors to realise them.

Theoretical relevance and significance

Economists have profoundly analysed the interdependence of monetary and fiscal policy. Yet, policy-making is often seen as a technical exercise in welfare maximisation. This study understands macro-economic policy-making as government action to achieve various conflicting aims, many of which have more to do with domestic policy than with international policy optimisation.

As far as specialised integration theories are concerned, the study goes along with the critique of e.g. Andrew Moravcsik¹ that the classification of the EU as a "construction sui generis" whose development can only be grasped by "sui generis"-theories is not adequate. Rather, the process of EU integration is seen as a series of rational decisions, by which member states try to optimise the pursuit of their targets. This focus allows to describe goal-oriented decisions by states and social actors within the existing framework, instead of attributing (e.g. in the neo-functionalist view) exaggerated weight to non-intended dynamics triggered by spill-over.

The thesis is based on an actor-centered model in a systemic context. It thus presumes that in the EU, e.g. states as rational actors define their interests in view of domestic constraints and institutional limits. Given the fact that fiscal policy-making in EMU is a very „young“ policy field and that the current set-up is unparalleled, the thesis will attempt to include the dimension of learning in systems. A further specificity emerges from the fact that (macro-)economic policy-making is strongly influenced by schools of economic thought, i.e. there was a strong role for

¹ e.g. Moravcsik, A. 1999: The Choice for Europe, Social Purpose and State Power from Messina to Maastricht, Cornell, Chapter 1.

economic beliefs in creating the current set-up and still is in policy-making under these constraints.

The theoretical interest is firstly to contribute to the research on how EU institutions and decision-making procedures intermediate and shape national preferences. A second theoretical interest is to contribute to a model, how change and evolution take place (in this case in the context of the fiscal dimension of monetary integration). This includes two perspectives: the actors' individual perspectives as far as interests, goals etc. are concerned, and secondly a systemic view. The first perspective tries to analyse the potential of change inherent in the current system by answering e.g. the following questions: Are there new assessments, frustrations, preferences, insights? When do results of co-ordinated policy-making become relevant in domestic constituencies? In how far has the information available to different governments changed? Etc. The second approach recurs to social science research that has identified factors/preconditions for the evolution of systems/organisations. This involves findings of European integration studies and IR as well as systemic analysis, collective learning and, for both approaches, the role of economic and political belief systems².

Methodology

The thesis follows the modelling research design in that a few theoretical principles will be set out, e.g. on interest intermediation in the EMU system, learning processes etc. When the impact on national policy-making or actors preferences are discussed, the comparative method will be applied, selecting most dissimilar cases (e.g. France and Germany with contradictory interests in the shaping of the institutional arrangements, low vs. high-growth countries, and low vs. highly indebted countries etc.). For the question of fiscal policy-making in EMU, the period covered expands from the start of EMU in January 1999 to June 2001. Yet, in order to explain how the current set-up emerged, the study has to go back to the early nineties. As far as data sources are concerned, the study will first rely on existing literature and EU documents. In the second phase, EU and national officials from selected countries will be interviewed with at least three objectives: first, to cross-check the national interests derived from secondary literature, secondly,

²Assessing the role of ideas and economic beliefs in policy-making and international co-operation has become popular since the mid-eighties - theories on the role of ideas in foreign policy treat ideas as mechanisms for rational adaptation under uncertainty. This is of particular interest in the "venture EMU", an institutional arrangement unique in the world, and characterised by multiple and heterogeneous actors in a multi-level system.

to gain evidence for possible learning processes and impulse for change, and thirdly, to trace evidence for the relevance of economic beliefs.