Europe's Future Hinges on Greater Unity

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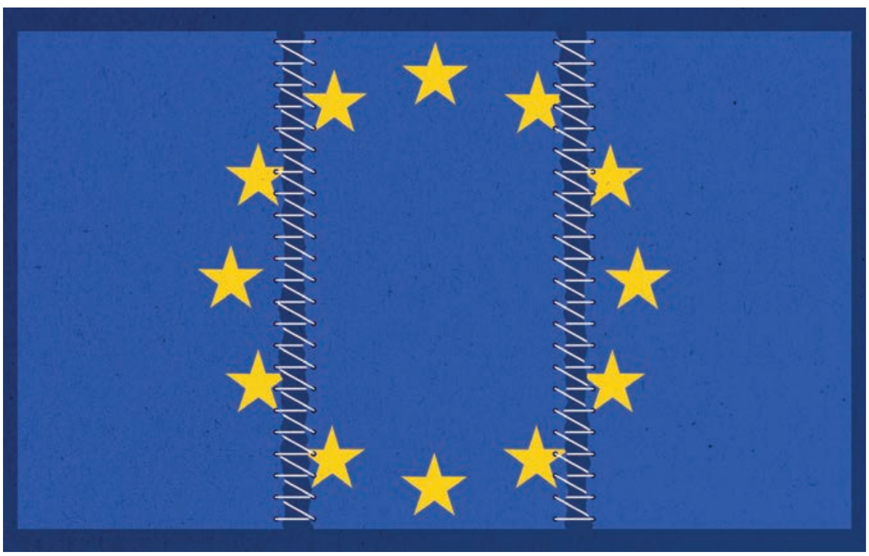
But first the EU must overcome distrust between its member states and in its institutions



Europe, as Jean Monnet, one of the founding fathers of the European Union, famously predicted, has been forged by crisis. But what makes the crisis engulfing the continent today so grave is that it has three interlocking dimensions: geopolitical, economic, and institutional. It's a crisis that cannot be resolved solely by more borrowing or a blizzard of new rules from Brussels. It requires a complete change in mindset. Are Europeans really prepared for such a leap?

Europe's first challenge is to ensure continued access to the resources it needs to power its economy in a world where the old rules-based system is breaking down. The EU is both a product of the global rules-based order and, as a region that lacks resources of its own, deeply reliant on it. Demand for critical minerals necessary for clean energy technologies is expected to rise fivefold by 2040, yet the EU's share of global production is less than 7 percent. Production of most minerals is highly concentrated in one or two countries. China, meanwhile, dominates refining—to the extent that it even refines Europe's own modest mining output.

The EU has sought to diversify access to critical minerals through trade agreements. But these remain vulnerable to a combination of trade wars, rising export restrictions, a desire by developing economies to capture more of the value chain, and the absence of a functioning dispute resolution mechanism at the World Trade Organization.

Securing access for US companies to critical minerals is a centerpiece of President Donald Trump's America First foreign policy. But European businesses—held back by environmental, social, and governance rules and concerns over political stability and the rule of law—are barely present in the critical minerals supply chain. Can rule-bound Europe develop the geopolitical and industrial strategies to compete in this more contested global order?

Deeper integration

Europe's second challenge is to deepen economic integration so as to boost productivity and competitiveness. Reports by Enrico Letta and Mario Draghi set out with brutal clarity the shortcomings of the single market and provide clear blueprints for reform that the European Commission has vowed to deliver. Both former Italian prime ministers stressed the need to cut red tape and extend the single market in sectors that have proved resistant to integration, including defense, energy, telecoms, and finance.

Yet the EU has been debating these matters for years, if not decades. The EU first announced a better regulation agenda in 2002 and launched another,

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Illustration by Chantal Jahchan

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the Regulatory Fitness and Performance Programme (REFIT), in 2015. Similarly, it's talked about deeper integration in financial services for almost as long as the single market has existed. The Giovannini reports set out proposals in 2001 and 2003; many of these reappeared as part of the push for a capital markets union in 2015. Now the project has been rebadged as a savings and investment union. Yet the EU still has 18 clearing and 21 settlement markets, compared with just one of each in the US. Fragmentation in market infrastructure is reflected in fragmented products and services.

Gold-plating

The real barrier to deeper integration is not a lack of ambition on the part of Brussels but protectionism by member states. Often this takes the form of "gold-plating"—member states pile on local requirements when transposing EU single-market directives into domestic law. The Commission has promised to counter such practices. Koen Lenaerts, the president of the European Court of Justice, reminded commissioners in a speech in January that they have the power to bring cases against offending member states. But is the Commission really prepared to take legal action against governments over gold-plating?

What makes the push for deeper integration in defense, energy, telecoms, and finance harder is that these intrude on core aspects of sovereignty. Take financial services. No one disputes that establishing deep capital markets is vital to channeling Europe's vast savings—much of which sits in bank accounts or is invested in overseas funds—into supporting European businesses. Yet a true savings and investment union requires more than simply establishing a new single EU securities regulator. It requires harmonization of national insolvency rules, corporate law, and aspects of tax law, as well as promotion of pan-European pension vehicles. Recognizing the political impossibility of such harmonization, the Commission has resurrected the idea of a 28th legal regime as an alternative—a solution first proposed in 2009 but which so far has amounted to little.

Meanwhile, it's striking that completion of the EU's banking union, which would have been at the top of almost every policymaker's list of single market priorities at any point over the past decade, is almost entirely absent from discussions about how to revive Europe's competitiveness today. It's as if measures such as a single banking rule book, a backstop for the Single Resolution Fund to restructure failing lenders, or a common deposit insurance program have simply been put in a box marked "too difficult." Yet without thriving cross-border banks to underpin European capital markets, a savings and investment union is unlikely to fulfill its potential.

A related concern is that while a single market might deliver economies of scale, member states fear that the disappearance of domestic industries would expose them to new risks. Would a genuine capital markets union leave some member states vulnerable to an exodus of domestic savings from their financial system? If the European defense sector were consolidated, would member states still be able to access weapons in a crisis? If national barriers to mobile telecom market consolidation were removed, would governments lose control over a vital piece of infrastructure? Would an integrated energy market leave countries vulnerable to higher prices or even shortages if a crisis hit elsewhere on the continent?

That points to the third challenge, which is a lack of trust both between member states and in the EU's institutional processes. The EU has long been hamstrung by what Fabian Zuleeg, chief executive of the European Policy Centre, a think tank in Brussels, calls the unity-ambition dilemma. The bloc has always sought to proceed as far as possible by unanimity, even when it's not strictly needed, even at the expense of some of its integrationist goals. But that unanimity has become even harder to achieve as politics at both the national and European levels has become more fragmented. Indeed, Europe's apparent inability to rise to its economic challenges only further undermines support for EU integration.

Improvised arrangements

The problem is compounded by the fact that some of the key players in addressing Europe's most pressing challenges lie outside the EU. Britain especially has a potentially important role to play in pan-European defense, capital markets, and energy sector integration. Part of the answer may lie in bypassing EU institutional processes to establish coalitions of the willing in areas such as defense and rely instead on improvised intergovernmental arrangements. But these must be flexible enough to accommodate changes in government and could potentially create new legal complexities and exacerbate fragmentation.

Europe has taken many large and seemingly impossible leaps forward in integration in response to shocks over the past 80 years. Faced with a shock that poses profound risks to security and prosperity, one should be wary of betting against the continent's overcoming today's geopolitical, economic, and institutional challenges. But if Europe is to be a pole in the new multipolar world, it must forge a unity beyond anything it has previously contemplated—and quickly too. F&D

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