

## Book Review

### **Jordi Gual (ed.) *Building a Dynamic Europe: The Key Policy Debates* Cambridge University Press**

**Dermot Hodson, London School of Economics and Political Science**

This short, edited volume provides a timely contribution to the debate on economic reform in Europe. Although the five essays contained within stem from a conference held in advance of the Barcelona European Council in March 2002, they pose questions that remain highly salient for the current debate on the Mid-Term Review of the Lisbon Strategy and the reform of the Stability and Growth Pact.

The book focuses, with varying degrees of success, on three principal questions. Why is economic reform necessary in Europe? What are the key challenges for Europe's economic reform agenda? Can the European Union's system of economic governance deliver these reforms?

The answer to the first question is provided in Jordi Gual's short, but well-argued, introduction. His central message, which sets the tone for the rest of the book, is that the reform of European product, labour and capital markets must go hand in hand with the process of economic integration itself. More specifically, Gual argues that structural reform is necessary to realise the long-term economic gains from market integration in an enlarged Union and to absorb the short-term economic and political costs that may be incurred in the process. He also recognises that the ability of such reforms to deliver higher growth, employment and productivity will have a significant bearing on the Union's capacity to deliver the social and cohesion policies that are demanded by its citizens.

The answer to the second question takes the form of four extended essays on the European social model, the liberalisation of network services, macroeconomic policy and integration in the banking sector respectively. A highlight here is Francesco Giavazzi's contribution on Europe's key macroeconomic challenges. This essay, which summarises much of the author's recent work in this field, explores issues ranging from macroeconomic adjustment under EMU to the reform of ECB voting rules. Giavazzi's discussion of inflation differentials and current account deficits is especially relevant to current policy debates. In the case of the former, he argues that the classic Balassa-Samuelson effect cannot account for the magnitude of inflationary differentials experienced by Ireland and Spain during the early years of EMU. In the case of the latter, he argues that Portuguese and Greek current account deficits should be seen, in part, as a positive side-effect of the economic integration of poorer Member States that have high growth potential and favourable rates of return on investment. However, Giavazzi warns against entirely disregarding current account statistics within the euro area because relative price and potential output adjustment to repay foreign debt may still be relatively high due to the fact that economic integration remains partial.

A second highlight is Assar Lindbeck's essay on improving the performance of the European social model. The point of departure for this contribution is that welfare reform is essential to (1) improve financial viability in the face of economic and demographic shocks, (2) strengthen incentives to work and invest, and reduce moral hazard and benefit cheating, and (3) adjust to changing socio-economic conditions like increased female labour force participation and changing family structures. The chapter, which is helpfully organised around the life-cycle of (i)

childhood, (ii) employment and income security, (iii) sick-leave insurance and healthcare, and (iv) pensions and old-age care, provides a useful summary of the recent literature and highlights a number of untested hypotheses for future research. Lindbeck's analysis of policies to combat unemployment stands out. Having surveyed a range of product and labour market reforms, he concludes that the sum of all institutional reforms thus far has had a limited impact on persistent unemployment, except perhaps in the Netherlands and the UK. This leads to the provocative conclusion that Europe's reform gridlock may simply be due to the fact that governments and economic agents lack confidence in the proposed policy measures – a conjecture that is likely to ruffle the feathers of policy makers and academic economists alike.

The answer to the third question is perhaps the least satisfactory. The issues raised in the rest of the volume would lead the reader to expect a discussion of the mechanics of EU economic governance, covering matters such as the reform of the Stability and Growth Pact, the merits of the Open Method of Coordination and the effectiveness of the Broad Economic Policy Guidelines. Instead, the essay by Gérard Roland on the new European governance focuses on the constitutional politics of the European convention. By itself this piece provides a thoughtful overview of parliamentary vs. presidential models of European government followed by an interesting discussion of the pros and cons of democratically electing the President of the European Commission. In spite of these merits, it is hard to see what this chapter brings to bear on the question of how, as Gual puts it in his introduction, Europe can move forward with its economic reform agenda. Roland's additional assertion that "welfare systems are already strong in most European countries and [that] there is no real evidence that they are being eroded by globalization or European integration" further highlights the lack of fit between this essay and the rest of the volume.

### **Geoffroy Matagne, University of Liège**

Economic reforms have long been high on the agenda of the European Union. The Lisbon European Council in 2000, the Eastern enlargement, the elaboration of a new constitutional treaty have given even more salience to the economic and social policy challenges the European economy faces. The ambitious Lisbon objectives – in a nutshell, making the European Union the most innovative and dynamic knowledge economy by 2010 – have been often referred to, debated and/or ridiculed. In the context of the current mid-term assessment of the Lisbon process, the academic analyses provided by the volume edited by Jordi Gual are timely.

The declared purpose of this book is 'to analyse key policy reforms aimed at bringing about the kind of economic dynamism Europe so sorely needs' (p. 2). It proposes five contributions, focusing on macroeconomic policy and structural reforms, by scholars from across Europe.

In the first chapter, Gérard Roland looks at the institutional aspects of the European Union, at its 'governance' problem. He explores an interesting dimension that runs throughout the volume: the relation between institutional arrangements (notably their legitimacy and capacity) and economic reforms (notably their efficacy). The underlining focus here is on the economic effect of political institutions. For Roland, the challenge is to find 'a more democratic and accountable set of institutions while keeping an adequate balance between both pan-European interests and national sovereignties' (p. 19). In this contribution, he looks at the issues at stake in the elaboration of the new constitutional treaty. He analyses the tradeoffs between presidential and parliamentary regimes in the context of Europe and compares their respective benefits and drawbacks. In his final section, he argues in favour of presidential governance, the president being elected by an electoral college composed of national parliaments. He argues against the election of the president of the Commission by the European Parliament and against a 'double executive' (President of the Council and President of the Commission). As regards the Commission, he argues for strengthened executive powers as well as strengthened accountability to the Member States and the citizens of Europe.

Next, Assar Lindbeck looks at welfare state achievements and problems in various West European countries. He studies the main welfare and employment policies and organises his analyses as a 'journey' over the life cycle: childhood; working life (employment and income security, sick-leave

insurance and health care) and retirement period (pensions and old-age care). He outlines the main weaknesses and limitations of the current arrangements (financial instability, undesirable behavioural adjustments, limited adjustment to changes in socioeconomic conditions, entrenched interests) and argues that structural reforms are necessary (and indeed possible with enough political will) to ensure the viability of the social protection systems and more broadly to improve the performance of European social models. He concludes by some comments on the challenges raised by the increased mobility of labour and the development of information and communication technology for welfare states.

In the third chapter, David M. Newbery analyses the liberalisation and integration of network services markets, focusing on the gas and electricity industries. He argues that a key challenge is to strike the 'right balance between complete liberalisation and ensuring capacity and investment', between regulation and structural reforms. He stresses that 'proactive competition policies will be necessary to resist the powerful forces for vertical and horizontal integration visible in the Union' (p. 97). He also underlines the need not to take into account other goals, seen as nationally important.

The following chapter, by Francesco Giavazzi, addresses the challenges for macroeconomic policy in EMU. It analyses different sets of issues: the monetary and fiscal co-ordination in EMU; the macroeconomic adjustment inside EMU (esp. inflation differentials and current account imbalances within the euro area); the reform of the Growth and Stability Pact and the reform of the voting rules on the European Central Bank Council. On these issues, he argues that there is no need for an explicit co-ordination of monetary and fiscal policies in EMU, as long as monetary and fiscal authorities 'keep their houses in order'; that 'inflation differentials can be desirable, leading to higher real income and the proper economic adjustment' and that the same can be said about current account deficits in the lower-income countries; that the GSP should be amended to allow for the separate treatment of investment expenditures and he stresses the importance of solving the ECB's numbers problem.

In the last chapter, Jordi Gual assesses the European Union policies pursuing the creation of a single banking market. He analyses the specificity of the European Union's approach to the integration of European banking (mutual recognition with a minimal degree of harmonisation) and discusses the main features and the consequences of this approach. He shows how the degree of integration of banking markets has increased as a result of the European Union single market policy and the adoption of the single currency, while (and why) the integration is not complete in retail markets.

The volume addresses a series of particularly interesting issues. Given the ambitious subtitle of the book, the reader may be surprised by the absence of some salient and current debates and issues, e.g. the 'Bolkenstein directive' or the qualities and shortcomings of the new constitutional treaty as far economic policies are concerned. Yet, one of the qualities of volume is to focus on broad and long-standing economic policy challenges. Such a succinct volume could not address all of them of course. The selection offers an interesting and diversified panorama.

Timely, well argued and well documented, this book will be of particular interest to European and National policy actors and analysts. Yet, it is also highly readable. It could therefore appeal to a more general public and contribute to the reflections of any European citizen on the future challenges of European integration.