

EUROPE: MARKET OR CARTEL?

Speech by Mr John O'Sullivan
Given in Prague on 7th November 2007

Mr. President, distinguished guests, ladies and gentlemen.

May I begin saying what a great pleasure it always is to be back in Prague. My first visit to this great city was in the darker days of 1971. That year I arrived here from the more relaxed atmosphere of Budapest and was at once overwhelmed by the grim mood of the city and people. In addition to the omnipresent fact of oppression at that time, there was a sense of despair that for the third time in thirty years the freedom and independence of the city had been snuffed out by a combination of external and internal enemies. Few people were optimists. Many were resigning themselves to a drab and controlled future.

In fact what I didn't see was more important than what I did—namely, that many people were also quietly resisting, establishing internal escapes from totalitarianism, escapes as different as plays performed in private homes to philosophy lectures given in secret by scholars whose day job was janitor or coalman. Later we in what used to be the West gained some sense of this resistance from the plays of Tom Stoppard, the writings of Roger Scruton in England, the manifesto of Charter 77, and the international example of Vaclav Havel. Even so we were surprised by the sudden upsurge of the “velvet revolution” and the dramatic disappearance of the totalitarian power that had only the day before seemed permanent and even invincible.

I have visited Prague many times since those heady days. In 1996 I was one of those who founded the New Atlantic Initiative at the splendid Congress of Prague with the message that the Czech, Slovak, and other Central and East European peoples, as undeniable Europeans, should be admitted without delay to the modern institutions of Europeanism and Atlanticism. I am glad to say that that has since largely happened.

But it is the exertions of the Czech people that have produced the most important change: with every visit I make the city of Prague seems to grow more prosperous, more civilized, freer, more stylish, more truly itself. It is a great pleasure to be here once again in this free and civilized city.

I must also thank you, Mr. President, for the kind, if slightly intimidating, invitation to address this society. I might as well confess at once what would soon become clear: that I am no economist. My trade is that of journalist. That makes me one of what Friedrich Hayek once called “second hand dealers in ideas.” Before you leave in disgust, however, let me point out that some people make perfectly successful careers in business, politics, and even academic life without dealing in ideas at all. We at least deal with them at second hand. And that gives us a slight advantage: we examine them after they have been used for some time. We see how they have performed outside the lecture theater in the real world. We see if their performance in practice bears much relationship to their performance in prospect.

THE EUROPEAN PROJECT

Bearing those considerations in mind, let me look at one particular idea tonight—namely, the “European Idea.” Or, since this idea is one that is already being realized in practice, I will give it the more accurate title of “the European Project.”

Let me say candidly that this phrase—the European Project—sets my teeth on edge. But that is at least half due to the word “project.”

Civil politics as an activity should be directed towards creating a framework of rules within which individuals and groups are able to pursue their interests and aspirations as freely as possible. Project politics is always an attempt to draft citizens for some large activity chosen by their rulers. My distinction here between civil politics and project politics is similar to Oakeshott’s distinction between a “civil association” and an “enterprise association” and Hayek’s distinction between a rule-governed “nomocracy” versus an end-governed “teleocracy.”

Admittedly, there is an irreducible minimum of coercion in everyday civil politics. For instance, taxation is required to maintain common services—and taxation is rarely voluntary. But coercion limited to providing the resources for common services and the enforcement of common rules is much lighter and more bearable than the coercion required to recruit citizens to pursue their rulers’ ambitions.

We must also accept that project politics is a legitimate, indeed inevitable, form of politics when a nation is fighting a war of survival. The project then becomes winning the war and citizens are legitimately conscripted in order to do so.

But lesser political “projects” amount to the coercion of the citizen for the dreams of his rulers well beyond the necessities of common life. Such a politics actually blurs the distinction between fighting a war of survival and other political programs such as making arrangements for the health care of the citizenry. The lives of three generations of Europeans were blighted immeasurably by rulers with “projects” who effectively made it a crime to have personal aims and ambitions.

Thus political ‘projects’ are inherently suspect and should be kept to a minimum. A phrase like “the European project” suggests that this is not being done.

What, then, is the European Project and what is the “end” or “enterprise” to which it is directed? Simply put in the official documents of the European Union, it is “ever closer union” between European people and peoples.

From a purely theoretical standpoint, this could mean many possible outcomes:

1. A new European state, possibly a highly centralized unitary state, more likely a federation, both governed by central institutions;
2. A looser European confederation effectively run by national governments;
3. A free trade area encompassing most or all existing European states;
4. A gradual cultural evolution towards a European “civilization” decentralized politically downwards to today’s regions but united by common legal rules and standards;
5. Or, finally, some new “entity” that is neither nation-state nor supra-national body but a post-modern compromise between these different types of organization in which regions, nation-states, and federal institutions exercise overlapping sovereignty over citizens with multiple identities and allegiances.

I am sure that a people as ingenious and gifted as the Czechs could come up with several other types of theoretical Europe. In practice, however, the debate is not about the final destination but about the direction in which the European train is going.

Advocates of the European Project stress the point that we must always go in the direction of “ever-closer union.” They may indeed differ about what they see as the final destination—most are federalists, some are adherents of the post-modern Euro-entity sketched above—but they all wish to keep moving “forwards” towards ever-closer union. Under the treaties, indeed, the European courts have a constitutional responsibility to reach verdicts that push European governments and peoples in this direction.

The opposite camp—generally described as Euroskeptic—is skeptical in a broader sense. It does not believe that politics necessarily moves in a particular direction, let alone towards some inevitable objective. It does not like the idea of rulers conscripting their people for forced marches into the future. It resists demands that we have a historical duty to move towards “ever-closer union.” It therefore tends to favor decentralized concepts of European unity, such as a free trade area, that leave powers within existing nation-states or even seek the return of powers now wielded by Brussels

This dispute between supporters of the European Project in its purest form—let me call them “Europhiliacs” from now on—and Euroskeptics about whether history has a direction and, if so, whether it leads to a unified European polity of some kind, is a vitally important debate. It has serious and dangerous implications for two institutions, democracy and the market economy, that only recently seemed securely entrenched in our lives. And we risk ignoring those dangers if we regard the European Project of ever-closer union as above the usual criticism of democratic debate.

DEMOCRATIC DEFICITS

In the last two years we have had a mild grumbling crisis over the European Union constitutional treaty. Its rejection by the Dutch and French voters in referendums created this crisis. Legally speaking, the referendums should rather have solved the crisis since, under EU rules, the treaty’s rejection by a single state should have meant its demise by November of last year. Instead, a European summit decided to extend the deadline for its ratification

indefinitely. Postponing ratification was a device for saving the constitution. In accordance with this decision Ireland, Poland and Denmark promptly postponed their own referenda on the constitutional treaty (since they knew they would lose the votes at the time.) And the EU authorities decided to re-write the Constitution slightly, re-christen it a treaty, and submit it for ratification—not to the voters in a referendum but to the more predictable electorate of national parliaments.

This determination to press ahead was entirely predictable. It arises directly from the notion that “ever-closer union” is the only legitimate direction of politics. From that it follows that the only legitimate outcome of the debate on the constitutional treaty is ratification. So the question will go on being asked until all member-states have given the right answer.

We are still waiting for this ratification to bring the constitutional treaty into legal force. But some of its main provisions have introduced anyway under earlier treaties—and not small items, either. The European defense procurement agency is up and running and doing business and spending tax revenue even though it has no legal existence as yet. The EU foreign minister (or in the Euro-jargon, “High Representative”) does not exist as yet either—though more than three thousand of his corps diplomatique are already being recruited and trained.

Brussels can safely proceed with this semi-legal procedure because the latest version of the constitutional treaty will not be submitted to any referendums that might produce the wrong result. Ireland alone will hold a referendum because its constitution compels it to do so, but is expected to vote Yes. The British, the French and the Dutch are all unlikely to hold referendums this time—even though the Dutch and French voters rejected the same treaty earlier and the present British government specifically committed itself to hold a referendum in its last election manifesto.

We might perhaps understand this legerdemain if it had been prompted by the need to deal with some crisis. There was some attempt by European leaders and officials that the EU would suffer from “institutional paralysis” if the constitution were defeated two years. Experience since then has proved these claims to be entirely false. The number of Council and Commission legislative instruments (directives, regulations and decisions) enacted in 2003 was 1557. This figure fell very slightly to 1477 in 2004, before increasing to

1534 in 2005 and jumping to fully 3255 in 2006. Far from the amount of EU legislation declining since the French and Dutch rejections, it actually increased. (I am tempted to add “Alas,”))

The blunt truth is that overriding the wishes of voters is business as usual for the European Commission, European governments within the EU, and Europhiliacs in general. This determination has already served the EU well on two previous occasions, when Danish voters rejected the Maastricht Treaty in 1992 and when Irish voters decided against the Treaty of Nice in 2001. These inconveniences were simply brushed aside; further referenda were held the following year; and when both resulted in “Yes” votes, the crisis was declared over and the matter closed. No third referendum was suggested.

To be fair, advocates of ever-closer union have long conceded that the EU has a "democratic deficit." Unfortunately, they treat their concession as a solution to the problem—“Yes, we’re not complacent, we recognize the EU has a democratic deficit”—and leave it at that. Occasionally, the bolder spirits propose some solution but invariably these solutions run up against the directional nature of the project. Here are three:

First: there has long been criticism of the fact that the European Commission enjoys a monopoly of legislative initiative in the EU. As the “Economist” complains, this grants a right of “advance veto” over European legislation to a body entirely composed of appointed officials. It is a scandalous denial of democratic principles. Yet apparently little can be done about this because the Commission is seen as the “engine” of the European project driving it in the right direction. Occasional attempts to garb this bureaucratic power in democratic disguise are almost comically inadequate. Here is one from a recent European Council: “Germany has suggested that if a third of national parliaments object to a proposal, then the Commission will have to submit a "reasoned opinion" as to why it is bringing the law, but will not be obliged to withdraw it.”

Second: a wide-ranging EU Charter of Fundamental Rights is part of the new constitutional treaty. This will give the European judiciary the power to repeal, amend or confirm laws in twenty-seven countries from Estonia to Portugal in accordance with its own interpretation of loosely-phrased principles and aspirations. Because European law has primacy over national law, the ultimate decision-maker on contentious political matters will be a

court in Brussels or Strasbourg. Some of the matters removed from the control of national parliaments will now be determined by remote judges in foreign cities with no necessary knowledge of “local” traditions and legal practice. This mocks any idea of democratic accountability.

Third, and most plausible, giving more powers to the democratically-elected European Parliament. This is seen logically as the most direct response to Europe’s “democratic deficit.” But this idea runs up against the social and political reality that the European Parliament, like the EU itself, is a highly imperfect body from a democratic standpoint.

For democracy is more than merely holding elections, counting votes and putting the winner into office. Before electoral procedures can create a genuine democracy, there has to be a common political consciousness, one that generates a nation-wide public opinion, to which all the parties can pitch their appeals in a debate open to all that the voters can understand. In short there has to be a political community to which democratic institutions and elected representatives can be genuinely accountable.

It is not hard to make a short list of the minimum underpinnings – the minimalist metapolitics, so to speak – that democratic politics requires. When we do so, it becomes clear that these are also the foundations of a nation state.

First, there has to be a common language and culture which shapes a common political consciousness, making vigorous democratic debate possible.

Second, there has to be a sense of political community and common destiny so that the losing side in an election will not fear being dispossessed or even murdered when its opponents come into power.

And third there have to be not merely common interests uniting the nation but overriding common interests such that people are prepared to make serious sacrifices—even the sacrifice of their lives—for them.

Almost all European nations now enjoy these underpinnings singly. But the European Union as a whole enjoys only the second – the citizens of EU member-states no longer fear that they would be dispossessed after a European election.

Otherwise, Europe speaks several languages. It has a fragmented political culture. There are no Europe-wide political parties advancing common

programmes – the Strasbourg groupings are mere collections of uncomfortable bedfellows. Even the same words – subsidiarity, for instance – have different meanings in different countries. And as the historian of Bosnia and Kosovo, Noel Malcolm, observed in his fine pamphlet on sovereignty: one can just about imagine the idea of joint Finno-Portuguese interests; but the notion of overriding joint Finno-Portuguese interests is simply a fantasy.

If none of the EU's central institutions—neither Commission, nor Court, nor Parliament—can provide democratic governance on a reliable basis, then the only structure of European government that can deliver it is one that concentrates power in the member-governments and parliaments. After all, today's Europe is composed of democratic nation-states within a non-democratic Union. Some form of inter-governmentalism is thus the only possible democratic Europeanism. Europhiliacs are reluctant to examine this, let alone concede it, because they recognize that (a) it might place a brake on ever-closer union, (b) allow different European countries to develop independently along “variable geometry” lines, and so (c) frustrate the evolution of a “united” (i.e., uniform) European state.

What follows from their rejection (and their insistence on the goal of ever-closer union) is a permanent acceptance of the EU as a structure of bureaucratic rule. Some of the bureaucrats making decisions in all these EU institutions may be called judges, government ministers, parliamentarians, or commissioners. But “bureaucrats” is what they will be functionally. They and the “candidate-members” of this bureaucracy in NGOs and national parliaments are the only group of Europeans who do have a common European political consciousness and culture. For those who remember their history, they see themselves ominously as the “vanguard” of European integration.

How do they conduct their business? Horse-trading, unrelated to the political debates of any one country, determines the decisions in a wilderness of committees. Often these meet in secret and without recording their decisions. Determining blame or responsibility for decisions is often rendered impossible. And when the decisions that come down are unpopular, the national government has to explain that nothing can be done—as governments have recently been explaining that changes to the constitutional treaty are impossible since it is—curious phrase—“politically binding.”

CARTELS, MARKETS AND REALITY

Bureaucracies can sometimes produce good policies. But this benefit tends to be temporary since a bureaucracy's natural drive to accumulate more power tends to produce over-regulation and its stultifying effects over time. In the case of the European Union, the long-term drift to over-regulation can be put down to the basic nature of the EU as a cartel of governments.

That is a challenging statement. Let me justify it.

There has always been a tension within the EU between the principles of internal free trade enshrined in the Treaty of Rome and the regulatory drift of its bureaucracy. Those who favored free trade and competition were able to cite the principle of "mutual recognition" of national standards as the proper basis of intra-European trade. But the regulatory impulse received a strong boost when the Maastricht Treaty bringing in the single European market introduced the idea that genuinely free trade required a "level playing field" across the entire Union. As a statement of economic theory that is nonsense. Trade is almost invariably conducted between unequals (in one sense or another) because it consists of people exchanging what they have for what they want. The traders themselves are the best people to judge whether or not the deal is fair.

But this "principle" gave the European bureaucracy an excuse to extend its power by replacing "mutual recognition" of national regulations with their "harmonization." That transformed a treaty supposedly extending free trade into a vehicle for extending regulation—and over time it is transforming the EU from a market in governments into a cartel of them.

A cartel is a device for raising prices by restricting competition. The price of government for consumers and businesses consists of taxes and regulations. If governments want to attract investment, hold onto high-earning workers, and encourage business start-ups, they keep regulation light and taxes low. Other governments will then have to keep regulations light and taxes low in order to compete with them for the same scarce resources. The resulting market in government services will tend both to restrain the size and intrusiveness of government and to allow the best mix of tax and regulation to emerge from competition among them. In principle both inter-

governmentalism and federalism allow this jurisdictional competition. So the EU could have developed along the lines of a market in governments.

In practice, however, the EU has become a cartel of governments in which Brussels “harmonizes” different national regulations (and even some taxes) to produce uniform standards across the Union. Such harmonization is almost invariably “upwards” to tighter and more expensive rules since the industries harmed by competition tend to be more politically active than consumers who benefit from it. And it produces other damaging effects.

As any economist would predict, this increasingly misallocates resources over time. Why is it that, if Tony Blair and other EU leaders wanted a more efficient economy with more rational priorities (i.e., less spending on agricultural supports and more on scientific research), such policies always seemed to elude them? Why is it that when such policies managed to get adopted, as in the “Lisbon agenda,” they had such limited and disappointing results? And how come the EU has stubbornly resisted reform of the CAP and continues to spend 40 per cent of its budget on 4 per cent of economic activity when anyone can see this is foolish?

The answer is that the EU, as a bureaucratic cartel of government, increasingly transforms economic priorities into political ones—and political priorities are driven by non-economic considerations. They reflect the interests of powerful groups—rent-seekers such as French farmers and Spanish fishermen—with close links to the bureaucracy rather than textbook economy theory. Such groups will not surrender valuable privileges simply because they do not maximize returns on spending or represent optimal economic outcomes for the EU. States representing the interests of those groups will insist on being “paid” for conceding some of the privileges by obtaining some other benefit—the siting of an EU agency in their country, for instance. In a non-market political system of distribution—which a cartel of governments is—log-rolling becomes the standard method of directing investment. This systematically misallocates resources over time.

Indeed, it requires heroic measures to keep the losses to moderate proportions, let alone abolish them in the course of setting more rational priorities. Hence the persistence of CAP spending should not astonish us.

Is there an alternative policy?

[see diagram below]

To explore what such policy might look like, let me resort to political science and draw a theoretical diagram. This will demonstrate that when we distill the various disputes over EU policy, we will be left with three large debates. Each of those debates is, so to speak, a spectrum of opinion going from left to right:

1. Spectrum A on political economy goes from the Social Model on the left to the Market model on the right.
2. Spectrum B on international relations goes from the anti-American “counterweight” model of the EU on the left to the Atlanticist model on the right.
3. Spectrum C on governmental structure goes from supranationalism on the left to intergovernmentalism on the right.

It is fair to say, I believe, that there are family resemblances linking the positions people take on these different models. I have labeled the policies on one side as belonging broadly “adaptive evolutionism” and on the other to “constructivist rationalism” which correlates roughly with civic politics and project politics respectively. Thus those who favor the social model in political economy will tend to support both the “counterweight” model of Europe in foreign policy and supranational model of European integration. Ditto those favoring the market model will lean towards the same end of the other two spectrums.

Such inter-relationships are tendencies, however, rather than absolutely firm relationships. Some especially logical souls will find themselves at the same extreme end of all three spectrums. Ex-President Chirac embraced the social model, the counterweight model and the supranational model. The British Tories would tend to be at the opposite end of all three spectrums to President Chirac—I certainly would find myself there. But others would pick and choose. I think it reasonable to describe the current head of the EU Commission, Manuel Barroso, as a supra-nationalist who is nonetheless nearer to the market model than the social one and who as an Atlanticist dislikes the counterweight concept of EU foreign policy. Most East Europeans, because of their experience in Comecon, are currently market modelers who favor intergovernmentalism and Atlanticism. But all three preferences may be subtly

modified if they succumb to the temptations of larger subsidies from Brussels. Britain's Gordon Brown thinks of himself as a market modeler, intergovernmentalist and Atlanticist, but none of those three claims would survive examination. And so on.

At first glance it seems more pragmatic and reasonable to mix-and-match different positions from the three spectrums. But there are reasons for these different attitudes to be linked aside from the imperatives of political dogma.

Consider, first, the relationship between the spectrums on political economy and governmental structure in the light of current controversies. Suppose, for instance, that Gordon Brown genuinely wants the EU to develop a more flexible labor market that would reduce labor costs in order to cut unemployment. He would then have to face the fact that many French voters rejected the Euro-Constitution precisely because they believed—wrongly, in my view and in that of the French government—that the constitution would weaken their treasured social model on “Anglo-Saxon” lines. No French politician could win an election by advocating what the French quaintly call ultra-liberal “modernization.”

Here is where governmental structure comes in. In an intergovernmental Europe (or what is sometimes called a “free trade area”), that difference of opinion need not matter overmuch. Both French and British governments would pursue their distinctive economic policies in an environment of “jurisdictional competition.” And there would be endless battles of statistics to seek to prove which tax-and-regulation model had delivered the goods.

In a supranational Europe, however, such a live-and-let-live arrangement would be impossible. The requirement for common policies and the “harmonization” of different national regulations would compel both countries to adopt the same set of rules. No doubt those rules would be a compromise of sorts between markets and social intervention. Neither country would be satisfied; the compromise would probably lack the virtues of both approaches; and we would never settle the superiority of either system through competition. If there really is to be market competition in Europe, the EU needs to lean heavily towards the inter-governmental end of the spectrum.

The social model in the economic spectrum also clashes with the Atlanticist end of the diplomatic one. Nor are the reasons obscure. A social model a la française increases domestic industrial costs and reduces competitiveness. If those costs can be exported to other EU members through harmonization, costs rise throughout the cartel. With higher costs, continent-wide, the EU now has either to export its regulations internationally or erect various tariff and non-tariff barriers to trade. In fact it is likely to do both. The U.S. is currently protesting the EU's attempt to impose new and more onerous chemical regulations through the "cultural exception" in WTO rules, and the Chinese are angry at the EU for cutting textile import quotas. The more ambitious the social model, the more protectionism it requires, and the more likely it is to provoke trade disputes, and over time the more it will alienate its alliance partner.

Now, the same is true—though less obviously—of the relationship between Spectrum B and Spectrum C. Supra-nationalism may not actually mandate a diplomatic stance of rivalry towards the U.S., but it makes one more likely. For their own nation-building purposes, EU supranationalists tend to promote anti-Americanism as the glue of an otherwise disaggregated European identity. Still more fundamental, supranationalism makes rivalry possible. An intergovernmental Europe simply could not be a rival of the US even if it wished to be one. It would be unable to maintain a consistent common stand. It would have no armed forces. It could never unite around opposition to U.S. policies since there would always be some nations on the side of the U.S. Atlanticism would then be the only sensible and effective common foreign policy open to it.

What the model suggests, therefore, is that supra-nationalism in the EU context obstructs not only economic rationality but also continuing good transatlantic relations. Bureaucratic government and a Euro-cartel suit each other almost precisely, just as inter-governmentalism will tend to favor (though not guarantee) free trade and markets. All bad things go together—and most (at least) good things too.

If Europe is to be an efficient corporate economy, let alone a vibrant market one, then we would have to reform the entire institutional and legal structure of the EU and to re-write the existing European treaties. We would have to replace regulatory harmonization with the principle of "mutual recognition" of

national standards. We would have to transform the present cartel of governments into a market of governments in which European nations compete with each other by offering different mixes of tax and regulation to attract investment and talent. And since the existing policies admirably suit the interests of Europe's bureaucratic ruling class, we would have to bring in political reforms to make the EU and its institutions more democratic, liberal and flexible.

At present there is little chance of such policies being adopted. In fact, the recent European Council showed that we were moving in precisely the opposite direction: An attentive diplomat noticed that several key words had disappeared from the previously circulated draft of a "mandate" for a new European treaty. It no longer promised the "free and undistorted competition" of earlier drafts. Nicholas Sarkozy, the newly-elected French president, had quietly approached Angela Merkel (wearing her hat as holder of the six-monthly rotating European Council presidency) and persuaded her to drop the offending phrase. Tony Blair, Gordon Brown, and others, having failed to get the phrase re-inserted, now argue that it is a meaningless concession that is contradicted by other provisions of the proposed treaty. But the fact that Sarkozy got his way—in company with the German Chancellor—is not meaningless.

It was a symbolic victory of Maastricht over Rome—and of French etatism over Anglo-Saxon liberalism. It will influence the judiciary's interpretation of the constitutional "reform treaty" in the direction of greater regulation and less competition. And it will therefore have major consequences for policy over time.

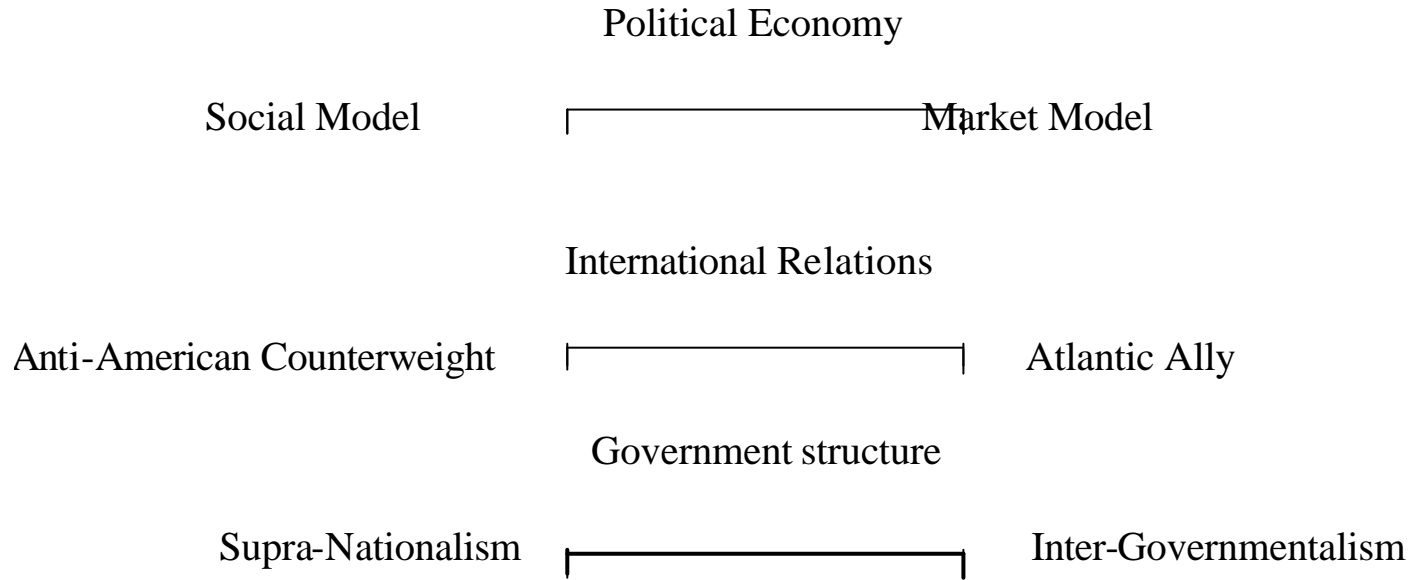
Let me be clear, however. My objection to this excision is not that Sarkozy will now drive a fleet of Peugots and other "national champions" through the loophole it made. He could do as much in an open, decentralized and flexible Europe based on jurisdictional competition. But then he would be competing with other economies following more liberal models, and we would discover which model worked best. What is legitimately worrying about Sarkozy's modest little triumph is that it re-wrote a European constitutional treaty. It can therefore be cited as justifying a common European policy of picking industrial winners and subsidizing national champions. No doubt that will take time and require determination, but Sarkozy has plenty of both.

Sakozy has something else on his side. The underlying ideology of the EU is uniformity—whether liberal uniformity or statist uniformity is a secondary question as long as all states go in the same direction. So, if Sarkozy continues to push his cause, politicians, governments, and nations that now think themselves liberal could find that they have been press-ganged for a Colbertian policy of economic nationalism on a European scale. They did not expect this and they may not like it.

As I warned, however, that is the nature of “project” politics.

IMPRESSIVE SOCIAL SCIENCE DIAGRAM

Constructivist Rationalism



Adaptive Evolutionism