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POLICY BRIEF

AFTER MERKOZY: HOW FRANCE AND GERMANY CAN MAKE EUROPE WORK

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SUMMARY

The eurozone crisis has shown that the Franco-German tandem remains a vital driver of European governance. The election of François Hollande should be good news for the tandem's capacity to generate constructive compromise in Europe. It will help correct the perception that Germany is the overly dominant partner, although French influence has been underestimated. As the historical evidence shows, the partnership between Berlin and Paris tends to work best for Europe whenever it produces a synthesis between politically opposed starting positions. This makes it easier for other countries and political forces to buy into Germany's and France's proposals for new European policies.

Despite some grandstanding on both sides, the outline of a new eurozone deal rebalancing austerity with new measures to help growth is already recognisable. Once it is achieved, France and Germany should embark on a work programme to adapt national administrative and political practices to the new European rulebook. Angela Merkel and Hollande should also move to facilitate cross-border labour mobility in the EU and take steps towards modest eurozone welfare policies than can act as automatic financial stabilisers. Finally, Berlin and Paris should engage in more consultations with their European partners. All this will help to create goodwill for the treaty change that, in the long term, is needed to give the eurozone the leadership it needs.

The rise of the Socialist leader François Hollande to the powerful presidency of France will transform the politics of the eurozone and rebalance the European Union's most important partnership. Both historical evidence and the recent experience of the "Merkozy" era suggest that cross-party constellations in Franco-German relations often work best for Europe. When the leaders of the two countries start from different ideological positions and belong to different party political families, it makes it easier for others to contribute to the debate, mediate and recognise Franco-German deals as their own. When the relationship between Berlin and Paris is seen as too symbiotic, on the other hand, it diminishes the duo's potential as a laboratory of beneficent European compromise – precisely the problem with "Merkozy" during the last year.

Barring the unforeseen, Hollande will lead France at least until May 2017. Under an extreme scenario for the next five years, a severe worsening of the euro crisis could see governments and parliaments forced to choose between the rapid creation of powerful federal instruments (such as joint debt liability or a common treasury) and the collapse of the euro. Even without such a dramatic chain of events, however, the economics and politics of the eurozone are set to dominate Hollande's time in office: his spectacular inauguration-day visit to Berlin demonstrates this vividly.

In the short run, the Franco-German tandem will be busy managing the difficult situation resulting from the elections in Greece, the worsening growth prospects for the eurozone, and Hollande's push for new EU and eurozone policies to sustain demand. In the longer term, treaty change is set to make it back to the top of the EU's political agenda. It is often overlooked that a political decision to this effect has already been taken: the 25 signatories of the Fiscal Compact have committed to attempt to integrate it into the EU's regular treaty after a maximum of five years. With the Fiscal Compact scheduled to enter into force by 2013, full-blown EU treaty change will therefore return to the EU's political agenda no later than during the second half of Hollande's mandate.

Hollande, in fact, has been careful to formulate his demands in such a way as to make most of them acceptable to Berlin. The choice of Jean-Marc Ayrault as prime minister, a low-key socialist with an aversion to grandstanding, strong local roots and a pragmatic approach to politics, will be welcomed as another positive signal in Berlin. Ayrault, a former German teacher, speaks German – as does his closest collaborator, his directeur de cabinet Christophe Chantepy. Given the worsening of growth prospects in the eurozone and the difficult situation in Spain and Italy, Hollande's election should act as a welcome catalyst for a course correction in the eurozone's joint economic policy that would have been necessary anyway – such as pushing back national timelines to reach balanced budgets. Chancellor Angela Merkel signalled even before Hollande's electoral victory that her government would be ready to do more for growth through the European Investment Bank (EIB) and the EU budget – provided the ultimate goal enshrined in the Fiscal Compact of bringing down public debt and deficits remains unquestioned. The renewed tension in the financial markets resulting from the elections in Greece makes it even more urgent for France and Germany to come to a new agreement reasonably fast. Given sufficient political will, this should be achievable by July, freeing the way for the legal adoption of the Fiscal Compact by 2013.

Rebalancing the eurozone's macroeconomic policy framework is for now; full-blown EU treaty change is a longer-term issue. This brief argues that France and Germany should define and take action on other eurozone policy priorities in the intervening years. First, they should initiate a programme of administrative and political reforms to make national and European governmental practice sufficiently compatible to deliver on the new missions resulting from the reform of EU and eurozone governance. Second, they should launch a work programme to facilitate cross-border job searches and take first steps towards building a small complementary European welfare system. Third, France and Germany should make a sustained effort to make their joint leadership more inclusive. All of this would strengthen the eurozone's political efficiency, improve the EU's standing with disaffected parts of the electorate, and boost the chances to secure popular support for a new attempt at giving the eurozone and the EU the more forceful and more accountable political leadership it so desperately needs.

An elective and selective relationship

France and Germany have driven European integration since the 1950s. The euro crisis has shown it was false to think that the EU's big eastern enlargement would make the tandem obsolete. Responding to the weakness of the eurozone's system of governance, Paris and Berlin have acted as the self-appointed nucleus of the eurozone's crisis management system. "The (European) Commission was technically and politically unprepared and therefore unable to take the lead and act swiftly", said a French official. "This is why we had to step in."

Although it was vital for France and Germany to act as an ad hoc emergency government in order to contain the crisis, it has not enhanced the duo's prestige or popularity. Under the increasingly symbiotic stewardship of former president Nicolas Sarkozy and Angela Merkel, the Franco-German couple has been perceived by many of its partners as divisive, dominant and careless in its casual bypassing of joint EU and eurozone institutions. In many capitals, a grudging acceptance of the need for Franco-German initiative now goes hand in hand with deep resentment about what is seen as a permanent exclusion from European leadership circles – a situation worsened by the dysfunctional elements of the Lisbon Treaty's new system of European government.

In acknowledging the Franco-German tandem's central role, it matters to take note of an important but rarely mentioned restriction: in most areas of EU politics, there is no such thing as a special Franco-German relationship, let alone a joint leadership role. As the year 2011 and the military operation in Libya have amply demonstrated, foreign policy is not an area of regular Franco-German co-ordination, and neither are defence, nuclear policy, trade, environmental, competition and many regulatory issues. The Franco-German engine dominates European institution-building and broad macroeconomic issues. Because the euro crisis dominates European politics today and because it is playing out in precisely these two policy fields, it feeds the mistaken impression that France and Germany are able, or aiming, to leave their joint mark across the whole range of core European policy.

A closer look reveals a further layer of complexity. Even on economic issues, Paris is not Berlin's first port of call. "We know that we normally want things which are very different from what the French want", said a German official dealing with financial policy. "The real brainstorming, reflecting on good ideas, thinking about how to make the Fiscal Treaty work and how to build a system of fiscal control, that we do with the Finns and the Dutch first. These are the partners we really share an approach with. We call the French only once we have established a common position among our group of like-minded countries. And we know that once we start speaking with the French, then the trouble starts." The discreet operational alliance between the German and the even more hawkish Dutch finance ministry goes back decades. France was never Germany's closest partner in

Europe. Rather, it is the partner with whom achieving a compromise has the greatest overall impact on EU policy.

Imbalances hurt

The euro crisis has reaffirmed the relevance of the Franco-German tandem and changed its internal dynamics. These are now harder to read and more difficult to manage. For decades, there was what Stanley Hoffmann called the "symmetry of asymmetry" between a France that was perceived to lead in political terms and a West Germany that was stronger in the economic sphere, which worked as a stabilising feature of the duo. In reality, Germany shaped the EU politically at least as much as France, and French economic growth averages often matched and occasionally outperformed Germany's. But the sense of balance that arose from a politically confident France and an economically confident Germany helped the couple through numerous power battles.

Even more than German reunification, the Treaty of Nice dealt a first big blow to this equilibrium by ending the most powerful expression of institutional equality between the two, namely their similar share of votes in EU Council formations. Since then, an increasing divergence of economic performance has reinforced a sense of growing disparity. Germany, having reformed its welfare state and labour laws and overcome the long crisis resulting from integrating the bankrupt GDR, has strengthened its primacy as the EU's most successful big economy. France, of course, is not a weak power: as a military nation ready to engage overseas and a veto-wielding member of the United Nations Security Council, it has preserved global stature. Moreover, thanks to the shrewd eurozone crisis management of Sarkozy, France managed to escape the Italian and Spanish contagion scenarios and the downward economic spiral that ensued for these countries.

Yet a rapid shrinking of France's industrial fabric, accelerated by the rise in the euro's external exchange rate, has fed a sense of anxiety and dispossession, with globalisation publicly debated as a threat rather than as an opportunity. Germany, whose industrial base is ideally structured to meet the demand of countries such as China, still produces close to 30 percent of its GDP in the industrial sector, whereas the figure for France has dwindled to less than 20 percent.[1] France lacks small and medium-sized enterprises able to compete on a global scale; Germany has roughly a thousand of them. They deliver wealth to rural areas and act as economic and entrepreneurial educators for the population, showing that global entrepreneurial success is achievable even for small companies located in rural parts of the country.

In France, hardly a week goes by without reports of yet another closure of a factory or company. Unsurprisingly, when French interlocutors are asked about the prospects for their country's relationship with Germany, the fear of *décrochage* (economic decoupling) is a recurrent theme.[2] The only structural economic factor bolstering French self-confidence when the country looks across the Rhine is its much healthier demography. But this does little to counter the prevailing sense of angst in France. The French have the feeling that they are "no longer on the same eye-level as the Germans", a French observer said.

The euro crisis has exacerbated the sense of fragility. France objectively faces a far greater risk than Germany that the markets will lose confidence in its ability to refinance its debt. This reduces France's room for manoeuvre and makes it imperative to French policymakers to sustain the perception that they form part of a bloc with Germany rather than with Italy or Spain. The political consequences for France are real, but the tendency in Europe and in France itself has been to overstate them to the point of distortion. There is a widespread perception that until the election of François Hollande, Germany alone has called all the shots in the crisis, forcing France and others to subscribe to the German vision of how to manage the eurozone.[3] But this is not how things are seen in Berlin.

The fact is that Germany has seen several of its sacred cows led to the ideological abattoir during this crisis; *Bild* (Germany's best-selling tabloid) stirred up popular emotion whenever another such sacrifice became inevitable. For example, the creation of the European Financial Stability Facility (EFSF) and the European Stability Mechanism (ESM) amounted to an implicit recognition that financial solidarity for debt-laden countries under massive pressure from the financial markets must be a permanent feature of Europe's monetary union – a de facto breach of the "no bailout" principle enshrined in the EU treaties at Germany's insistence. The self-reinvention of the ECB as a guardian of financial stability, expanding its mandate to save banks from collapse and facilitate the refinancing of otherwise bankrupt states, was another blow to Germany's psyche – and a move seen by many citizens as a further betrayal of the promises made when the euro replaced the deutschmark in 1999: most Germans want their central bank to focus on fighting inflation.

More recently, statements by Bundesbank President Jens Weidmann and Finance Minister Wolfgang Schäuble that Germany must accept a little higher inflation to balance the European South's loss of competitiveness dealt yet another

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1 2011 CIA World Factbook 2011, available at https://www.cia.gov/library/publications/the-world-factbook/fields/2012.html

2 The authors interviewed more than a dozen leading politicians, civil servants, media representatives and researchers in France and in Germany for this paper.

3 See, for example, Ifop, "L'image de l'Allemagne en France", no. 19787, January 2012; Gerrit Wiesmann and Ralph Atkins, "Schäuble ready to tolerate German inflation", *Financial Times*, 10 March 2012, available at http://www.ft.com/cms/s/0/49e9e708-9abe-11e1-94d7-00144feabdc0.html#axzz1usPB7eor (accessed 15 May 2012).

jolt to German public opinion.[4] The following day, *Bild*'s front page screamed: "Inflation alarm". Finally, Germany battled in vain against a decision to convene regular meetings of eurozone heads of state and government, an old French idea revived by Sarkozy that Merkel accepted only after fierce resistance. "We had to accede to French demands because our initial German vision for the eurozone did not work", said a German official. But the German government lacked the courage to acknowledge this in a way that every citizen would understand.

Giving up on the "no bailout" principle, extending the role of the ECB and underwriting substantial financial guarantees for eurozone partners are seen in Germany as painful huge concessions for which Germany can legitimately ask for something in return: namely cutting, wherever necessary, government spending and living and welfare standards, so that citizens and states in the eurozone no longer finance their lifestyle on credit. Whereas the French and the British speak of "austerity", a word with mostly negative connotations, the operative word in the German public debate is *Sparpolitik* – a policy of virtuous frugality based on prudent housekeeping.[5] The French see a Germany that is emerging from the euro crisis stronger than ever and imposing destructive austerity on its neighbours. The Germans perceive themselves as prudent managers of their own finances who are now being asked to rescue a cohort of spendthrifts, some of whom seem unwilling to reform.

A narrative of victimisation by external forces is now part of the debate in both countries – as it is in most other eurozone member states. This makes the search for a consensual approach in the eurozone even more difficult. The political challenge for Berlin and Paris is to identify areas where France and Germany can marginalise the impact of these differences by identifying concrete projects useful to themselves and to the greater stability of the eurozone. In a sense, Europe must now redesign its social contract – that is, the relationship between the state and the market and between labour and capital. And only a new synthesis between the French and the German social and economic cultures will make this possible.

Making the European system work

To survive and flourish in the long term, the eurozone will need to acquire many federal features of government it lacks today: the crisis has demonstrated that membership of a currency union must spell the end of autonomous macroeconomic national policy, with power transferred to a central authority. The best way to organise the necessary limitation of national power is obviously not through the current approach resting on a bewilderingly complex and fragile array of atypical political bodies, rules and sanctions. The sensible way forward would be the creation of joint institutions powerful enough to manage a crisis and set the course in ordinary times, led by elected politicians who campaign for their job across the eurozone. But barring a cataclysmic crisis, such a profound reform of the eurozone's political architecture looks politically unachievable in the very near future.

In Germany, a broad public discussion about the need to reinvent the eurozone's system of governance and strengthen its democratic legitimacy has at least started. All major political parties now advocate some substantial treaty change and are requesting a politicisation of the EU system through direct elections of the EU president or more legislative power for the European Parliament. In France, however, only a handful of leading politicians and commentators are debating these issues. Many advocates of further mergers of European sovereignty caution against engaging in a major treaty change discussion at a time of economic anxiety in France and great economic and social hardship in many EU countries. Most importantly, Hollande himself – who, when France voted on the Constitutional Treaty, saw his party split over Europe under his leadership – has no appetite for putting this item on the political menu at the start of his mandate.

However, delaying the high-risk debate about full-blown EU institutional reform for a few years does not mean that Germany and France can do nothing to make the eurozone's existing new governance more efficient. It is often forgotten that the new eurozone rules agreed so far in response to the crisis – the European Semester, the toughened Stability and Growth Pact, the yet-to-be ratified Fiscal Compact – need a number of corresponding national reforms to function properly. The new eurozone rulebook may ultimately not be practical and powerful enough to give the eurozone the macroeconomic cohesion it needs, but it will inevitably fail unless political authorities and administrations in the eurozone's member states adapt their own modus operandi to the eurozone's new governance. Some of the required changes are merely administrative in scope; others have quite serious political or even constitutional implications.

Giving national finance ministers the power to enter into a European commitment binding the government as a whole is one obvious case in point; if the head of government can ignore promises his or her finance minister has made in Brussels, co-ordination in the Ecofin or the Eurogroup will not work. The relationship between national parliaments and the European Commission is another example. One of the core aims of the new eurozone rulebook is to increase the involvement of national parliaments in the EU's and the eurozone's macroeconomic policy co-ordination. This is much more than a nod to the separation of powers inside member states. The eurozone's first decade has shown that European agreements between governments

4 "ROUNDUP/Weidmann: Inflation in Deutschland steigt nur geringfügig", dpa-AFX, 13 May 2012, available at http://www.finanzen.net/nachricht/aktien/ROUNDUP-Weidmann-Inflation-in-Deutschland-steigt-nur-geringfuegig-1862435 (accessed 15 May 2012).

5 *Sparen*, or "saving", is a word with powerful positive connotations in German. For example, German children are raised on the maxim: "Spare in der Zeit, dann hast Du in der Not" ("Save in time, so that you have in need").

regarding the conduct of macroeconomic policy often fall by the wayside. By giving national parliaments a sense of political ownership, the hope is to involve them in holding their national government to account and to avert damaging scenarios where a parliamentary majority is ignorant of, or chooses to ignore, European policy guidelines.

Faced with this new situation, the relevant committees in national parliaments understandably wish to be able to invite the European Commissioner in charge for regular auditions – a legitimate request if the macroeconomic policy proposals tabled by the Commission are to shape the policy choices of parliamentary majorities. In practice, this sensible desire poses a major problem. The sheer number of parliamentary assemblies in the eurozone – with many member states having two rather than one – makes it obviously impossible for a single European Commissioner to meet the demand for direct dialogue.

There are two possible solutions to this problem. Either the Commissioners should be given deputies who have time to travel regularly to the national capitals and are empowered to speak for their senior Commissioner (replicating a practice in many member states' governments); or national parliamentarians must travel to Brussels to hold joint auditions – ultimately raising the issue of a new parliamentary assembly in Brussels made up partly or wholly from national MPs. Currently, the choice in many cases is to have the Commissioner address national parliamentary committees via video screen, in some cases with pre-recorded messages. This leads to deep frustration among national MPs, decreasing the likelihood that parliaments will really buy into the EU's joint policy framework.

Reorganising the work of national governments and parliaments so that it fits with the new eurozone rulebook is a matter with potentially substantial political implications. Other issues are politically less sensitive but hardly less important in practical terms. Officials in charge of implementing the new co-ordination mechanisms speak of a considerable diversity of established national practice regarding the management of the national economic data flow, including the timing and nature of governments' assessment of projected fiscal revenue. Yet the Commission needs comparable data to come in roughly at the same time in order to draft its joint guidance for member states. Clearly, such problems can be fixed – but in some countries it will need strong and sustained political will to change administrative practices grown over decades or more. "Making Europe really happen will only work if we accept a fundamental change in the ministries throughout the levels of hierarchy", said one finance ministry official.

A particularly vital issue relating to the Fiscal Compact is the calculation of a country's structural deficit – a highly contentious issue between economists even when this largely artificial economic figure does not serve as a hair-trigger for evaluating a country's respect of its European treaty obligations. The easiest answer here would be an agreement to let the Commission's calculation prevail – but, so far, member states have not signalled that they are ready to do this. France and Germany should take up the task of drawing up a list of other bigger and smaller issues that also need to be tackled to adapt national practices to the new European rulebook. A European programme of national administrative and political reforms initiated, overseen and controlled by the European Commission would be an alternative; but it would easily be seen as overly intrusive and could backfire politically. Letting member states take the lead would send a strong signal of their commitment to the new governance framework, and none are better placed than France and Germany.

Building on their track record of close co-operation, the French and German finance ministries have already made a start and set up a special working unit in which such issues affecting them both can be discussed. Drawing up a list of issues to be addressed, exchanging information with other member states and inviting those who wish to join in the exercise would turn it into a shared priority. The case of Greece has shown that administrative issues, meaning the capacity of public administrations to perform, are directly related to the eurozone's viability. The importance of adjusting national administrative and political practice to eurozone governance should never be underestimated again – ignoring the problem would be tantamount to a declaration that the member states themselves have no faith in the new rulebook they have drafted.

Strengthening eurozone cohesion

Helping to make the new European rulebook work through changes in national practice would send an important signal to financial markets and national policy actors alike – but it would not engage Europe's citizens. Once they have thrashed out their compromise on how to boost growth in the eurozone, France and Germany should agree on a further work programme to strengthen the eurozone's cohesion. Two policy areas, neither of them requiring treaty change, could deliver tangible economic and social benefits with substantial political impact. The first concerns the removal of remaining administrative hurdles to labour mobility, the second a move into a partial Europeanisation of selected welfare state policies through schemes such as the creation of a complementary European unemployment assurance scheme, as several French interlocutors suggested.[6]

Facilitating labour mobility within the EU has been a priority for decades and considerable progress has been made. But the administrative, regulatory and social policy disincentives remain substantial – even if language is

6 To avoid paying for poor policy, a sensible European unemployment assurance scheme would cover only short-term unemployment. That way, it would finance transfers related to variations in the business cycle rather than transfers to regions with structurally high jobless rates due to inadequate regulation, bad infrastructure, poor training or wrong incentives.

the main obstacle. With countries in the south of Europe suffering massive youth unemployment and countries such as Germany experiencing severe labour shortages in some sectors and regions, the economic and social case for enticing young Spaniards to seek employment in, for instance, Baden-Württemberg is huge. Currently, a young Spaniard who has never been formally employed loses financial support in his country if he moves to Germany to look for a job – but has no right to German aid.

The European Commission is working to keep up the pressure to make it easier, especially for young people, to seek work in other EU countries, but given the complexity of the issue in an EU environment of nationally fragmented regulations and welfare state provisions, agreement among all the member states is often difficult and extremely slow to achieve. There is nothing to stop France and Germany to help sustain the momentum by acting as pioneers in this field: as French officials and interlocutors from different sides of the party political spectrum point out, the planned political declaration for the fiftieth anniversary of the Elysée Treaty in January 2013 could be an excellent occasion to announce the launch of an ambitious Franco-German work programme to remove remaining policy obstacles to cross-border mobility and facilitate cross-border job searches and the acquisition of language skills – keeping the initiative open to other EU member states who wish to participate.

With striking unanimity, senior French officials and politicians recommend that France and Germany embark on an even more ambitious endeavour. Because the euro crisis reduces individual member states' margin for budgetary manoeuvre and exacerbates economic and social disparities in the EU, the case has grown massively for taking a first step into establishing a system of automatic financial transfer mechanisms for the eurozone – a structural feature of all other successful single currency zones. Such stabilisers help badly hit regions get through severe economic and social crises, sustain demand in places where it might otherwise collapse, facilitate labour mobility and send a strong signal that EU policy is about helping people get through bad times and not just about exerting pressure to bring wages and welfare payments down.

The economic case for introducing them was strong even before the euro crisis. The crisis, which dangerously exacerbates economic and social disparities in the eurozone, has made it overwhelming. One of the mechanisms most commonly advocated would be a complementary European unemployment insurance scheme working alongside national unemployment insurance schemes and modulated according to average wage levels in each member state.[7] Another option would be a pan-European complementary pension scheme – an idea advocated by Italian Prime Minister Mario Monti.[8] All this would help citizens and the markets to view the eurozone as one integrated economy and social space. Distinctions would increasingly be made between growth regions and non-growth regions, rather than differentiating between the economic performances of member states as a whole.

Seeing the EU develop even a modest arsenal of welfare state provisions designed to help the unemployed or the old would do much to counter the widespread accusation in France and other eurozone countries that the EU has become a brutal tool for the lowering of living standards and employment safety in the interests of big banks and other big businesses. The charge was made aggressively in the French presidential debate by far-left and far-right candidates such as Jean-Luc Mélenchon and Marine Le Pen, and indirectly fed by Sarkozy when he accused the EU of not doing enough to protect European citizens. The former European Commission President Jacques Delors has warned since the early 1990s that the EU would lose the support of large numbers of citizens if it offered no active welfare state policies; his prediction materialised in France when the charge that the EU worked for employers rather than employees became a significant factor in the rejection of the Constitutional Treaty in 2005.

Winning the support of the Merkel government for a Franco-German action plan for full labour mobility should be feasible; convincing the chancellor of taking a first – even modest – step towards the creation of a European welfare state will be far more difficult. The Christian Democratic Union's most recent Europe programme explicitly rejects automatic transfers between member states.[9] The attitude in Berlin ranges from sceptical to hostile within the current government coalition and is lukewarm even among the opposition Social Democratic Party (SPD). To shift the German position, it would help to win the support of German trade unions and, ideally, German employers' associations. But the best French argument in favour might be to persuade Berlin that creating the nucleus of a European welfare state policy – starting from a Franco-German initiative – is a necessary precondition to achieve the support of a majority of the French electorate in a future referendum on EU treaty reform.

A change of government in Berlin as a result of the general elections in the autumn of 2013 would offer a different political landscape, especially if a Social Democrat chancellor succeeds Merkel. Selling the idea to Merkel's successor might still be difficult: "The SPD too feels constrained by German austerity thinking", said a party official. Despite intense common programmatic work, German Social Democrats and French Socialists continue to differ in

7 See Sebastian Dullien, "Improving Economic Stability in Europe", working paper, Stiftung Wissenschaft und Politik, Berlin, 11 July 2007, available at http://www.swp-berlin.org/fileadmin/contents/products/arbeitspapiere/Paper_US_KS_neu_formatiert.pdf (accessed 15 May 2012).

8 European Commission, "Green Paper: Towards adequate, sustainable and safe European pension systems", COM(2010), 7 July 2010.

9 CDU Beschluss, "Starkes Europa – Gute Zukunft für Deutschland", 24. Parteitag, 13–15 November 2011, available at http://www.cdu.de/doc/pdfc/111114-beschluss-europa.pdf (accessed 15 May 2012) (hereafter, CDU Beschluss, "Starkes Europa – Gute Zukunft für Deutschland"). However, the explicit rejection concerns automatic transfer mechanisms between states, not other forms of automatic financial stabilisation.

their approach to numerous economic issues, essentially as a result of diverging economic cultures.[10] But a Social Democrat victory in 2013 should still facilitate an agreement and open up other major fields of potential productive compromise: in principle at least, both the SPD and the French Socialist Party (PS) back a future mutualisation of debt through Eurobonds.[11]

More inclusive Franco-German leadership

In pioneering such policy proposals, France and Germany would go a long way to address the reproach that their leadership has become dominant, disruptive and sterile. But initiating an ambitious new work programme will not do enough to de-escalate the growing tensions within the EU. During the "Merkozy" era, Germany and France have at times neglected EU institutions such as the European Parliament and discarded the policy – traditionally pursued especially by Berlin – of investing in coalition-building among small countries. Reacting to the growing irritation, Merkel and German Foreign Minister Guido Westerwelle have recently conducted a discreet listening exercise to gauge the thinking of European partners regarding the future of political integration.[12] Hollande, for his part, criticised his predecessor's policy during his campaign, promising to pay greater attention to other member states while continuing to cultivate Germany as France's most important partner. After his first meeting with Merkel in Berlin, Hollande called for a relationship that is "balanced between our two countries, respectful of our political leanings, and also respectful of European partners and its joint institutions. We want to work together for the benefit of Europe, but also by engaging all the other countries of the Union.".

The conditions for moving to a more open Franco-German leadership style are there, but the difficulty for Berlin and Paris in finding the right approach should not be underestimated. Enlargement, the Lisbon Treaty and the growing necessity to develop specific policies for the eurozone all add to the complexity of managing internal EU dynamics. The disappearance of the Benelux as a relevant grouping in European politics has deprived the EU of an influential caucus of mid-sized and smaller member states with deep experience of European integration. The Lisbon Treaty, as one senior official pointed out, has diminished the European Commission president's role as a mediator by creating a competing claim for this function between him and the president of the European Council.

Looking to the future, two facts stand out. As long as EU institutions and their leaders are not strong enough to seize power and steer the eurozone through times of dangerous turmoil, France and Germany will remain an indispensable crisis-management tandem, stepping in whenever the EU or the eurozone need swift and decisive leadership. Secondly, there is no definable group of eurozone or EU member states that Berlin and Paris can co-opt into a regular, informal leadership alliance. Attempts to convene informal *directoires* of demographically big member states have invariably run into trouble, with leaders who have been "left out" attempting to gatecrash gatherings. The EU3 policy towards Iran is one of the rare exceptions in which other member states have accepted that granting France, Germany and the UK a special leadership role within the EU is the best available option. The G6 gathering of the interior ministers of the largest EU member states has run into much stiffer opposition and would trigger an uprising if the participating countries attempted to turn it into a leadership group concerned with a wider range of issues.

What France and Germany can and must do – beyond a regular but inevitably limited cultivation of each and every member state – is establish a pattern of informal consultations involving larger and smaller member states. These should obey a variable geometry determined by the topic under discussion and the European mindset of the governments of the day. As the example of Poland and Spain has shown, changing political majorities can have major consequences for a country's approach to European issues. The personalities of the key leaders are also a significant factor. Jean-Claude Juncker's influence in European politics has resulted from his personality and experience, not from his power as prime minister and finance minister of Luxembourg. Mario Monti's economic expertise and inside knowledge of the Brussels institutions make his voice an important one among the current set of leaders – and, after the years under Silvio Berlusconi, it is important to signal to Italy that good leadership wins it back a seat in the innermost circle of European leadership. This is in Germany's interest as much as it is in the interest of France: Italian and German institutional approaches to Europe are generally closer than those of France and Germany.[13]

Poland has an important function as a bridge between the eurozone members and the wider EU and it makes sense to respond to the current government's EU-friendly mindset by seeking it out. Sarkozy had famously poor relations with the Polish prime minister Donald Tusk, continuing a counterproductive pattern of prickly hostility in Franco-Polish relations. France then dealt a blow to Warsaw's attempt to reposition itself at the core of EU politics by insisting that eurozone consultations should be strictly closed to member states outside the eurozone. "The Poles

10 The SPD and the PS have invested considerable time in drafting common concepts for the eurozone's governance. Since 2008, they have met on average four times a year. See, for example, "Common declaration of the Social Democratic Party of Germany and the French Socialist Party: More courage and solidarity in the crisis – together for a strong economic government in Europe", presented by Sigmar Gabriel and Martine Aubry, 21 June 2011; see also the interview with François Hollande and Sigmar Gabriel, *Libération*, 16 March 2012.

11 Barring a major crisis, it is clear that Eurobonds are not for tomorrow. To secure German approval, they would require a major federalisation of the EU or the eurozone, including much strengthened parliamentary controls.

12 Merkel has so far invited three groups of three heads of state and government to Meseburg Castle in order to discuss European issues. Westerwelle has consulted nine "likeminded" EU foreign ministers on the future of European integration. This indicates the strength of German ambition to shape the next round of institutional and political integration of the EU.

13 In particular, the French Union for a Popular Movement (UMP), the political heir of French Gaullism, takes a much more intergovernmental approach to EU issues than the German CDU.

come every day and ask us to keep them in", a German official said during the last weeks of the Sarkozy presidency. Reviving the dormant Weimar triangle may not be the best approach, given that Weimar never developed political momentum. A better alternative might be to invite Poland to some Franco-German bilateral meetings on an ad hoc basis and to involve Warsaw in consultations about important issues.

Spain's place in such a shifting landscape of informal circles of influence is for Madrid itself to determine. In principle, size, economic weight and diplomatic ambition should place Spain among the countries that Germany and France find often imperative to consult. But, in practice, a striking reluctance of leading Spanish politicians to intervene forcefully in the pan-European debate about how to shape Europe in the coming decade has weakened Spain's weight as an essential interlocutor. There is no endogenous reason why Spain's voice in Europe should be so relatively muted, compared, for instance, with Italy's. The reasons are linked to current Spanish political preferences, the structure of Spanish politics and perhaps to Spanish history. In Berlin and Paris there is a perception that many key actors in Madrid are more interested in strengthening Spain's influence in Latin America than in working towards a stronger Spanish presence in Europe.

Finally: treaty change?

Hollande's striking campaign decision to attack Sarkozy for his alleged subservience to Merkel and to criticise Germany for excessive dominance serves as vivid proof that the lack of powerful European leadership institutions can unleash highly problematic dynamics in European politics. Top policymakers in Germany are beginning to feel the heat and increasingly see the creation of European institutions that can shoulder the burden of eurozone leadership as a matter of urgency. "The weakness of the system is not about spending and how to promote growth, but about legitimacy", said a finance ministry official.

The leading German political parties have put forward proposals for institutional reform that would require treaty change.[14] A consensus is forming in Germany around the idea of directly electing a European president – either the president of the Commission or the president of the Council – so as to strengthen European democracy and voter engagement. Other proposals stress the need for stronger parliamentary control in the EU system, either through an expansion of the powers of the European Parliament or through the creation of a second chamber made up of members of the budgetary commissions of national parliaments.[15] The German Bundestag, which saw its European policy powers boosted by Germany's constitutional court, has also started a serious debate about its responsibility for integration.[16]

The rulings of the constitutional court have triggered a related discussion about the need for Germany to change its constitution to allow for further sovereignty transfers to Brussels, requiring, according to some judges and other constitutional experts, an unprecedented referendum because of the magnitude of the changes involved. Sensing the danger of opening a new Pandora's Box, senior politicians from both government and opposition have dismissed the debate about a referendum as unnecessary and premature. But the informal talks launched by Merkel and Westerwelle with their fellow eurozone leaders show that the issue of substantial EU reform continues to occupy the government in Berlin. The current plan is to table reform proposals before the summer, one possible idea being the extension of the right of legislative initiative from the Commission to the European Parliament.

As French interlocutors readily acknowledge, the debate in France is seriously lagging behind the discussion in Germany. Some influential publications such as Le Monde have published appeals for a move to federal European and eurozone institutions that are both stronger and more accountable.[17] France's business federation Mouvement des Entreprises de France (MEDEF) has called for the transformation of the EU into a United States of Europe.[18] Yet politicians from across the political spectrum caution against major treaty reform at a time when the electorate wants to see action on growth rather than EU institutions. Although Hollande is an advocate of deeper European integration and more respectful of EU institutions than his Gaullist predecessor, he is eager to avoid an early replay of the French debate over the constitutional referendum. For the time being, Hollande has offered his backing only for reforms possible without treaty change, such as choosing a Commission president who has campaigned for the job in the European elections.

It will be the job of friends of a more federal Europe in Berlin, Paris, Rome and other capitals to convince the French president that he is right when he says that Europe needs better Franco-German leadership – but that Europe needs far more changes than those a better Franco-German tandem can deliver. It may be possible to put off treaty change for a few more years. But the provisions of the Fiscal

14 See the resolutions of the CDU, the SPD and the Greens at their respective party conferences: CDU Beschluss, "Starkes Europa – Gute Zukunft für Deutschland"; S. Gabriel, I. Gabriel, F.W. Steinmeier and P. Steinbrück, "Der Weg aus der Krise – Wachstum und Beschäftigung in Europa", SPD, 15 May 2012, available at http://www.spd.de/linkableblob/72310/data/20120515_wachstumspakt.pdf (accessed 15 May 2012); Die Grünen, "Mehr Europa Wagen", 9 May 2012, available at http://www.gruene.de/themen/europa/mehr-europa-wagen.html (accessed 15 May 2012).

15 See, for example, Joschka Fischer, "Europe's Sovereignty Crisis", Project Syndicate, 31 July 2011, available at http://www.project-syndicate.org/commentary/europe-s-sovereignty-crisis (accessed 15 May 2012).

16 In its Lisbon ruling, the constitutional court has given the Bundestag more rights to control Germany's European decision-making. See http://www.bverfg.de/entscheidungen/es20090630_2bve000208.html (accessed 15 May 2012).

17 "Construisons une Europe de la relance!", *Le Monde*, 8 May 2012, available at http://www.lemonde.fr/idees/article/2012/05/08/construisons-une-europe-de-la-relance_1697621_3232.html (accessed 15 May 2012).

18 See http://besoindaire.com/lib_ie/h/couverture.html (accessed 15 May 2012).

Compact, the pressure on Germany, the weaknesses of the Lisbon Treaty and the imperative need to give the eurozone strong, representative and accountable political authorities will ensure that the issue returns to the agenda sooner than many expect. In the meantime, making the EU's new rulebook work better, fostering economic growth and launching new policies to boost the eurozone's social cohesion are the best way to prepare for the next transformative moment in the EU's history.

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