

# Research agenda section

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## THE EURO AND POLITICAL UNION: DO ECONOMIC SPILLOVERS FROM MONETARY INTEGRATION AFFECT THE LEGITIMACY OF EMU?

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**ABSTRACT** The technical and institutional achievements of Economic and Monetary Union in Europe (EMU) are just the necessary condition for its overall success: the sufficient condition implies a widespread acceptance of the spillover effects triggered by EMU for other areas of economic policy-making, such as possible redistributive effects across euro-area member states. The article notes that much of the recent academic debate on EMU's legitimacy can be reduced to differences in assumptions on those effects. It thus calls for resuming the debate with a specific emphasis on analysing data that would provide information on observable spillover effects from EMU and allow for more solid arguments in that debate.

**KEY WORDS** Democratic deficit; Economic and Monetary Union in Europe (EMU); European Central Bank (ECB); euro; legitimacy; monetary policy.

### 1. INTRODUCTION<sup>1</sup>

Nearly fifteen years after the negotiation of the Maastricht Treaty and six years after the introduction of the euro, Economic and Monetary Union in Europe (EMU) is certainly no longer in its starting phase. The European Central Bank (ECB) is now a well-established institution enjoying similar levels of credibility within the financial community as comparable central banks (De Haan *et al.* 2005). It has developed a comprehensive system of channels of communication and practices of accountability (Jabko 2003). The euro has been successfully introduced and is gaining ground as one of the leading currencies in the world (ECB 2005a). This has led to the observation that EMU should be seen as a factor of stability in the European project, or, to use the words of an

important practitioner, as a 'solidly rooted pillar of continuity in the midst of institutional change' (Padoa-Schioppa 2003).

But EMU's technical and institutional achievements are just the necessary condition for its overall success. The sufficient condition implies a widespread acceptance of the implications triggered by EMU for other areas of economic policy-making in the member states. Given the close functional links between different economic instruments, there are almost inevitably spillover effects from the creation of the single currency to other policy fields.

Prior to the start of EMU and during its early years, it was almost impossible to get a clear picture of such effects. This is now changing. Seven years after the start of stage three of EMU a still restricted but relatively solid set of data and evidence is available. Against that background this article calls for refocusing the debate on the 'democratic deficit' in EMU with a specific emphasis on observable spillover effects from EMU.<sup>2</sup> It notes that it is striking how much of the academic debate on legitimacy in EMU can be reduced to differences in assumptions on the functional implications of monetary integration. Was EMU to improve aggregate social welfare on the basis of efficiency increases (i.e. triggering a 'Pareto improvement') or to generate distributive effects unlikely to be rebalanced by redistributive policy measures?

This article begins by looking at the concept of legitimacy and its applicability to monetary policy. It then continues with reviewing the literature in political science on legitimacy resources in EMU and shows that much of the debate is based on assumptions rather than on outcomes. The article then looks at the current economic research on the effects of EMU and discusses the implications for the debate on the democratic deficit in EMU. It ends with some concrete areas for future research on the institutional set-up and legitimacy of EMU.

## **2. LEGITIMACY OF A MONETARY UNION: WHY EMU IS DIFFERENT FROM THE TRADITIONAL NATION STATE CONTEXT**

Every monetary union that is not a so-called 'optimum currency area' will at one point face the challenge of its own distributive implications, calling for some kind of rebalancing through redistribution. Economic historians give several accounts of how the trade-off between preserving monetary union and preserving national cohesion ended in the breakup of a previously politically integrated area (see Bordo and Jonung (2003) for an overview). In 1997, Martin Feldstein employed this type of argument to justify a pessimistic picture for the outlook of EMU and predict 'future intra-European conflicts' (Feldstein 1997).

A monetary union thus has to strike a balance between considerations of union-wide efficiency and legitimacy (citizens perceiving the single currency and its potential redistributive implications as normatively appropriate). Obviously that balance is more easily reached in an optimum currency area,

where establishing a monetary union is a pure Pareto improvement and does not generate any redistributive implications. However, as soon as efficiency-increasing policies generate spillovers of a redistributive nature, striking the balance between efficiency and legitimacy becomes more difficult – and this is true for most areas of economic policy-making. Scharpf (1988) has argued that from a purely institutional perspective the conflict between efficiency and legitimacy is related to the size of the underlying political units, with large units enhancing the former and small units the latter. It would seem more appropriate not to focus on size as the main criterion in this context, but rather on the degree of political integration. A strongly integrated and politically cohesive unit (even of a large size) will face lesser difficulties in accepting redistributive spillover effects for the sake of overall efficiency increases than a smaller but politically less integrated unit.

The efficiency of a monetary framework can mainly be described by its technical capacity to provide liquidity to financial markets in a way that ensures the appropriate functioning of the macroeconomy. The most widely accepted notion of legitimacy of a monetary framework rests exclusively on a pure output criterion: monetary policy is in most cases geared towards the achievement of certain pre-defined objectives, mainly price stability, and is perceived as legitimate on the basis of reaching that goal. In the nation state environment, possible spillover effects from pursuing that objective are generally not taken into account. Mainly, because in the nation state context there are structural or political features that counter-balance such spillover effects: labour mobility, fiscal federalism, and price adjustments (see section 4 below). As is well known, EMU lacks those features. The question thus has to be raised to what extent the compatibility between efficiency and legitimacy in the EMU context is conditioned by a political dimension related to the willingness of citizens to accept the spillover effects and possible redistributive implications from the single currency.<sup>3</sup>

As in other areas of economic policy-making, the legitimacy of monetary policy may best be assessed on the basis of the distinction between input and output legitimacy (e.g. Scharpf 1999). From an output perspective, one might take the view that so long as EMU is welfare-increasing, non-majoritarian types of governance are likely to generate acceptable levels of legitimacy, deriving from the achievement of a desired policy output (here mainly price stability). From a more input-oriented perspective, one might emphasize more strongly the potential negative spillovers from the integrated monetary framework on other areas of economic policy and argue that EMU could generate undesired economic and/or political consequences lacking a sufficient degree of embeddedness in the democratic decision-making process to be perceived as legitimate.

The rather technical economic question of the implications of a single monetary policy for economic output variables should thus be at the heart of the literature on legitimacy of EMU. The answer to it is required to gain a better understanding of how much policy delegation (and in which areas)

would be necessary to ensure effective and efficient economic processes while establishing a sufficient degree of political ownership to legitimize the economic consequences of policy delegation.

### 3. DIFFERENCES IN ASSUMPTIONS: THE LITERATURE ON THE DEMOCRATIC DEFICIT OF EMU

The debate on the 'democratic deficit' of EMU began several years before the introduction of the single currency. It focused largely on the question of whether the architects of EMU had been correct in solving the feared collective action problems in a currency union by establishing a rigidly designed system of rules of the game. While widespread agreement emerged on the nature of the actual legal and institutional framework, disagreement still persists on the appropriateness of that framework.

With regard to the purely descriptive dimension of the nature of the present framework, there is now a solid common understanding. The EMU chapter in the Maastricht Treaty is described as a rather rigid legal construction geared towards specific objectives, on which societal preferences have largely converged. Price stability and the soundness of fiscal policies are considered to be the constitutive pillars of the framework and enshrined with comparatively great detail in the Treaty and primary legislation, thus enjoying significant isolation from direct policy input (Gormley and de Haan 1996). The ECB's mandate is exclusively geared towards the maintenance of price stability (the support of the general economic policies of the Community being only required if conducted 'without prejudice to the objective of price stability', EC Treaty Art. 105(1)) and thus leaves little room for policy discretion. In a similar vein, the legal framework on fiscal policy co-ordination as set out in the Stability and Growth Pact (SGP) and the Excessive Deficit Procedure (EDP) is focused on sustainability issues ('close to balance or in surplus', Council Regulations 1466/97 and 1467/97) rather than on welfare consequences of fiscal stances and their inter-temporal implications (e.g. Fatás *et al.* 2003). Many analyses point to the normative origins of that approach as the emulation of the widely respected German case and its conceptual groundings in the monetarist literature in economics (mainly Dyson and Featherstone 1999; McNamara 1998, and to some extent also Hall 1993).

When it comes to assessing the appropriateness of that framework, however, views differ greatly. I see three main types of arguments. As will be discussed below, these differences in views may be derived from differences in assumptions on the implications of EMU in terms of welfare increases versus welfare redistribution.

First, it is argued that the delegation of some parts of economic policy-making to the European level is a simple matter of efficiency increases. In this perspective, monetary policy (often quoted together with competition policy) is interpreted as the area of economic governance that enjoys insulation from direct political contestation. Delegating this task to the European level should

thus be considered as legitimate as keeping it in the national realm. In theoretical terms, the particular nature of monetary policy as a functionally clearly delimited task geared towards the objective of price stability justifies the exclusive focus of legitimacy provisions on the output side (Verdun 1998, 2000), even though the typical problems deriving from such a principal-agent set-up are likely to arise (Elgie 2002). The ECB frequently uses this line of argument, pointing out that it has been entrusted with the task of pursuing a commonly agreed goal that does not hamper member states' own policy choices (ECB 2001, 2002). Although member states are generally obliged to consider their economic policies as a 'matter of common concern' (TEC Article 107), they enjoy sufficient room for manoeuvre to follow citizens' policy inputs, thus complementing the output legitimacy dimension of monetary policy with an input dimension in other areas. The multi-level framework of economic policy in EMU is thus justified as a 'symbiotic relationship between national and EU policy-making' (Moravcsik 2000: 606) based on a clear allocation of responsibilities. The overarching logic of this kind of literature is that policy delegation to the European level in the monetary area is about efficiency increases that outweigh potential redistributive effects. Such delegation thus caters for similar or the same types of legitimacy as in the national context, namely output-oriented provisions of legitimacy. From the perspective of this argument, the legitimacy resources of economic governance in the EU are considered as area-specific and being separable on the basis of a functional differentiation of policy tasks.

A second set of arguments basically agrees with the functional importance and democratic legitimacy of delegating monetary policy to an independent central bank in the national realm. However, it takes into account the indirect impact of delegation to a supra-national central bank on those areas that even in the understanding of the aforementioned first set of arguments should stay under the prerogative of member states to ensure appropriate levels of legitimacy in EMU – mainly the area of welfare and social policies. The key argument is that the 'political decoupling' between economic and monetary integration on the one hand and welfare state policies at the domestic level on the other is of a largely artificial nature and generates asymmetries (Hodson and Maher 2002). Since EMU needs to be built on a strongly integrated internal market, national economic policies cannot freely choose their preferred domestic approach but have to adjust to significant regulatory pressure deriving from economic and monetary integration. Scharpf observes that 'compared to the repertoire of policy choices that was available two or three decades ago, European *legal* constraints have greatly reduced the capacity of national governments to influence growth and employment in the economies for whose performances they are politically accountable' (Scharpf 2002: 648; italics in original). In this perspective, the impact of EMU on member states is not of a direct redistributive nature (as the third approach suggests: see below) but rather is indirectly generated through a spillover via regulatory effects. It follows that the legitimacy resources of economic governance in the EU cannot be separated if there are spillover effects from functionally differentiated policy tasks.

A third set of arguments focuses on the direct impact from a single monetary policy on economic output in member states. The main point is that EMU is not only about efficiency increases or regulatory spillover effects but also (and perhaps even more so) about welfare effects across member states. The logic is based on two considerations. First, EMU is not an optimal currency area (i.e. the euro-area is characterized by a considerable heterogeneity of the fundamental economic variables). The ECB's single interest rate is therefore likely to translate into country-specific effects generating higher or lower growth rates (Enderlein 2004a, 2004b). Second, EMU lacks internal adjustment mechanisms that could react to such regionally specific effects of the single monetary policy – such as fiscal redistribution through a system of fiscal federalism<sup>4</sup> or a larger EU budget that could compensate specific regions through grants (as in the US). The implications of this double logic for the assessment of the legitimacy of EMU are far-reaching. If one assumes country-specific effects of EMU, then the current focus of legitimacy on the output side would appear inappropriate. Quite interestingly, such an assessment was explicitly discussed in very early writings on a common currency in Europe (e.g. in the MacDougall Report: Commission 1977) but has largely disappeared from the forefront of policy discussions since then. In this type of reasoning, it is argued that the legitimacy of EMU directly requires either stronger input legitimacy or further political integration to allow for the necessary adjustment mechanisms (McKay 2000, 2005; Siedentop 2001).

It becomes clear that all three types of approaches think differently about the economic effects of EMU. The discussion may thus be largely reduced to differing assumptions as to whether EMU is likely to improve aggregate social welfare on the basis of efficiency increases (i.e. 'Pareto improvements') or whether it is likely to trigger distributive effects that are not balanced by redistributive policy measures.

This difference in assumptions obviously has important implications for the question of the appropriate type of legitimacy. Pareto-improving policies may generally be legitimized on the basis of their result only ('output legitimacy': see above). Welfare-distributing policies, on the other hand, either require a direct type of procedural legitimacy ('input legitimacy') or a very strong collective normative basis (often a common national identity) establishing the readiness of all participants to comply with the redistributive implications of an output-oriented type of policy (one example from national politics is unemployment insurance; from the perspective of this article a more relevant example is fiscal federalism). In the EU, the degree of collective acceptance of possible redistributive implications of EMU is arguably quite low, in particular if one takes into account that such redistribution can hardly be justified as deriving from direct political input and thus bears the risk of being perceived as illegitimate.

It is therefore of considerable importance for the future discussion on the legitimacy of EMU to gain a clearer understanding of the real economic consequences. It is time to move from assumption of the type: 'Suppose that economic and monetary policies conducted in EMU could be regarded as efficient

policies (i.e. would benefit everyone participating in EMU)' (Verdun 1998: 115) to an empirically based understanding of whether that assumption is correct. The following section takes stock of the economic literature already available on that topic and outlines areas for further research.

#### 4. THE ECONOMIC EFFECTS OF EMU

Economic research on the consequences of EMU is still in its fledgling stages. There is simply not enough evidence available to fully assess the issue of efficiency increases versus welfare distribution. Moreover, there are different mechanisms with effects in both directions, implying that an encompassing analysis would have to weigh the relative importance of each. This article can only point towards some of these mechanisms and refer to the emerging set of research that focuses on the issue.

On the one hand, EMU has certainly triggered some welfare-generating effects through the increase of intra-EMU trade relations deriving from the elimination of exchange rate risks in the internal market and the reduction of transaction costs more generally, in particular through the establishment of price transparency. On the other hand, there is also evidence that the 'one-size-fits-all' policy of the ECB has translated into rather significant country-specific effects (and thus created some kind of welfare redistribution). Since the logic of welfare-generating effects has been widely discussed (see Emerson *et al.* (1990) for an excellent overview), I will focus on the less often assessed aspects of the latter effects.

The key mechanism behind welfare distribution in a currency union is the primacy of the real interest rate effect over the real exchange rate effect. As the ECB does not take into account economic developments in single member states but rather targets the euro area as a whole,<sup>5</sup> its 'one-size-fits-all' monetary policy potentially tends to destabilize those domestic cycles whose economic fundamentals are not in line with the euro area average. Member states with higher inflation rates than the euro area average face low real interest rates generating higher rates of investment and consumption. These effects drive up the domestic growth rate beyond its long-term potential, thereby generating even higher inflation rates, further reducing real interest rates, and ultimately generating cyclical overshooting and price bubbles. Similarly, in a context of low inflation and high real interest rates, growth rates are likely to fall below potential growth, thus triggering even higher real interest rates and potentially generating a textbook-type bust cycle.

Prior to the start of EMU, most theoretical analyses of monetary unions assumed that the real exchange rate effect would have primacy over the real interest effect and that domestic stabilization would therefore be generated automatically (see mainly Frankel and Rose 1998). This approach was built on the assumption that domestic prices (and thus also real interest rates) in a monetary union are bound to converge given the mobility of goods and services in the internal market. In EMU, however, a significant share of domestic output

derives from so-called 'spatially fixed factors' such as real estate and heavy machinery, which are not affected by direct price competition (Maclennan *et al.* 1998). Moreover, as analyses of the much more integrated US indicate, regional economic adjustments based on real exchange differentials take a significant amount of time (around four years: see Arnold and Kool 2002).

As initial evidence from the past six years indicates, the relevant economic fundamentals in most euro-area economies have tended to diverge. Looking at cross-country differences in the two crucial elements for the conduct of monetary policy – the inflation rate and the output gap – it becomes clear that there were persistent differentials which generated at least some kinds of redistributive effects. The ECB has published two main studies on inflation differentials (ECB 2003, 2005a) and notes explicitly that 'inflation differentials in the euro-area appear to be very persistent' (ECB 2005a: 63). Member states such as Ireland, Greece, Spain and The Netherlands have experienced significantly higher inflation rates than the euro-area average, and most of them have grown above potential.<sup>6</sup> Germany, on the other hand, has had the lowest inflation and highest real interest rates while remaining far below its potential growth rate. Overall, there is an intriguing positive relationship with a fit of roughly 0.5 between average deviations from euro-area inflation and average deviations from the euro-area output gap in the initial years of EMU (Deroose *et al.* 2004: 10). The International Monetary Fund also finds initial evidence for the primacy of the real interest rate effect over the real exchange rate effect (IMF 2004).

The relationship between the real interest rate effect and the real exchange rate effect has crucial implications for the analysis of legitimacy in EMU. If, as seems to be the case in the first six years of EMU, the primacy of the former over the latter is a structural feature of EMU, then it is quite likely that there will be a trend towards cyclical divergence instead of convergence in the euro-area. Ultimately, there could be a risk that EMU splits into two equally sized groups of countries, one with high growth and high inflation rates, the other with low growth and low inflation rates, with the ECB targeting a zero growth and zero inflation average in the middle. This scenario may become even more likely as new EU members join EMU. In such a context, the ECB's monetary policy would be inappropriate for all EMU members. As such, this would not generate insurmountable problems. As ECB President Duisenberg noted as early as September 1999: 'A single currency does not call for uniform wage developments or uniform economic or social policies in general. On the contrary – where national or regional economic developments are different, this should be reflected in different policy responses and wage developments' (ECB 1999). In other words: fiscal policy and wage-setting should be in charge of stabilizing the domestic business cycle. This would however put significant constraints on the room for manoeuvre of the quoted policy tools in the domestic domain.

In a context of low or negative real interest rates countries can quite easily stabilize their domestic economies by way of fiscal retrenchment and wage

restraint. In a bust context, fiscal policy's room for manoeuvre is limited in a twofold manner. First, at the domestic level, as soon as there is too much deficit spending, economic agents will start anticipating future tax rises and reduce consumption and investment. Second, at the European level, there is the well-known collective action problem related to fiscal free-riding and the famous solution to it: the Stability and Growth Pact. Were the European economy politically integrated and European policy approaches enjoying sufficient legitimacy, the solution would be a radical shift to a full-fledged system of fiscal federalism. The EU budget or some redistributive mechanism would ensure that surplus money from the fastest growing member states would be used to compensate low-inflation and low-growth countries.

Wage-setting cannot provide an effective response either. Although wage restraint can ultimately restore growth through gains in competitiveness, in the short run it depresses domestic demand (mainly consumption) even further. Real wage increases are not a good response either: they would reduce even further firms' profits and depress domestic investment. With regard to the question of the legitimacy of EMU it is crucial to note, however, that even if price adjustments in the euro area were ultimately taking place via adjustments in the real exchange rate, this consequence could undermine EMU support in those countries that would have to experience a decrease in their wages (note that Germany's price competitiveness has increased by about 10 per cent since 1999 mainly as an effect of real wage decreases).

## **5. IMPLICATIONS FOR RESEARCH ON THE LEGITIMACY OF EMU**

Research in economics on the impact of the single currency on economic developments in member states should be given more emphasis in the analysis of legitimacy in EMU. If it was confirmed that inflation and output-gap differentials in EMU tend to increase rather than decrease as a direct consequence of the primacy of the real interest rate effect over the real exchange rate effect, the current EMU framework and its underlying provisions on legitimacy should be reassessed. In particular, new thoughts would have to be given to the future of the fiscal framework and to the possibility to preserve different social and employment models that currently coexist within the euro area. Finally, the question of the ECB's legitimacy could also deserve reassessment.

In the area of fiscal policies, a redistributive impact of the single monetary policy on member states would have far-reaching consequences. An ideal framework for fiscal policy-making in EMU would probably aim at preventing collective action problems while allowing for appropriate fiscal stabilization in the domestic economies. While it could be technically possible to devise such a framework, it would in all likelihood suffer from a considerable lack of democratic legitimacy.

A first approach could be to fully transfer the decision-making authority over domestic fiscal stances to the European level. This would amount to establishing

prescriptive and binding fiscal targets for each member state within a rigid institutional framework (e.g. Fatás and Mihov 2003). This approach might seduce political economists, yet their implementation at the European level would probably create new problems related to a perceived lack of legitimacy. It is unlikely that voters would accept binding fiscal prescriptions from EU bodies – they might remember the aphorism ‘no taxation without representation’. Moreover, the enforcement of such rules would certainly prove difficult.

A second approach could be a shift to a full-fledged system of fiscal federalism (e.g. McKay 2000, 2005; Siedentop 2001). The EU budget, which currently amounts to about 1 per cent of EU GDP, would have to grow dramatically and would have to include some redistributive mechanism to ensure that surplus money from the fastest growing member states be used to compensate low inflation and low growth countries. This solution, which to some extent exists in the US and also in Germany, might have some theoretical appeal but it looks unrealistic at the present juncture; fiscal federalism in Europe could be a long-term target but not a short-term solution.

A third approach could be to return the authority for fiscal policy choices to member states. It would be based on the assumption that the euro-area would be better off in a framework without sanctions and enforcement (i.e. without a rule-based approach to fiscal discipline). Authority over domestic fiscal choices would be fully returned to the member states. Decisions on national fiscal stances, their financing, and their inter-temporal implications (i.e. inter-generational distribution) are at the very core of government’s prerogatives and there are reasons to separate them from direct electoral choice in very extreme cases only (Enderlein 2004a; see also Calmfors 2003).

In the area of social and employment policies, the impact of redistributive effects of EMU could also be far-reaching. The key argument used by the ECB with regard to the persistence of inflation and output-gap differentials in the euro area relates to structural rigidities in labour markets (ECB 2003). Overcoming the destabilizing effects of monetary policy across member states would require more price flexibility, and thus more wage flexibility. As many of the wage-setting systems in the current euro-area member states are built on relatively co-ordinated structures, often involving tripartite social pacts (e.g. Hassel 2003), labour market deregulation for the purpose of allowing EMU to function more effectively would in all likelihood meet resistance and might even trigger rising political contestation of EMU. This also relates to the question whether a variety of capitalisms can coexist in a single currency framework.

Finally, the ECB’s focus on output legitimacy could itself be questioned again. A single monetary policy triggering asymmetric welfare effects across EMU would have to deal with the question of whether and how monetary policy could or should contribute to either avoiding or perhaps even rebalancing such effects would become a key interrogation in discussions on the democratic deficit of EMU – in particular if the ECB faced a ‘ $n = 0$ ’ problem, with its monetary policy being appropriate for the euro area as a whole, but not for any individual member country. The ECB could be asked to drop its ‘one-

size-fits-all' approach and to target a homogeneous sub-region of the euro area (see Enderlein 2005).

## 6. CONCLUSIONS

Six years after the start of stage three of EMU, research in political science should put more emphasis on the economic consequences of monetary unification and check the largely assumption-based analyses of legitimacy in EMU against evidence.

The issue at stake is to determine the right balance between efficiency and legitimacy concerns in EMU. To use the language of cost–benefit analysis: the costs of preserving different levels of economic decision-making in EMU have to be weighted against the benefits of preserving political ownership of decision-making at the lowest possible level.

The solution to that cost-benefit problem is conditioned by the economic consequences of EMU. Does monetary union create redistributive effects and might thus require some majoritarian policy input, or is it possible to reduce EMU to a technical dimension of economic policy-making that allows reliance on a simple output component of legitimacy?

The question of the economic implications of EMU thus directly relates to the interrogation on the right normative standards of legitimacy (cf. Majone 1998). As long as EMU is about welfare increases, the largely non-majoritarian types of governance could indeed be perceived as generating acceptable levels of legitimacy, deriving from the achievement of a desired policy output. However, as soon the integrated monetary framework generates welfare redistribution, the questions of how to achieve a basis of legitimacy on which this redistribution can be based or of how to establish a legitimate correction mechanism rebalancing such effects will have to be put on the research agenda.

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## NOTES

- 1 I am grateful for helpful comments and input by David Howarth, Erik Jones, Nicolas Jabko, Kathleen McNamara, Uwe Puetter, participants at the Chatham House Workshop at SAIS Bologna Center, and the anonymous referees.
- 2 The analysis of the 'democratic deficit' of EMU had started even before the ECB was established and the euro introduced (mainly Verdun 1998). After a strong focus on the ECB itself, scholarly focus on legitimacy issues in EMU spread out to connected areas such as the Stability and Growth Pact (e.g. McKay 2000, 2005; Collignon 2004), the Open Method of Coordination and the Lisbon Strategy (e.g. Hodson and Maher 2001; Scharpf 2002), and the EU Budget (Enderlein *et al.* 2005).

- 3 Jones expresses doubts on the possibility and purposefulness to discuss the legitimacy of a monetary union on the basis of its potential redistributive effects, arguing that such effects cannot be identified *ex ante* or *ex post* – and thus normatively should not (Jones 2002).
- 4 The role of structural and cohesion funds is economically negligible: it amounts to less than 0.4 per cent of EU GDP.
- 5 In one of its first public statements, the ECB notes: ‘The Governing Council of the ECB makes it clear that it will base its decisions on monetary, economic and financial developments in the euro area as a whole. The single monetary policy will adopt a euro-area-wide perspective; it will not react to specific regional or national developments’ (ECB press release, 13 October 1998).
- 6 The Dutch economy, which is one of the most open in EMU, now seems to face stronger real exchange rate effects than real interest rate effects (see IMF 2004: 109)

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