

Southern Europe and the ‘Trade Off’: Architects of European Disunion?

Martin J. Bull

Introduction

The global economic downturn and ensuing Eurozone crisis has focused attention on the traditional ‘periphery’ of the European Union (the ‘old’ southern Europe of Portugal, Italy, Greece and Spain) and revived an age-old fear that Europe, in the words of the *Financial Times*, ‘is economically and politically divided between a northern hard core and a flaky southern fringe’ (quoted in Verney, 2009: 1). Excepting Ireland (which might be described as a ‘periphery’ of the North), the Eurozone crisis stood out both for the public indebtedness of the four ‘old’ south European states and the collapse in confidence of the markets in their capacities to repay those debts.¹ With the Greek government close to default on its debts in the Summer of 2010, the Eurozone, in a first ever bail out of a debt-laden country, negotiated a Euro 110 billion rescue package. This was followed, in late 2010, by Ireland, and, in April 2011, Portugal. This coincided with a re-emergence of the Greek crisis when it was evident that the bail-out was failing, requiring a further Euro 109 billion rescue package on new (easier) terms and conditions described by Jean-Claude Trichet (then head of the European Central Bank), as a form of expected ‘selective default’ of temporary duration; a package, however, that took months to negotiate and was not accepted until November. During this process, the fear of contagion became real as the economies of Spain and Italy came under severe pressure in the Autumn of 2011, with Italy in the subsequent months entering a dramatic crisis of borrowing which took the crisis to an entirely different level (since the size of the Italian economy and its public debt makes it effectively not subject to rescue).

This situation, not unanticipated in some general approaches to European integration (e.g. Dyson and Marcussen 2010), prompted a political crisis at two levels. The first was in

economic governance in the EU, resulting from an inability to provide decisive leadership and management of the Greek and southern European situations and therefore the Eurozone overall. The second level was the domestic. March 2011 saw the resignation of Portugal's Prime Minister, José Sócrates. Shortly after, the Spanish Prime Minister, José Zapatero, announced that he would stand down and elections in November saw the Socialists effectively wiped out on the back of a massive centre-right majority on a programme of austerity. In October the Greek Prime Minister, George Papandreou, having caused a veritable political storm by unexpectedly announcing that the second rescue package he had agreed with the Eurozone leaders would be subject to a referendum before it could become formally accepted (a position that was subsequently rapidly abandoned), was forced to resign and was replaced by an economist, Lucas Papademos. In November, the crisis of market confidence enveloping Italy took with it the Berlusconi government, Berlusconi resigning and being replaced by a technical government headed by an economist and former EU Commissioner, Mario Monti.

This chapter will view the southern European enlargement in the 1980s and the EU-southern European relationship as based on a form of 'trade-off' between 'solidarity' on the one hand and 'sovereignty' or 'discipline' on the other. It will suggest that, while the trade-off appeared to work well until the launch of the single currency in a period which might be described as a 'golden age' in the EU-Mediterranean relationship (e.g. Tsoulakis 2006), in the 2000s it began to deteriorate through a combination of different factors (launch of the Euro, enlargement, reform of cohesion policy, prospective reform of the common agricultural policy, economic crisis) of which the Eurozone crisis became the most critical reflection. This has produced a third level of crisis (between the EU and the southern European states themselves) that could produce new forms of solidarity and discipline embodying much tighter restrictions on economic sovereignty than in the past.

‘Solidarity’ and Southern Europe: Rise and Fall

It could be argued that the southern European democracies, in contrast with their northern counterparts, have been characterised by using European integration in three complementary ways: first, to support and reinforce their (at one time) fragile democracies; second, to obtain ‘solidarity’ through funds to support their economic development; and, third, to help resolve problems and impose fiscal and economic discipline where the political classes proved unable or unwilling (the EU as a welcome ‘external constraint’). In short, the membership of the EU involved a ‘trade off’ which went to the heart of the *raison d’être* of the integration process: democratic consolidation and solidarity (in the form of cohesion) in return for better economic and fiscal discipline, which itself would be assisted through European economic rules. For existing members, entry of the southern European states would be a mixed blessing. On the one hand, it would provide greater security on its southern border, while, on the other, it introduced peripheral economies which might constrain European Community ambitions into being no more than a free trade area; hence, the importance of cohesion and convergence policies to the European framework.

It is therefore no surprise to find that the introduction, development and extension of cohesion policies mirrored the enlargement of the EU (although even in the period before the launch of a regional policy in 1973, Italy benefited from a form of spatial policy through the European Social Fund). The introduction of regional policy and the creation of the European Regional Development Fund (ERDF) that followed two years later was a product of the deal negotiated over accession of the UK and Ireland. The Mediterranean enlargement of the 1980s (Greece – 1981, Spain and Portugal – 1986) led to the adoption of the Integrated Mediterranean Programmes, larger funding and the creation of a Cohesion Fund. This fund began to operate in 1993, the budget rising to about 3 per cent of the overall EU budget by 1999, with the 1995 Scandinavian enlargement leading to the adoption of further objectives

particularly relevant to these countries (regions with sparse populations). In the course of the new Millennium the Fund was expanded and reformed again (in relation to budgetary redistribution and policy substance) with the entry of new members from the former communist states in 2004 and 2007. By 2010 cohesion policy was the largest item in the EU budget, surpassing even the Common Agricultural Policy (Begg, 2010: 77).

As Begg (2010: 78) argues, cohesion (and specifically territorial cohesion), while ‘tending to be equated operationally with regional divergence in economic indicators, such as GDP per head, and (in a less easily calibrated way) social conditions is ultimately a political notion.’ Its political nature was seen not just in its nature as a goal (that the nation-states should ‘converge’) and in the negotiations at different phases that led to its implementation, but also in convergence being a fundamental part of the longer-term goal of economic and monetary union. This was in the form of a *quid pro quo* which was made explicit as early as 1973 in a European Communities *Report on the Regional problems in the Enlarged Community* where it was stated that: ‘No Member States can be expected to support the economic and monetary disciplines of Economic and Monetary Union without Community solidarity involved in the effective use of such instruments; equally Member States must be prepared to accept the disciplines of Economic and Monetary Union as a condition of this Community support’ (quoted in Manzella and Mendez 2009: 9). For this reason, despite the fact that cohesion policy, over the years, developed multiple goals that were not easily reconcilable (equity, solidarity, sustainable development, competitiveness, good governance) the redistributive bias towards less prosperous states was consistent, and led critics to argue that the policy, in fact, amounted to little more than a form of ‘side payment’ to certain countries to ‘buy’ their support for other objectives: ‘In this...view, the Cohesion Fund could be seen as the price extracted by the (then) four cohesion countries –

Greece, Ireland, Portugal, Spain – for acquiescing in the establishment of economic and monetary union’ (Begg 2010: 82).

If this was a ‘trade off’ there can be little doubt that, at least in the initial period, the southern European states reaped its benefits. Their fledgling democracies were consolidated under the EU umbrella, and their economies underwent a process of opening out and change, supported by significant financial assistance from agricultural, regional development, training and cohesion programmes. Empirical analyses up to 2000-01 concluded that convergence of the Mediterranean countries with the European average had occurred (notably after 1986) and that structural funds had had a clear impact on this process (Beugelsdijk and Eijffinger 2005; Barry 2003).

In the Millennium, however, the issue of solidarity with southern Europe was gradually (if not inevitably) called into question, largely as a result of the enlargement to central and Eastern Europe that occurred. In 2004 eight central and east European former communist countries (Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia) and two more Mediterranean countries (Malta and Cyprus) entered the EU, and 2007 saw the addition of Bulgaria and Hungary. The accession of these twelve countries transformed the nature of the EU and specifically its periphery, widening regional disparities considerably. In 2005, the fourteen regions with the lowest GDP per head were from three countries: Bulgaria, Poland and Romania. Moreover, countries such as Poland entered with large agriculture sectors. The Cohesion Fund was reformed (in line with the Lisbon Agenda’s aims) for the period 2007-13 and, while southern European states were still allocated substantial allocations of structural funds, the likelihood of this into the post-2013 period is unclear. Depending on how the funds are allocated, countries such as Italy and Spain may find themselves in the positions of being net contributors. More generally, European regional policy faces dilemmas in relation to member-state expectations which may not bode well for

southern Europe, as the debate on the future of structural funds suggests. For the least prosperous Member States, convergence is about raising GDP per head nationally, and the most effective method is to invest in growth poles with the greatest returns (e.g. in capital regions such as Warsaw or Bratislava); for more prosperous Member States, the concern is more with territorial imbalance both across Europe and specifically within their own states. Consequently, ‘an especially contentious issue is how to interpret the Treaty commitment to cohesion for richer states; or to put the question starkly: should the EU try to deal with regional problems in eastern Germany, northern England or the Mezzogiorno, or should they be left to the Member States?’ (Begg 2008: 8). Finally, 2013 will mark the year when the Member States which acceded in 2004 and 2007 will be entitled to full support from the Common Agricultural Policy (the European Council having decided on this delay back in 2002). In short, by 2011 solidarity with the European southern periphery, as traditionally defined and implemented, was becoming a thing of the past.

‘Discipline’ (or Restricted Sovereignty) and Southern Europe: Rise and Fall

If ‘solidarity’ was part of a trade off the other side involved accepting new economic rules related to sound money and financial discipline. These were first represented in the five Maastricht Criteria which had to be met for any nation-state to participate in the single currency. The benefits involved in such a trade off were: removal of exchange rate uncertainty; greater transparency in relative prices across national borders; reduction of transaction costs; lower inflation; and falling risk premia in interest rates, leading to long-term gains in trade and growth and a consolidation of public finances. The challenges involved accepting restrictions on one’s economic sovereignty, specifically in the form of acceptance of an economic regime which ruled out nation-states recovering loss of competitiveness through devaluing the exchange rate, and made sound public finances essential. The trade off was hardly questioned in southern Europe, especially as it was

recognised that a model of the economy based on competitive devaluations (which fuelled inflation and further devaluations) and large public sector deficits was unsustainable in the long-term (Bardone and Reitano 2009: 37-8). Yet, while the first would be imposed by the single currency itself (i.e. a sovereign currency was removed), the second required action by the nation-states both *before* (and as a condition of) entry to the single currency and *after* as an economic model based on sound finance.

In view of the likely benefits, as well as the negative implications of being left out of the 'core' single currency group, the southern European states were more than willing to accept the external constraint in the 1990s and to use it domestically (even by technocrats against hesitant politicians) to drive through the measures necessary to bring about fiscal adjustment (Dyson and Featherstone, 1996). Consequently, and against expectations, all four of the south European states met the Maastricht criteria and entered the single currency (Italy, Spain and Portugal in 1999 and Greece in 2001). Yet, the nature of this achievement did not in and of itself guarantee that these countries' fiscal adjustment would continue into the post-entry phase, for three reasons.

First, rigid as the Maastricht criteria were, they 'gave more emphasis to fiscal consolidation rather than fiscal sustainability' (Blavoukos and Pagoulatos 2008: 233) and such consolidation could be achieved through methods (especially raising tax revenue) which avoided the more difficult to achieve structural reforms essential to the foundation for sustainability in the future. Moreover, the one criterion which might have provided a better foundation for future progress (reducing the public sector debt to 60% of GDP) was, in the run-up to the deadline relaxed to 'a steady decrease of the public debt rate' (ibid., 250).

Second, since there was no supra-national prescription for the means by which fiscal consolidation should be achieved it was left to the choice of the individual nation-states to

develop their own approaches. While existing evidence suggested that ‘budget consolidations relying too heavily on the revenue side by raising taxes rather than on the expenditure side by cutting spending are likely to be successful and sustainable’ (ibid., 234), only in the case of Spain was a programme of fiscal consolidation based on a reduction in government expenditure and extensive structural reform (pensions reforms, labour market reforms, welfare reforms, privatisations) (ibid., 241-42; Royo 2009). In contrast, Portugal, Greece and Italy successfully achieved fiscal consolidation primarily through increasing tax revenue (and at least in one case through some creative accounting²) with little or no reduction in government primary expenditure and limited structural reforms – those which were begun (in Italy and Greece) remained partial and incomplete (Blavoukos and Pagoulatos 2008: 236-41; Torres, 2009; Pagoulatos and Triantopoulos 2009; Bardone and Reitano 2009).

Third, once participation in the single currency was secured and once the currency was launched, the rules of the game changed somewhat. The (spirit of the) pre-entry implications about sustainability were meant to be enforced through the Stability and Growth Pact (SGP)’s Excessive Deficit Procedure for those countries in breach of the 3% rule, and, in 2002, Portugal fell foul of this and had to enact urgent measures. However, shortly after, with the French and German economies similarly struggling but arguing for more flexibility in the policy, the rules effectively became ‘softer’ and the credibility of the SGP was undermined, thus reducing the pressure on the southern European states to continue with fiscal consolidation.

As a consequence, fiscal consolidation was relaxed in Italy, Greece and Portugal, and structural reforms, where they had been commenced, were given less priority (where not abandoned). This situation was reflected in both the primary balances (in the cases of Greece and Portugal dropping into deficit for some years) and general governmental balances (with all three either breaching or coming very close to breaching the Stability Pact’s threshold of

3% of GDP), situations usually met through one-off corrective measures. In contrast, Spain managed to run consistently healthy surplus primary balances and to keep within the Stability Pact's threshold, actually producing surpluses in two years (Blavoukos and Pagoulatos, 2008: 242-44). Public debt as a percentage of GDP remained largely unchanged in Greece, Portugal and Italy, while it was brought down in Spain.

At the same time, there were two common effects of operating within a single currency. First, due largely to high rates of inflation and the strengthening of the Euro, there was a decline in their competitiveness (which could not be offset through devaluing the currency), reflected in a worsening state of their current accounts. The average figures for the decade 1999-2008 (in per cent of GDP) were, for Spain, -5.90 (against -1.73 for the previous decade), for Greece -8.75 (against -3.28), for Italy -1.26 (against 0.49) and for Portugal -9.13 (against -2.01), with the average for the Euro area 0.31 (against 0.26 for the previous decade) (Le Cacheux 2010: 51). In theory, this should have led to a reduction in wage rates and the development of a more flexible labour market in order to maintain the GDP growth rate and employment levels. However, second, the single nominal interest rate set by the European Central Bank (ECB) for all Euro area countries brought down real interest rates (i.e. accounting for inflation), helping to boost economic growth by making investment and debt less costly (and providing an alternative to the enforcement of wage restraint). The average real long-term interest rates for 1999-2008 were 1.16 in Spain (against 5.03 for the previous decade 1989-98), 0.66 in Greece (against 5.58), 2.22 in Italy (against 6.18) and 1.55 in Portugal (against 6.76), and were 2.2 for the Eurozone as a whole (Le Cacheux 2010: 51). This meant that, despite the loss of competitiveness, growth was able to be maintained through easier credit (reinforced by liberalisation of banking regulations under the single market programme) and more manageable deficits. Nevertheless, Italy and Portugal were sluggish compared with Greece and Spain, where average growth rates for the decade 1999-

2008 were 3.54% in Spain and 4.15% in Greece (in contrast with 1.70% in Portugal and 1.36% in Italy, and an average growth rate of 2.12% for the Euro area overall) (Le Cacheux, 2010: 50).³ However, gross national income showed convergence with the Euro area average in these years for Spain, Greece and Italy, and unemployment fell and was kept at the Euro area average, except for Spain (which nonetheless had come from a high figure of 20% in the mid-1990s)

In short, this combination (non-structural approach to fiscal consolidation, relaxing of the rules and easy credit) laid the basis for increased (or over) borrowing by governments, banks and households and thus a rise in demand and potential overheating of the economies. In Blavoukos and Pagoulatos' words (2008: 242), 'Once membership was achieved, the ... [four south European states] ... could potentially free ride on the common currency's credibility without being individually penalized by financial markets.' Low interest rates contributed to a boom based on private consumption (and in countries undergoing rapid growth such as Spain, a housing bubble), masking at the same time other economic weaknesses (low productivity, growth based in areas not exposed to international competition, decline in competitiveness, high labour costs, family indebtedness, unresolved structural issues). The Euro, moreover helped to sustain severe demand imbalances through German banks lending to the southern European states and creating demand for its own exports. This exporting of credit dependence increased the divergence between German surpluses and south European deficits (Featherstone 2011: 200). As Tombazos (2011: 34) argues, '....the euro, in the short term encouraged the expansion of some "peripheral" economies, where the markets failed sufficiently to enforce "obligatory reforms" in the labour market and in the public sector...The financial markets, instead of imposing "discipline", displayed a greater propensity for immediate and uncertain profits'. The four

South European states were therefore ill-prepared to cope with the world economic downturn in 2008 and the sovereign debt crisis which began in 2010.

Crisis and Southern Europe: New Forms of Solidarity and Restrictions on Sovereignty?

The sovereign debt crisis of southern Europe was dramatic, at the heart of which was a collapse in market confidence in their capacities to repay their public debts, with Greece, Portugal (and Ireland) requiring bail outs, and the Greek bail out failing and requiring, therefore, a second. The management of the crisis by EU and Eurozone leaders was characterised by a mixture of weakness, division and procrastination, thus exacerbating the financial plight of the Eurozone (Underhill 2011). The first Greek bail-out, when it came, failed largely because it loaned Greece €110bn at *market rates* as a means of tiding the country over until it could borrow on the markets again. The delay on negotiating the second-bail out, the evident divisions in the German political position combined with the effects of successive downgrades of the crediting ratings of the four southern European countries by the international ratings agencies (Standard & Poors, Moody's, Fitch) were a recipe for a further collapse of confidence, as well as for contagion. Spain and notably Italy were dragged into difficulties, Italy's situation changing the whole nature of the debate. The run on the Italian markets began in August 2011 and was characterised by dramatic increases in the 'bond spread' (the difference between the German and Italian ten year bond yields) which touched historical highs in November (in November the Italian bond yield surpassed 7%, the threshold at which bail outs for Greece and Portugal had been necessitated) and suggested that the markets had serious doubts about Italy's capacity to repay its public debt.

European and international elites responded to the crisis in two ways, both of which were attempts in vain to reassure the markets. The first was to try to prevent contagion by transforming the bail-out fund into a much more ambitious financial instrument (European

Financial Stability Facility - EFSF) which would have the power to buy bonds of struggling debtor countries, to take pre-emptive action before a debt crisis developed too far and to provide loans to Eurozone countries to support their banks. Yet, once the crisis reached an economy the size of Italy's (where its public debt amounted to approximately a third of all Eurozone debt) it was clear that no EFSF 'firewall' would be big enough for that. Worse, by late November contagion was beginning to affect both France and Germany, the core countries of the Eurozone, France being warned by the credit-rating agency Fitch that it could lose its triple A credit rating if the debt crisis deepened, and Germany, on 23 November, finding investors shunning its bonds, as it was forced to retain nearly €2.4 billion of a planned €6 billion sale (and subsequently faced with yields on its ten year bonds higher than those of the UK).

The second response was to drive through a spate of emergency austerity budgets at the national levels, these involving a mixture of tax increases and draconian cuts to the public sector. These emergency budgets were not only demanded of the 'errant' states by the EU, ECB and International Monetary Fund (IMF), but were also closely overseen. In situations where national governments appeared incapable of carrying them through (Greece, Italy), the lack of political confidence at the European and international levels in them was made sufficiently apparent as to exacerbate the country's market position, the governments fell and were replaced by technocrats. Although there were few alternatives, critics were quick to condemn the EU for 'rushing to plunge the euro area peripheral economies into recession...' (Tombazos 2011: 34), which, of course, would exacerbate and not alleviate their public debt problems.

It is clear that the depth and protracted nature of the crisis was not just caused by the 'errant' behaviour of the southern European states (as well as Ireland) and EU 'mismanagement' of the crisis. It was also an inevitable consequence of structural flaws in

the Eurozone edifice, and especially those related to the nature and management of sovereign debt. Adair Turner (2011), adopting Charles Goodhart's distinction between 'fully sovereign debt' (where fully sovereign bonds are issued by a sovereign authority which is also a currency issuing authority), and 'subsidiary sovereign debt' (where the bonds are issued by political units which are not themselves currency issuing authorities) argues that the Eurozone nations were, with the single currency, transformed from fully to subsidiary sovereign bond issuers. However, the institutional precautions necessary to offset the greater risks this change embodied were not acted upon. Fully sovereign debt can, at the extreme, be monetised. This carries with it risks (inflation, currency depreciation) which are of a more manageable nature than default. Subsidiary sovereign debt, on the other hand, carries with it a nominal and real repayment risk, and where, as in Southern Europe, situations arise where the nominal debt cannot be re-paid, it cannot (under the existing arrangements) be monetised. The European governance framework separates responsibility for monetary stabilisation (European level) from fiscal, invariably distributive policies (at Member State level). While this placed it in a position to manage the 2008-09 crisis (which was about financial liquidity) it could not deal with the 2010-11 sovereign debt crisis where Member State autonomy had prevailed (Shelkle 2011: 381-2).⁴ The Eurozone model, therefore, was highly ambivalent about 'bail outs' of errant states, excluding them on the one hand but failing to provide any effective instruments for dealing with those states on the other: 'the logic was of stability increasing the credibility of the arrangements' (Featherstone 2011: 202). Finally, to exacerbate matters, the banks were incentivised by regulation to become major investors in sovereign bonds, making it easier to continue issuing those bonds until unsustainable levels were met and thus increasing the risk to the banking system as a whole.

Yet, if these problems suggested obvious solutions, they were far from easy to introduce, largely for political reasons. The idea of Eurobonds and the European Central

Bank acting as the lender of last resort, proposed formally by the President of the European Commission, José Barroso, was flatly rejected by Germany both for fear of inflation (embedded in the German psyche from the 1920s) and ‘moral hazard’ (that southern European nations would fear indebtedness even less in the knowledge that their debts would in the end be bought out by somebody else). The crisis therefore raised a fundamental issue of EU governance which the richer nations (and specifically, Germany) had been avoiding until then: whether EMU should be a ‘debt union’ based on solidarity and burden-sharing, in which the richer nations would guarantee the borrowings of the poorer nations. It had proved elusive in the original model, Dyson describing ‘the prospect of people being asked to make sacrifices for others with whom there was a weak sense of identity’ as the Achille’s Heel of the EU (cited in Featherstone 2011: 211). The dilemma, therefore, was to find an appropriate set of arrangements which would satisfy different member-states and the electorates their governments represented. Such arrangements could only be based on closer ties between the Eurozone economies entailing new forms of solidarity in exchange for restrictions on national economic sovereignty e.g. binding limits on borrowing. The profligacy of the southern European states, in short, had exposed the cracks in the Eurozone edifice and was forcing a significant reform of European economic governance as a consequence.

Yet, such moves would not only have to overcome the deep reservations of the peoples of the richer nations towards burden-sharing in relation to southern Europe, it would also have to address reservations from the periphery, for whom it was not clear how acceptable European ‘tutelage’ (depending on the form it took) would be in the long-term. For Tombazos (2011: 41), ‘Today the feeling in Greece is that the country is now under occupation. The IMF, the European Commission and the ECB not only dictate policy, but also oversee its implementation. More generally, the attempt to tighten the supervision of nation states by European bodies is perceived in Southern Europe as an attempt of the

European core to place the European periphery under check.’ The Italian government, for example, overseeing one of the largest economies in the world, was, in the latter part of 2011, essentially placed under a form of EU ‘tutelage’, being ordered to bring forward by a year its goal of balancing the budget and being informed what measures had to be incorporated in order to do so. And Berlusconi’s supporters did not hide their feelings that the centre right government had effectively been forced out of office through a collapse in confidence not just of the markets but of Chancellor Merkel, President Sarkozy and other European elites.

This raises the critical issue of whether we may be witnessing the beginning of an unexpected ‘falling out’ between the peoples of southern Europe and the European Union, and this during a time when Europe generally is undergoing a shift in support for the EU from a ‘permissive consensus’ to a ‘constraining dissensus’ (Hooghe and Marks 2009). The peoples of Southern Europe have (albeit with periodic exceptions, notably in relation to Greece) been fairly reliable and consistent supporters of the integration process. The most recent detailed analyses of Euroscepticism in southern Europe largely pre-dated the economic crisis (Verney 2011a), and concluded that, in the period until then (2008-09), southern Europe did make up the mainstream drift towards a ‘constraining dissensus’. Nevertheless, the analyses also revealed evidence of more nuanced forms of Euroscepticism in the past, a rise in Euroscepticism in the 2000s and relatively high percentages of those in some countries currently indifferent to, or ignorant, about the EU. These findings suggested that there is the potential for negative views about the EU to grow (Verney 2011b). The last Eurobarometer survey on popular attitudes to the Euro (2010) revealed that, apart from France, only the four southern European states fell below the Eurozone average of those who thought that having the Euro was a good thing for Europe, even if the percentages were still high (from 61% in Portugal to 65% in Italy against an average of 65% for the Eurozone as a whole) (Eurobarometer 2010: 10). True, the violent protests that have been witnessed in countries

such as Greece and Italy have, until now, been directed primarily against the failings of their national governments. Yet, the severe austerity is effectively being imposed on these countries from above and it is not inconceivable for the protests to be directed against the EU in the future, the more the supra-national level concerns itself not just with monitoring national governments' finances but regulating, if not dictating, their budgets. By the end of 2011, therefore, the southern European states faced a watershed: having lost the trust of their Eurozone counterparts they could no longer expect to receive European solidarity without increased externally-imposed discipline and restrictions on their economic sovereignty.

Conclusion

The 'golden era' that characterised the Mediterranean enlargement and the Mediterranean-EU relationship of the 1980s and 1990s has disappeared. The 'trade-off' between 'solidarity' and 'discipline' appeared to function well until the launch of the single currency, under the guise of the EU as an 'external constraint'. However, the particular mode of economic governance that developed under the single currency was (even if unwittingly) predicated on the idea that the 'external constraint' had, somehow, been 'internalised'. The flexibility this allowed, combined with the new challenges of operating in a single currency led the southern European states into a situation where they were poorly prepared for the world economic downturn that began in 2008. The result is a crisis in the EU-southern European relationship whose resolution has pulled the EU towards two opposing extremes: either towards some southern European states defaulting and exiting the Euro; or towards a debt union and full supranational economic governance. Whether a middle of the road route is possible ('a fudge, well short of fiscal union' – Manchau 2011) is possible remains open to question, but all

three scenarios signal a dramatic change in the EU-southern European relationship, and the definitive end of the golden era.

References

Bardone, L. and V. E. Reitano, 'Italy in the Euro Area: The Adjustment Challenge', in M. Buti (ed), *Italy in EMU: The Challenges of Adjustment and Growth* (Basingstoke: Palgrave).

Barry, F. (2003), 'Economic Integration and Convergence Processes in the EU Cohesion Countries', *Journal of Common Market Studies*, 41: 5: 897-921.

Begg, I. (2008), 'Cohesion in the EU', *CESifo Forum*, 1/2008: 3-9.

Begg, I. (2010), 'Cohesion or Confusion: A Policy Searching for Objectives', 32: 1, January: 77-96.

Beugelsdijk, M. and S. C. W. Eijffinger (2005), 'The Effectiveness of Structural Policy in the European Union: An Empirical Analysis for the EU-15 in 1995-2001', *Journal of Common Market Studies*, 43: 1: 37-51.

Blavoukos, S. and G. Pagoulatos (2008), 'The Limits of EMU Conditionality: Fiscal Adjustment in Southern Europe', *Journal of Public Policy*, 28: 2, 229-53.

Dimitrov, V. (2012), 'The New Member States from Central and Eastern Europe: Passive "Good Citizens" of the Union', in J. Hayward and R. Würtzel (eds), *European Disunion: Between Sovereignty and Solidarity* (Basingstoke: Palgrave).

Dyson, K. and K. Featherstone (1996), 'Italy and EMU as a "vincolo esterno": empowering the technocrats, transforming the State, *South European Society and Politics*, 1 (2), Autumn.

Dyson, K. and M. Marcussen (2010), 'Transverse Integration in European Economic Governance: Between Unitary and Differentiated Integration', *Journal of European Integration*, 32: 1, January: 17-39.

Eurobarometer (2010), *The euro area 2010. Public Attitudes and Perceptions. Analytical Report* (Brussels: European Commission).

Featherstone, K. (2011), 'The Greek Sovereign Debt Crisis and EMU: A Failing State in a Skewed Regime', *Journal of Common Market Studies*, 49 (2): 193-217.

Hooghe, L. and Marks, G. (2009), 'A post-functionalist theory of integration: from permissive consensus to constraining dissensus', *British Journal of Political Science*, 39: 1-23.

Le Cacheux, J. (2010), 'How to Herd Cats: Economic Policy Coordination in the Euro Zone in Tough Times', *Journal of European Integration*, 32: 1, January: 41-58.

Pagoulatos, G. and C. Triantopulos (2009), 'The Return of the Greek Patient: Greece and the 2008 Global Financial Crisis', *South European Society and Politics*, 14: 1, March: 35-54.

Manchau, W. (2011), 'Eurobonds and fiscal union are the only way out', *Financial Times*, 18 September.

Manzella, G. P. and C. Mendez (2009), 'The Turning Point of EU Cohesion Policy', Report Working Paper, ec.europa.eu/regional-policy, accessed 12 May 2011.

Pagaloutos, G. and C. Triantopoulos (2009), 'The Return of the Greek Patient: Greece and the 2008 Global Financial Crisis', *South European Society and Politics*, 14 (1): 35-54.

Royo, S. (2009), 'After the Fiesta: The Spanish Economy Meets the Global Financial Crisis', *South European Society and Politics*, 14 (1), March: 19-34.

Schelkle, W. (2011), 'A tale of two crises: the euro area in 2008/09 and in 2010', *European Political Science*, 10 (3), September: 375-83.

Sitter, N. (2012), 'Scandinavian Exemplarity', in J. Hayward and R. Würtzel (eds), *European Disunion: Between Sovereignty and Solidarity* (Basingstoke: Palgrave).

Tombazos, S. (2011), 'Centrifugal Tendencies in the Euro Area', *Journal of Contemporary European Studies*, 19 (1), March: 33-46.

Torres, F. (2009), 'Back to External Pressure: Responses to the Financial Crisis in Portugal', *South European Society and Politics*, 14 (1), March: 55-70.

Tsoulakis, L. (2006), 'The JCMS Lecture: Managing Diversity and Change in the European Union', *Journal of Common Market Studies*, 44: 1: 1-15.

Turner, A. (2011), 'Debt and deleveraging: Long term and short term challenges', Presidential Lecture, 21 November, Centre for Financial Studies, Frankfurt: http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2011/1121_at.shtml (accessed 24 November 2011).

Underhill, G. (2011), 'Paved with good intentions: global financial integration and the eurozone's response', *European Political Science* 10 (3), September: 366-74.

Verney, S. (2009) 'Flaky Fringe? Southern Europe facing the financial crisis', *Southern European Society and Politics*, 14:1: 1-6.

Verney, S. (2011a) (ed), 'Euroscepticism in Southern Europe: A Diachronic Perspective', Special Issue, *South European Politics and Society*, 16 (1), March.

Verney, S. (2011b), 'Euroscepticism in Southern Europe: A Diachronic Perspective', *Southern European Society and Politics*, 16: 1, March: 1-29.

Notes

The author is grateful to Leonardo Morlino for his suggestions and advice.

¹ And in stark contrast with other EU 'regional' groupings, albeit partly (but not only) because of the fragmentation within these groupings between Euro and non-Euro countries (see Dimitrov 2012 and Sitter 2012).

² An audit conducted in 2004 by a former Finance Minister, George Alogoskoufis, concluded that Greece had never, in fact, met the Maastricht criterion of the public deficit being within 3% of GDP (Featherstone 2008).

³ The Portuguese economy, in fact, experienced a small boom before entering the single currency, based also on increasing indebtedness (Torres 2010: 56-9).

⁴ This heightened risk explains why, even though the aggregate Eurozone percentage of debt to GDP was, in 2011, lower than for the UK, US or Japan, the average interest rate paid on its debt was much higher.