

Germany and Europe: A very federal formula

di Quentin Peel

The 20th anniversary of the signing of the Maastricht treaty passed largely unremarked on Tuesday as the crisis in the eurozone preoccupied governments and the financial markets. Yet even as negotiations in Athens edged towards Thursday's agreement on rescheduling the Greek debt burden, the pact that laid the foundations for Europe's single currency was heralded by Chancellor Angela Merkel in a speech to students.

In an unusually appropriate setting – surrounded by Greek antiquities in the reconstructed Neues Museum in the centre of Berlin – Germany's normally cautious leader spelt out elements of her vision on how to solve the eurozone crisis long-term.

Much was familiar. Eurozone countries needed both budget austerity to reduce their debts and structural reforms to boost their competitiveness and employment, she said. They needed to recreate trust in their finances and in each other. Then she turned to the construction of the EU. "Without doubt, we need more and not less Europe," Ms Merkel declared. "That's why it's necessary to create a political union, something that wasn't done when the euro was launched."

She went on to suggest that this political union – "there will still be a lot of argument about it" – would be organised around the existing bodies of the soon to be 28-nation bloc. The European Commission, the Brussels-based executive arm, would – with competences transferred to it by nation states – act as a government reporting to a strong European parliament. The European Council of national heads of state and government would function as a second legislative chamber; the European Court of Justice would be the highest authority. "We believe that we will stand better together if we are ready to transfer competences step by step to Europe," she said.

"That is just about as federalist as you can get," says Henrik Enderlein of the Hertie School of Government in Berlin. "Is she serious? That is the real question. She is very good at the rhetoric. But I do take it seriously that she wants to move towards political union."

It is a vision that could cause alarm in France, Germany's closest European ally, even as Ms Merkel has announced her intention to campaign for the re-election of Nicolas Sarkozy as French president. Mr Sarkozy does not want the Commission to become Europe's government: Paris wants that job to remain with the European Council, where the nation states rule supreme. He is unlikely to be alone.

Hers is a vision that would also imply dramatic changes in the distribution of power between Brussels and member states. Such a big change might require a referendum in Germany itself – something every chancellor since the second world war has sought to avoid.

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But what does “political union”, a term abandoned in recent years by most EU leaders for fear of alarming their increasingly eurosceptic electorates, really mean? The detailed vision of Ms Merkel – the continent’s dominant political leader, widely seen as having the future of the euro in her thrall – remains unclear. She talks of a “fiscal union” but her definition sounds like fiscal discipline. She insists there should not be a “transfer union” in which Germany guarantees the borrowings of its partners.

From Washington to Westminster, political leaders complain that they understand neither the tactics nor the strategy of the German government and its chancellor in the crisis. They see conflicting signals, ranging from a rigid insistence on budget discipline to a willingness to turn a blind eye to the unorthodox monetary policies of the European Central Bank. Ms Merkel says she will “do what it takes” to save the euro, but then constantly seems to block the view of most partners on the need for a bigger “firewall” to prevent contagion.

Part of the problem lies in the constant debate within Germany, and within Ms Merkel’s centre-right government, about the way forward. A confused communications strategy tries to reconcile the demands of the competing ministries of finance, foreign affairs and the chancellor’s office itself. And Ms Merkel, by training a physical chemist, plays at political alchemy to reconcile a domestic constituency that is essentially pro-European but is decidedly hostile to bailing out the eurozone’s debtor nations.

In countries such as Greece and Spain, undergoing ferocious austerity programmes to meet German-led demands to reduce their public debt and budget deficits, the chancellor is caricatured as a jackbooted bully. Yet at home she is seen as cautious, dedicated to consensus, a leader who is both pragmatic and determined, and a natural conciliator: she is the most popular politician in the country and her Christian Democratic Union is well ahead of its rivals in the polls.

“I don’t think she is a visionary, and we don’t want a visionary in Germany,” says Almut Möller of DGAP, a German foreign policy institute. “She has no institutional vision.”

Yet the chancellor’s advisers say that has changed. The turning point was last July. “Two things came together,” says Ulrike Guérot of the European Council on Foreign Relations, a think-tank. The first was Italy, which came under attack from financial markets almost as soon as EU leaders had finalised an agreement aimed at promoting calm. Then, pro-Europeans in the CDU warned that Ms Merkel was in danger of losing the debate in Germany. “They said: we are losing our constituency in the centre and not gaining anything on the right.”

There was also a realisation among party officials that the chancellor would have to take a series of tough bills through the Bundestag to pay for eurozone rescue plans and needed a narrative to persuade her sceptical supporters. “For the Germans the message has to be: if we are going to have a transfer union anyway, we need a political union to control things,” says Daniela Schwarzer of SWP, the German institute for international and security affairs.

Close advisers confirm that the chancellor has indeed been thinking long and hard about reforms of the EU that go far beyond the recent “fiscal compact” of budgetary rules agreed as an intergovernmental treaty last month by 25 of the 27 members.

At a recent meeting with three fellow European leaders at Schloss Meseberg, her baroque government retreat outside Berlin, she urged them to spell out their ideas of how the EU should look in 10 years’ time. To her obvious frustration, they were all much more focused on the present crisis. Yet she gave only hints of her own thinking in a series of statements and speeches. “She is

quite clever in not spelling it out,” says Joachim Fritz-Vannahme of the Europe’s Future programme at the Bertelsmann foundation. “She is playing chess. She knows what she has to do. She knows it will take time. And she knows it will be very controversial.”

It is, he adds, “a vision for the transformation of the EU – or at least the eurozone – in a very short time frame: three to five years. Political union is not a very clear concept. She doesn’t dare speak about a United States of Europe, but she is thinking about what has to be in it.”

Conversations with senior officials and political analysts in Berlin reveal a lot more detailed thinking than Ms Merkel has demonstrated publicly.

The “fiscal compact” is seen as just a first step to make the rules of budget discipline genuinely binding on all eurozone members: they must put a commitment to balanced budgets into their national constitutions, or equivalent legislation. In exchange, Germany proposed and is the principal financier of the permanent European Stability Mechanism, due to start operating in July. It is in effect a €500bn European monetary fund to deal with debt crises in the 17-member monetary union.

The rules agreed would set ceilings for national spending and borrowing but would not interfere with tax and spending choices. But the next phase contemplated in Berlin would be more intrusive: co-ordinating or even harmonising taxes, with budgets supervised by the Commission and all eurozone finance ministers. They would be able to insist on certain spending priorities, to ensure competitiveness and growth targets were met and that adequate funds were devoted to areas such as education. It would mean a big transfer of sovereignty away from national capitals and parliaments.

At that stage, many leading German officials and politicians privately concede, the introduction of jointly guaranteed eurobonds might be possible, even irresistible. The concept would provide cheaper financing for the most indebted eurozone states. It is still fiercely resisted in Ms Merkel’s CDU and by the liberal Free Democrats, junior partner in the coalition. The chancellor herself sounds sceptical. But Wolfgang Schäuble, her passionately pro-European finance minister, has always said “not yet” rather than “never” to the bonds. (Both the main opposition parties, the centre-left Social Democrats and the environmentalist Greens, are in favour.)

Yet eurobonds and a loss of budgetary autonomy would be likely to fall foul of the constitutional court. “Any loss of sovereignty would be problematic” for the court, says Ms Schwarzer. “It would probably mean having a referendum. But the big problem for Germany isn’t just the constitutional court: it’s also Paris.”

Confrontation with France could come in a third phase of EU reforms, in which the Commission would become the real European economic government and the European Council would become a legislature alongside the European parliament. “The reality is that Germany is starting this reflection and other countries are not,” says Ms Guérot. “France has to have the debate. They are not ready to give up the Fifth Republic.”

For Ms Merkel it is a question of the democratic legitimacy of the entire integration process. She sees a dangerous disconnection between national politics, and national parliaments, and the European parliament. Her party wants to see the Commission president directly elected.

The chancellor knows perfectly well that these are profoundly important political issues, and hugely controversial. But she has decided that only with such fundamental reforms can European monetary union survive.

The good thing for Germany, says Mr Fritz-Vannahme, is that she is not a bully – in spite of the Mediterranean caricatures. “She is a lady, but not an iron lady,” he says. “She is also a scientist, and that is perhaps part of her problem. For politics is not an exact science.”