The Eurozone and Brexit

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## 1. Introduction

In this Chapter, we explore the evolution of the Economic and Monetary Union (EMU) and argue that there was little possibility that an effective currency union can be achieved given the economic, historical, and cultural differences between the nations involved and the influence of the emerging neoliberal ideology in the 1980s, which created a dysfunctional architecture that appeased those differences.

We also consider where the more recent decision by the British government, following their June 2016 Referendum, to leave membership of the European Union fits into this narrative.

Initially we take an historical approach to understand the difficulties that nations with very different economic structures and a lack of cultural solidarity face when they try to fix exchange rates and adopt a common currency. It also allows us to understand how the growing dominance of neo-liberal economics in the 1970s and 1980s intersected with the post-World War II Franco-German rivalry to create the EMU, which we argue has undermined prosperity, denies reality, and rejects viable solutions thus exposing the Member States to a state of on-going crisis and stagnation.

The great European political leaders in the immediate post World War II period were not motivated to put the European economies into a straitjacket of austerity and hardship. Their aspiration was to achieve peacetime prosperity and they devised the ‘European Project’ as an ambitious plan for European integration. Their goal was to ensure that there were no more large-scale military conflicts fought on continental European soil and they broadly embraced a Keynesian economic policy consensus with governments committed to sustaining full employment and reducing inequality.

Politicians learned from the Great Depression that without major government intervention, capitalism creates periodic crises with elevated and persistent mass unemployment. The Keynesian era of macroeconomic policy that followed World War 2 saw government using deficits to supplement private spending to ensure there was sufficient jobs for all those who wanted to work. Governments around the world found the recipe for sustained material prosperity for their citizens. This consensus started to break down in the mid-1970s.

Within this broad policy consensus, it was the Franco-German rivalry that conditioned the process of integration. France’s aim was to stop Germany from ever invading it again. It considered an integrated Europe to be the means for it to consolidate its dominant position in European affairs but wanted to surrender as little national sovereignty as possible. On the other hand, Germany was a pariah and sought a restoration of national pride through economic success. The ‘European Project’ offered the Germans a way back as a world citizen. The problem was that their obsessive fear of inflation stemming from the 1920s, meant that negotiations over the new Europe would be conditioned by Bundesbank culture. This contrast in ambitions constrained the process of integration until the 1980s.

In the 1960s and 1970s, the European leaders commissioned studies into what structures are required for federations to function effectively. Economists studied Australia, Canada and the United States and concluded that such a federation would require a strong fiscal function at the federal level, integrated closely with the central banking function, and both, embedded into a federal parliament system to provide democratic legitimacy. Such a fiscal function would stand ready to make permanent transfers between the geographic units with the federation to resolve asymmetric shocks with threaten convergence. The studies uniformly concluded that the historical, cultural and political situation within the European Community would make it unlikely that such a structure could be successfully agreed upon. In particular, France and Germany were reluctant to surrender their sovereignty on terms that would be acceptable to the other.

The situation changed in the 1980s with the advent of Monetarist economic thinking emerging as the dominant school of thought in macroeconomic policy making. France was emboldened to pursue a ‘fort franc’ policy that brought it closer to the Bundesbank culture, which reflected an obsessive fear of inflation and a willingness to embrace fiscal rectitude. Once that change in geopolitical relations occurred, it was a small step for Jacques Delors to take to produce the monetary architecture that was laid at in Maastricht.

Europe embraced neoliberalism and embedded the ideology in the very legal structure that binds the Member States. This ideology led to a certain homogeneity among the different political parties with respect to macroeconomic policy, which made it easy for the then European Commission to introduce the fiscal rules known as the Stability and Growth Pact (SGP). The culture of austerity was then prominent in Europe and the consequences have been stagnating growth, elevated levels of unemployment with very high levels of youth joblessness, cuts in services, wages, pensions and increasing divergence. The very opposite to what the European elites promised the citizens of Europe.

Many progressive thinkers seem to think the problems can be resolved within the structure of the EMU, with tweaks such as the introduction of a Europe-wide unemployment scheme. Our contention is that the euro is the problem. The problems are embedded in the architecture of the union defined by the Treaties which are almost impossible to reform.

We argue that it is better for the Treaties to be dissolved and the Member States of the EMU to restore their currency sovereignty. They are then able to negotiate mutually agreeable arrangements in the form of intergovernmental agreements rather than tie themselves in a neoliberal straitjacket within the Treaty system.

We also consider the exit by the United Kingdom from the European Union, noting that the EMU is separate from the Union. We construct that discussion within the context of the European Union as exemplifying the most advanced form of neoliberalism known and the need for the British people to reassert their democratic voice.

## 2. Why a single currency?

At the end of World War II, most of the World nations entered the Bretton Woods agreement to fix their exchange rates and tie them to the value of gold via the US dollar. The latter was convertible into gold at a fixed price and so the designers of the system considered this would maintain global financial stability. The use of the US dollar as a reserve currency exposed the instability of the Bretton Woods system early on. Economist Robert Triffin warned in the early 1960s that the system required the US to run balance of payments deficits so that other nations, who used the US dollar as the dominant currency in international transactions, were able to acquire them. By the 1960s, nations started to worry about the value of their growing US dollar reserve holdings and whether the US would continue to maintain gold convertibility. These fears led nations to increasingly exercise their right to convert their US dollar holdings into gold, which significantly reduced the stock of US-held gold reserves. The so-called Triffin paradox was that the Bretton Woods system required the expansion of US dollars into world markets, which also undermined confidence in the dollar’s value and led to increased demands for convertibility back into gold. The loss of gold reserves further reinforced the view that the US dollar was overvalued and, eventually, the system would come unstuck (Triffin, 1960).

Realising the system was unviable, the US President abandoned convertibility in August 1971. For the next two years, under the guise of the Smithsonian Agreement, there were attempts to reform the fixed exchange rate system. But inevitably, it collapsed and by the mid-1970s, most nations adopted floating exchange rates, which hailed the advent of the fiat currency era.

However, the EEC nations adopted their own variants, first, ‘le serpent l’intérieur du tunnel’, then just the snake, and when those systems failed, they introduced the European Monetary System in 1978 to maintain currency stability across a membership that was disparate in terms of economic structure and trade strength.

The problem for the EEC nations was that the first major initiative of the newly formed EEC in 1962 created the Common Agricultural Policy (CAP), which was motivated by the French desire to protect its farmers and gain subsidies from Germany, and the German desire to expand its industrial export market. However, the administrative complexity of the scheme forced the Member States to maintain fixed exchange rates. The goal was currency stability to support the CAP, but that aim proved impossible to achieve, as the course of history over the next several decades demonstrated. Even in the 1960s, as the mark strengthened in value and became dominant, France and Italy had to endure regular currency crises and suppress domestic economic activity to maintain the agreed parities.

All the pre-EMU currency arrangements were dominated by the German mark, in recognition of the strength of its export machine and the other nations were then forced to maintain domestic policy to continually defend their vulnerable currencies. The resulting bias towards high levels of unemployment and high interest rates proved to be politically difficult. The experience should have should have taught the European nations that entering a currency union would be a fraught exercise.

Which raises the question: why would the European nations choose to surrender their currencies altogether and adopt the euro? To answer this question, we need to explore the ideological underpinnings that established the European Union (EU) as a neoliberal project. The euro can be best understood as another cog in the wheel driving the process of depoliticisation of European democracies - the creation of institutions that are irresponsive to popular demands such as an independent central bank or complex legislative processes estranged from the citizen. The single currency illustrates how limitations to monetary sovereignty not only constrain the space available for economic policy but also define boundaries for a popular democracy.

The series of European treaties signed in the 1950s - the European Coal and Steel Community, the Treaties of Rome establishing the European Economic Communities (EEC) and Euratom - were drawn in the spirit of overcoming nearly a century of Franco-German enmity and avoiding a repetition of the great wars that had wreaked havoc on the continent for more than a century. While the Treaty of Rome (1957) was designed to establish a spirit of trust and cooperation amongst European countries through trade and economic integration, the leaders in the 1960s and 1970s were more ambitious and sought to further the process of monetary integration.

The pro-European proponents wanted more than a regime of pegged exchange rates. The euro was touted as a symbol that would bring together Europeans in a shared identity. As former European Commission (EC) President Jean-Claude Juncker remarked, once citizens held the new notes and coins in their hands at the start of 2002, ‘a new we-feeling would develop: we Europeans’ (Streeck, 2015: 11).

But we need to take a step back to understand how the great European rivals – France and Germany – agreed to surrender their own currencies and enter an arrangement that constrained the democratic choices of each.

The Treaty of Rome formalised the ‘European Project’ – which was a plan for increased European integration – to accomplish the goal of lasting peace. But the process of integration was dominated by the Franco-German rivalry with France seeking ‘European-level’ structures that they could dominate, which would stop any further Germany’s military aggression. Their aim included maintaining as much national sovereignty as was possible and created integrated initiatives as inter-governmental agreements. Germany’s motivation was to salvage its national pride by repairing its damaged economy. They saw the ‘European Project’ as a way back as a world citizen. But their inflation angst, which arose from their experience in the 1920s, was ever present and any negotiations with France on economic integration reflected the stern culture of the Bundesbank. Up until the 1980s, it was these factors that constrained any significant movements towards a monetary union.

The 1970 Werner Report (European Commission, 1970) and the 1975 study by the MacDougall Committee (European Commission, 1977) both sought to outline the requirements for the creation of a full economic and monetary union. After studying successful federations such as Australia, Canada, and the United States. Both reports concluded that an effective economic and monetary union would require a strong fiscal presence at the federal level that had political legitimacy through a European level parliament. The latter study concluded that “It is most unlikely that the Community will be anything like so fully integrated in the field of public finance for many years to come as the existing economic unions we have studied” (MacDougall Report, 1977: 11). As a result, there was little progress towards a monetary union during this period because neither France nor Germany could agree to cede sovereignty, such were their suspicions of each other.

In the 1980s, the situation changed markedly, not because there was any shift in the long-standing Franco-German rivalry nor any cultural enlightenment, but, rather, because the Monetarist surge within the academy in the 1970s, spread into central banking and treasury departments. The idea of a single currency seemed advantageous from the German perspective because they could preserve German competitiveness from the periodic revaluations that the Deutschemark experienced. They knew, however, that this would require significant changes to domestic policy, to reduce unit costs. However, it was other EEC member states such as France and Italy who pushed for monetary integration. Both countries were fed up with the hard-currency interest policy of the Bundesbank, which, given the premise of the free movement of capital in a financialising common market, had become the de facto central bank of Europe. They were also irked, the French above all, by the periodic necessity of devaluing their currency vis-à-vis the Deutschmark to maintain their competitiveness (Streeck, 2015: 16).

For the first time, the old Keynesian planning ministry in France was overtaken in policy influence by an increasingly Monetarist-influenced finance ministry. The Barre Plan in 1976 effectively abandoned the Gaullist ‘Keynesian’ influence, and, later, Delors pursued a ‘fort franc’ policy under Mitterand’s famous ‘tournant de la rigueur’ in 1983. At this time, the Franco-Germany rivalry morphed into a Monetarist consensus, Bundesbank-style between the two nations. Across Europe, unemployment became a policy tool aimed at maintaining price stability rather than a policy target, as it had been during the Keynesian era up until the mid-1970s.

The Delors Report (1989) ignored the findings of Werner and MacDougall Reports and, instead, embraced the new neoliberal orthodoxy, which channeled the Monetarist disdain for government intervention by designing the EMU architecture to deliberately suppress the capacity of national fiscal policy to maintain low unemployment. Delors appeased the French by maintaining economic policy making at the national level and the Germans with the accompanying harsh fiscal rules.

The reunification of Germany also created anxiety in the UK and France. For the French, a ‘federal’ Europe could help curb a reunified Germany within the principle of “not a German Europe, but a European Germany”. The Germans were initially not enthusiastic about monetary union, but Chancellor Kohl gave way for fear of losing support for German reunification. When major allies in Kohl’s political camp threatened to rebel, he overcame their resistance by ensuring that the common monetary regime would follow the German model, with the European Central Bank as a copy of the Bundesbank writ large (Streeck, 2015: 17).

Beyond European powers jockeying for position the economics profession also provided an ideological underpinning for the euro. The economists that had informed the Werner and Macdougall enquiries were of a Keynesian orientation, which ran counter with the emerging Monetarism that became the dominant voice in the Delors Committee. Further, the so-called theory of Optimal Currency Areas (OCA), which defined the conditions that were essential for nations to share a single currency (Mundell, 1961), predicated against the European states joining in such a union (see Mitchell, 2015 for an in-depth discussion).

The EMU proponents in the late 1980s largely ignored the requirements set out in the OCA literature to be significant for their plans. Wyplosz (2006: 212) said that the European Commission “officials did not waste much time on the issue, which they saw as mainly political”. The Maastricht Treaty was more about making progress towards the adoption of the single currency and the requisite institutional changes that would be required to accommodate this process rather than a deep analysis of whether it would be optimal. But the declaration that the OCA literature was irrelevant went much deeper than that.

In the 1990 *One Market, one money* publication, the European Commission (1990: 46) concluded that the OCA literature provided a “rather limited framework whose adequacy for today’s analysis is questionable”. They claimed that the “whole approach ignores policy credibility issues which have been stressed by recent macroeconomic theory” (p.46), which was code for OCA being associated with the Keynesian view that fiscal policy provides an effective means of stabilising economies hit with private spending fluctuations. The ‘policy credibility issues’ related to the unproven Monetarist assertions that fiscal policy was ineffective and caused inflation, which can only be controlled with tight monetary policy.

Any serious application of the OCA theory would have been highly inconvenient to the proponents of the EMU. Of the conditions necessary to satisfy the existence of an OCA, only the relating to openness of trade between the nations could be reasonably met. The other conditions were not satisfied. The Treaty deliberately negated the capacity for a federal fiscal capacity to redress regional unemployment and there was no sense that labour was mobile. Eichengreen (1992) that while capital movements would be unimpeded in the EMU, a depressed region could hardly expect job saving capital inflow. And that regional disparities brought about by movements in the economic cycle are resolved more effectively by fiscal transfers rather than labour or capital movement. De Grauwe (2006) argued that the EMU proponents were ideologically selective in their use of the prevailing knowledge.

Whichever way you wish to interpret the OCA theory, it is obvious that the group of nations that entered the EMU did not remotely satisfy the conditions required to ensure that the adoption of a common currency would be beneficial overall. The result was that the only adjustments open to them once a major private spending collapse occurred would be very costly, a point ignored by the EMU proponents.

Europe was to understand that folly more clearly with the onset of the Global Financial Crisis (GFC).

## 3. A dysfunctional union created

British Economist Wynne Godley wrote a short but prescient essay in 1992 on the Maastricht Treaty, which laid out the architecture for the Economic and Monetary Union (EMU) in that year. He opined:

The central idea of the Maastricht Treaty is that the EEC countries should move towards an economic and monetary union, with a single currency managed by an independent central bank. But how is the rest of economic policy to be run? As the treaty proposes no new institutions other than a European bank, its sponsors must suppose that nothing more is needed. But this could only be correct if modern economies were self-adjusting systems that didn’t need any management at all (Godley, 1992).

The original sin of the EMU was that it was concocted during the neoliberal era which saw the abandonment of Keynesian fiscal policy dominance as a means of sustaining full employment. The mainstream economists engendered a disdain for discretionary fiscal policy being used to smooth out fluctuations in private spending and maintain low levels of unemployment. To politically justify this paradigm shift, the economists claimed that, in fact, the full employment level of unemployment had shifted upwards and only structural reforms, such as cutting welfare payments, lowering the minimum wage, and the like, could reduce it. The policy makers shifted from seeing unemployment as a policy target to using it as a policy tool to discipline any inflationary pressures. In terms of macroeconomic policy assignment, fiscal policy was subjugated to a renewed emphasis on monetary policy aimed at keeping inflation stable and low. It was claimed that if this goal was attained, the economy would naturally equilibrate at full employment (Mitchell, 2015).

Italian economist Franco Modigliani, who was one of the economists who coined the term Non-Accelerating Inflation Rate of Unemployment (NAIRU), which drove the bias towards monetary policy dominance over fiscal policy, reflected on his legacy during a lecture he gave in Freiburg on April 6, 2000:

 Unemployment is primarily due to lack of aggregate demand. This is mainly the outcome of erroneous macroeconomic policies … [the decisions of Central Banks] … inspired by an obsessive fear of inflation … coupled with a benign neglect for unemployment … have resulted in systematically over-tight monetary policy decisions, apparently based on an objectionable use of the so-called NAIRU approach. The contractive effects of these policies have been reinforced by common, very tight fiscal policies

The European Treaties pursued this subjugation of fiscal policy to the extreme by declining to establish a European-level fiscal function, while at the same time, designing the Stability and Growth Pact (SGP) to ensure minimal flexibility existed for Member States to use their retained fiscal functions. Their fiscal capacity was limited by layered rules for deficit (less than 3 per cent of GDP), spending increases (limited by changes in GDP) and public debt rules (less than 60 per cent of GDP). The EMU had a single currency and a single monetary policy, and, in theory, each country would be allowed to operate independent fiscal policies. But, in effect, lacking the support of a central bank that could finance deficits or purchase treasuries when needed, and bound by the Maastricht criteria, government spending would be limited by tax receipts and borrowing in the open market in competition with the private sector (Wray, 1998: 91-93). Surrendering their currencies meant that they became dependent on private bond investors to run fiscal deficits, and, during the GFC that became unworkable.

In Federations, like the USA or Canada, central governments are currency issuers and spending logically precedes taxation. Taxes drive money and central banks carry out monetary operations to set the interest rates. In the EMU this sequence is reversed. Member states are reduced to the status of currency users, much like municipalities or regional governments, and they need to raise taxes or borrow money before spending. Interest rates on their bond issues are determined by the market (Godley, 1997; Wray, 1998).

The austerity bias became apparent even before the euro was introduced. Strict convergence criteria imposed by the Maastricht Treaty forced many European economies to cut government spending and increase taxes in order to meet the final transition stage criteria for entry to the EMU in the late 1990s. Consequently, GDP growth rates were suppressed, and unemployment remained at elevated levels. The European debates about how the common currency would work were dominated by German concerns about inflation and their distrust of Southern Europeans, who were suspect of not taking the convergence criteria seriously. These suspicions had two major consequences. First, it meant that the new union would have no integrated fiscal and monetary function. Second, given the fiscal tools were left at the Member State level, the Germans insisted that tight constraints be placed on the Member States to stop them abusing the common currency. The level of distrust was so high, that the Member States should have realised then that it would be difficult to work together to make the common currency deliver prosperity for all the European nations that joined.

The SGP included a ‘preventative arm’ and ‘reinforced surveillance of budgetary positions and the coordination of economic policies’. This was completed with a ‘corrective arm’ ‘which outlined a process for the elimination of so-called ‘excessive deficits’ (European Council, 1997). Although some deficit leeway above 3 per cent for nations that were enduring major recessions was provided it would soon be seen that the SGP undermined the capacity of the national governments to respond to recessions with increased discretionary spending (Mitchell, 2015).

The arbitrary 3 per cent limit to fiscal deficits condemned Governments to compensate the effect of automatic stabilisers, which increased fiscal deficits, with contractions in discretionary spending if they wanted to avoid fines and other corrective actions from the EC. The damage goes beyond the inability to manage the economic cycle. Austerity policies pursued after the GFC have permanently depressed public investment for most countries. Underinvestment has compromised public services, education, healthcare, public infrastructures and research and development. These are spending items that not only provide wellbeing for current generations but are also critical for improved productivity in the long run.

The fiscal rules are also reinforced by surveillance through the Excessive Deficit Mechanism. The system allows European Commission technocrats to overrule fiscal decisions of elected governments in the Member States. The arrangements revealed a blind belief that constraints on fiscal policy would allow the central banks to maintain price stability and that the operation of ‘automatic stabilisers’ that are built into national government fiscal positions would be sufficient to restore growth during recessions.

The Treaties also established the System of European Central Banks (ESCB) with the former national central banks integrated with the newly created European Central Bank (ECB), which had charge of monetary policy. Consistent with the developments in the economics profession, the ECB was declared independent from the political process and charged with maintaining price stability in the monetary union.

Article 123 of the Treaty on the Functioning of the European Union (TFEU) – the so-called no ‘bail-out’ clause - banned overdrafts or any other type of credit facility with the ECB or with the national central banks in favour of Union institutions, bodies, offices or agencies, central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of Member States, as well as the purchase directly from them by the ECB or national central banks of debt instruments.

Together with the SGP rules, the no bail-out clause was intended to force fiscal discipline on the Member State governments. The intent was to force the Member States to ‘obey’ the dictates of the private bond investors, who knew that the government debt carried credit risk because the States had surrendered their currency sovereignty. It was argued that this external discipline would ensure that deficits remained within the fiscal limits.

As we will see in Section 4, the hopes for the system were far-fetched and the defects in the monetary architecture manifest very early in the monetary union’s history.

## 4. The cracks appear immediately and widen as time passes

Ironically, soon after the adoption of the common currency, it would be Germany, followed by France, who would first trespass beyond the SGP limits during the 2003 recession. The transgression had little consequence for both countries and no action were taken after a stand-off between the European Council and the Commission, and some rule changes demanded by Germany. In the aftermath, Germany implemented the 2004 Hartz reforms which would enhance its economy’s competitiveness by disciplining its labour force through cutbacks in the welfare state and deregulation of the job market which created the Mini-job era, a diminished form of employment with pay and conditions stripped back significantly. The reforms ensured that Germany’s export-led growth model, which relied on repressing domestic demand and keeping unit costs relatively low, could continue after the nation lost its ability to manipulate the mark exchange rate. Germany effectively undermined the stability of the EMU by adopting a model, which given the dominance of intra-EU trade, relied on its currency partners running large external deficits, while it suppressed its own imports. German unit-labour costs were persistently lower than the other Member States (Bibow, 2019). Germany has regularly posted external trade surpluses between 6 and 8 per cent of GDP in the following years. In effect, Germany learned that a managed process of ‘internal devaluation’ pursued alone, would improve German exports at the expense of its EMU partners.

There were two negative consequences of this growing imbalance in an environment where the ECB ran a one-size fits all interest rate regime. First, the less competitive member states, that were now unable to enjoy the benefits of any exchange rate flexibility within the Eurozone, were forced to run burgeoning trade deficits by Germany’s mercantilist strategy. That, alone, was unsustainable. Second, the massive trade surpluses that Germany was running could not find a reasonable return in the German markets and, consequently, investors exported the capital to the other Member States. The ECB had set interest rates to suit the recessed German economy (2003) at a time when the southern states were growing. The uniform interest rate was clearly not suitable for a geographic area as large as the EMU where the economies were of vastly different industrial structures. The combination of low rates and a flood of capital into the ‘periphery’, fuelled the massive rise in private sector indebtedness in nations where real estate bubbles such as in Spain, Ireland and the UK developed in the lead-up to the GFC.

The introduction of the euro created an asymmetry in adjustment that is like that observed under the gold standard where increases in the amount of money requires that countries previously increase their gold reserves. But higher reserves do not imply an automatic expansion of spending and money supply since excess gold was frequently sterilised. Similarly, in the EMU, debtor countries are forced to reduce their deficits, prices and wages. However, creditor countries, which are accumulating balances in euros, are not required to adopt expansionary measures. When peripheral nations were forced to adjust through an internal devaluation process Germany imposed additional costs on them by failing to take expansionary measures and not allowing increases in its imports. (Esteve *et al.*, 2017).

There was a misplaced confidence in the stability of the system leading into the GFC. Basking in smug complacency, the European elites presented the euro as a resounding success and waxed lyrical about the macroeconomic stability of the area with the low inflation rates presented as evidence of success (Buti and Gaspar, 2008).

But history soon overtook this hubris and the disruption in financial markets that became the GFC exposed the dysfunctional euro architecture. On a global basis, the GFC exposed the fragility of a deregulated global financial system built on financial securitisation, shadow banking, lax prudential oversight, which had delivered relatively modest GDP growth rates, declining productivity (less investment in capital formation) and massive, unsustainable real estate bubbles. Despite the warnings of heterodox economists, governments, which had become captive to the financial speculators, overlooked the growing vulnerability of the overleveraged private sector balance sheets while celebrating their fiscal surpluses. These surpluses were only possible because the private credit binge allowed spending growth to be maintained in the face of the massive fiscal withdrawals. But predictably, the fiscal surpluses combined with burgeoning trade deficits generated record private sector deficits creating an increasingly unsustainable debt burden (Godley and Wray, 1999).

For the euro nations, the GFC quickly exposed the lack of a federal authority as a serious flaw in the design of the union. What started as a private debt crisis soon morphed into a public debt crisis. The GFC laid bare the rashness of the decision by Member States to roll their central banks into the euro system, which meant they no longer had a lender of last resort that they could rely on. Upon relinquishing their own currencies, the 19 Member States began issuing debt in a foreign currency, which immediately introduced the problem of credit risk. These nations were from that point on beholden to the bond market investors if they were spending more than their tax revenue. Countries that had joined the EMU with a legacy of high public debt, such as Italy or Greece, found themselves in a predicament. The crisis quickly entangled nations, such as Ireland or Spain, which had fostered massive real estate bubbles and financial speculation during the previous decade, in a doom-loop scenario. Although they had not been running large fiscal deficits before the crisis, the GFC pushed their deficits out, which increased the risk of default. The bond investors also understood that a two-way dependency between banks and their sovereigns existed. Bank resolution was still the responsibility of Member States but, without the issuing capacity of a central bank, rescuing a financial institution would lead to even larger public debt burdens. A real risk of default of the peripheral nations prompted a large-scale flight-to-safety to German and other Northern European bonds. By 2010 investors were demanding increasingly higher yields for Southern European treasuries which compromised the solvency of those states (Mitchell, 2015; Bibow, 2019).

Mainstream economists constructed the GFC as signalling a global problem of excessive fiscal deficits and public debt without differentiating between the currency-issuing states, which were having no problems maintaining low yields on the debt and the EMU states that had surrendered their currency sovereignty. Harvard economist Roberto Alesina coined the term ‘expansive austerity’ and convinced European policy makers that large discretionary reductions in their fiscal deficits would be successful in overcoming the crisis without causing recessions (Alesina, 2010). The IMF started talking about ‘growth friendly austerity’, which of course is a misnomer. European institutions pressed Member States to embark on fiscal consolidations and doubled down on its commitment to fiscal rectitude. The European Commission proposed the so-called Six Pack a new ‘Macroeconomic Imbalance Procedure’, with a ‘new surveillance and enforcement mechanism’ and harsher sanctions for compliance failure and the obligation to reduce the ‘gap between its debt level and the 60 per cent reference (Mitchell, 2015).

Two infamous letters sent in 2011 by ECB president Jean Claude Trichet to Spanish and Italian Premiers Zapatero (Trichet and Fernández Ordóñez, 2011) and Berlusconi (Trichet and Draghi, 2011), conditioning the support of the ECB to structural reforms in the labour and other markets, caused the downfall of the latter and led the Spanish Social-Democratic premier to introduce a golden rule amendment to the Constitution and abandon discretionary stimulus packages. Greece, Portugal, Cyprus, Ireland and Spain were bailed out through the European Stability Mechanism (ESM), an agreement outside of the EU treaties, which created a € 700 billion loan facility lent by Eurozone member states. The rescue effectively placed those countries under the supervision of the European Commission, the ECB and the IFM, the so-called *Troika*. The so-called ‘democratic deficit’ widened.

The crisis also revealed that European solidarity was in short supply. Southern nations were accused of profligacy and former Eurogroup President Jeroen Dijsselbloem irked public opinion in those countries by condemning them for wanting to spend “all the money on spirits and women and then ask for help” (Bertrand , 2017). The results of the austerity were predictable with endemic stagnation and persistently high unemployment becoming the norm in the post GFC period (Mitchell, 2015). Some refer to this decade as creating a ‘lost generation’, given the sustained high youth unemployment rates.

While the introduction of the ESM was constructed by the European elites as a success, the only way the monetary union has survived, and Member States have remained solvent, is because the ECB has effectively defied the no bailout restriction and funded the fiscal deficits of the Member States through its bond buying programs. Almost all the debt being issued by governments in the monetary union over the last several years has been purchased by the ECB.

The necessity for the ECB to engage in this way can be traced back to the initial decision by Member States to surrender their currency sovereignty but at the same continue to accept the primary fiscal policy responsibility. In the early days of the GFC, bond yields rose rapidly for the Member States most impacted (Spain, Italy, Portugal, etc) and the ECB had little choice other than to suppress the discretion of the private bond markets to set yields for fear that the already recessed nations would find it difficult rolling over funding for the deficits that the recessions had created. In May 2010, the ECB introduced the Securities Markets Program, which was the first of several large-scale government bond purchasing programs that persist today. These programs purchased large quantities of government debt in secondary markets and effectively took away the credit risk facing private dealers. They allowed the Member States to continue to issue debt into the primary markets and fund their deficits. Without these on-going ECB purchases, several Member States, including Italy, would have become insolvent during the GFC and beyond.

The ECB justified the bond-buying programs as being necessary to ensure ‘a functioning monetary policy transmission mechanism by promoting the functioning of certain key government and private bond segments’ (González-Páramo, 2011) - that is, as a legitimate monetary policy operation. However, the reality is that they have been buying government bonds in the secondary markets in exchange for euros, which the ECB creates out of ‘thin air’, in quantities far beyond anything that would be required for purely operational reasons. The purpose has been to lower yields on government bonds as bond investors knew they could offload securities from distressed states onto the ECB. The ECB has been effectively funding the Member State deficits and acting contrary to the spirit, at least, of the no bailout clause in the TFEU.

The problem with that policy is not the fact that the ECB has been funding the deficits despite the misgivings the mainstream economists might have about that practice. Rather, the problem has been that up until the pandemic, the purchases were conditional on Member States obeying the fiscal dictates of the European Commission and, in that vein, while they avoided the collapse of the Eurozone, they also perpetuated the austerity bias (Mitchell, 2015).

But it is ironic that despite all the efforts of Delors and those that followed to limit the fiscal function in the EMU and impose no bail out restrictions on the ECB, the central bank they created has effectively been maintaining a type of fiscal function which fills the void left by the Treaties and maintains the solvency of the Member States. This irony exemplifies the poorly contrived architecture that the Maastricht process pushed onto the European nations.

## 5. The new fiscal policy dominance – temporary or a path to reform?

More than twelve years after the GFC there is growing awareness that the dominant New Keynesian economics paradigm has become degenerative in the Lakatosian sense. It is full of internal theoretical inconsistencies and lacks empirical veracity. In practical terms, it failed to anticipate the crisis, believing that financial markets were efficient and would not fail in the way they did. Efficient market theory was used as the authority for governments around the world to deregulate financial markets and relax prudential oversight, which, in turn, created the conditions for the crisis. Further, mainstream economists then constructed the problem that they had helped to create as one of excessive fiscal deficits and pressured governments to implement austerity remedies that prolonged the crisis unnecessarily. The fiscal positions were largely just a response to the non-government spending collapse, which should have been the policy focus.

To maintain reputation, debates amongst mainstream economists are now revolving around a temporary return to fiscal dominance within the Neoclassical framework. Former IMF chief economist Olivier Blanchard, “argued that public debt may have no fiscal cost” since the ‘safe rate’ was historically low. Although he claimed that “public debt reduces capital accumulation and may therefore have welfare costs” these costs could “be smaller than typically assumed” (Blanchard, 2019).

This sort of erroneous reasoning is now commonplace among mainstream economists, who claim they have changed their views because monetary policy has, for now, hit the so-called ‘zero bound limit’ rendering monetary policy momentarily ineffective. In a 2020 speech Isabel Schnabel, Member of the Executive Board of the ECB, recognised that

The first consequence is that fiscal policy has become more important as a macroeconomic stabilisation tool. When natural rates are low and policy rates are constrained by the lower bound, a more accommodative fiscal policy is needed to lift the economy out of a low-growth, low-inflation trap … Fiscal expansion is indispensable at the current juncture to sustain demand and mitigate the long-term costs of the crisis. (Schnabel, 2020).

The *ad hoc* nature of the mainstream response to their past failures is breath taking.

While world economies were struggling before the Covid pandemic, it is now clear that the old narrative about sound finance and a reliance on private markets to solve the economic problems is discredited. The insights provided by Modern Monetary Theory (MMT) are to the fore. Not only do governments have to deal with the on-going costs of the pandemic, but they must also face the climate crisis, which will require a substantial role for fiscal policy over an extended period. The mainstream view that there is only a temporary need for expanded fiscal support, until monetary policy normalises again, indicates that they have not learned any lessons from the last few decades, which have been marked by poorly performing economies and rising inequality.

The problem in Europe is magnified given the flawed architecture of the EMU and the bias towards austerity embedded in the legal framework. In the face of the severest downturn in economic activity since the Second World War, the European Council agreed in April 2020, to activate an ‘escape clause’ in the SGP to allow Member States to increase spending beyond deficit limits. In tandem the ECB announced an additional bond-purchasing program – the Pandemic Emergency Purchase Programme (PEPP) - which supplemented the already significant Asset Purchasing Programmes. For the mainstream economists, this temporary suspension of rules is conditioned on the perpetuation of a low interest rate environment without any recognition that central banks can sustain zero interest rates in perpetuity.

Despite the current suspension of fiscal rules, it is hard to teach an old dog a new trick. Except for Germany, whose government deemed that it was in a fiscal position to invest heavily in economic recovery, member states remain coy about taking advantage of the increased flexibility. An IMF review showed that, amongst developed economies, Eurozone countries were less willing to implement direct fiscal impulse measures (additional spending or forgone revenue) opting instead for equity, loans and guarantees which have a smaller fiscal multiplier effect since the aid needs to be repaid or may never even produce a cash flow into the economy (IMF, 2021). Whether this reluctance is a product of an entrenched austerity bias, conditioned on years of hectoring from the European Commission, or, whether it reflects a fear that they will have to pay a greater price in terms of fiscal cuts when the Commission resumes the Excessive Deficit Mechanism, is a matter of conjecture.

But rather than risk increased deficits, the Prime Ministers of Italy and Spain promoted the idea of a rescue package known as Next Generation EU (NGEU) with a budget of 750 billon euros. NGEU gives the European Commission authorisation to issue debt that would be paid back in seven years after 2027 with increased national contributions to EU Budget (General Secretariat of the Council, 2020). The package was finally approved by the Council in July 2020 following acrimonious discussions. The so-called ‘Frugal Four’ (Austria, Denmark, Netherlands and Sweden) who had the sympathy of Germany in their fiscally conservative ambitions refused to concede on the issue of permanent transfers and blamed Southern Europeans for not having done enough previously to create the necessary ‘fiscal space’ and fund their own recoveries (Khan, 2020). Eventually, the group acquiesced to NGEU after securing rebates in their contribution to the EU budget (Khan and Peel, 2020). The proposal stimulus was inadequate in quantum, given the crisis, and the delays in implementation meant that the damage has been severe. Further, it mostly took the form of loans rather than grants, as a result of an unwillingness of the Northern nations to allow permanent transfers within the union.

Disbursement of the funds did not begin until a year later after the European Commission placed two bond tranches totalling 15 billion euros in the market (European Commission, 2021) and approved the structural reforms plans submitted by member states (Euronews, 2021). For most countries, annual transfers will not exceed 1.6 per cent of gross national income and most of the disbursement will be happening between 2022 and 2024 (Red MMT, 2021). Neither the size nor the timing of the disbursements will be sufficient to bring the nations most afflicted by the pandemic out of the recession. Also, supposedly inclusive energy transition goals of the NGEU programme are questioned by environmentalist and progressive movements who caution that funds will be hoarded by large companies (Dombey, 2020) and invested in large-scale infrastructure projects (Scherer *et al.*, 2021), while direct job creation and upgrading of neglected public infrastructure after decades of underinvestment will get symbolic support only. NGEU is a manifestation of the austerity bias and the continued hollowing out of the state that pervades the Neoliberal coteries ruling Europe.

## 6. Can the Eurozone be fixed?

Suboptimal outcomes in the Eurozone are the result of the institutional arrangements limiting the fiscal capacity of the member states. There are three options as a way forward: (a) Continue as before with on-going stagnation and growing social instability; (b) Address the dysfunctional architecture by creating a meaningful federal fiscal capacity closely linked with the central bank capacity – as in the functioning federations such as Canada and Australia. Within this context, we suggest overt monetary financing (OMF) of the Member States by the ECB become normalised practice to eliminate the reliance on private debt markets (Mitchell, 2015); and (c) Break-up the union, restore currency sovereignty to the Member States and engage in Europan agreements where appropriate on an intergovernmental basis, rather than a binding Treaty.

The first option does not appear to be attractive. Several *ad hoc* proposals have been made to work ‘within’ the current system, for example, the expansion of a European unemployment insurance capacity, but all fall short of dealing with the basic architectural shortcomings of the system.

Several authors have explored a federal solution with a European Fiscal Authority and European Treasury which could resort to OMF and have the capacity to issue debt (for example, Mitchell, 2015; Cruz Hidalgo, *et al*, 2019). The essential philosophy underpinning such a move would be that the Member States would subjugate their fiscal autonomy to a federal authority which to gain legitimacy would be embedded in a democratically elected European government. Essentially, this is what the Werner and MacDougall committees determined would be required. This would require an acceptance that permanent transfers would be made within the federation to address asymmetrical spending shocks. The federal authority would commit its treasury and central bank resources to maintain full employment and price stability, with a Job Guarantee program, introduced to bolster the safety net and strengthen the automatic stabilisers in the face of fluctuating non-government spending.

We do not consider the move to a truly federal Europe to be politically possible within the modern European context. In the first place, it would require major modifications to the European Treaties and thus require the assent of all EU Member States and a lengthy process of change. It is also highly unlikely that Germany or the ‘Frugal Four’ would ever agree to this sort of structural shift. The cultural obstacles persist against arrangements that would imply net transfers from the wealthier export economies of Northern European to Southern countries. Germany has shown an unwillingness to engage as a Member State in a true federal system where permanent transfers between states are commonplace. This reluctance is evidenced in survey data where German residents exhibited a “low willingness to accept fiscal risk-sharing through common unemployment insurance, while a sovereign insolvency procedure aimed at strengthening market discipline is supported by a majority of the survey participants” (Dolls and Wehrhöfer, 2021).

The paradox of the European project is that divergence rather than the aspired convergence has become the norm (Streeck, 2015: 13). Europe is split by an imaginary line that separates Northern creditor nations from Southern debtor nations. The latter have borne the brunt of the adjustment based on fiscal consolidation and internal devaluation to correct trade imbalances that both sides contributed to create. The cultural and economic fault lines in the European Union help us understand why the most likely fix for the single currency will neither be a federal government nor a system of fiscal transfers.

The most likely scenario is that nations will be forced into unilateral exit driven by social instability arising from persistent crises. Nations such as Italy have still not recovered from the GFC as a result of the austerity bias imposed. While there are strong pressures to sustain the common currency and institutional blockages exist to discourage exit, the long-term decline in material prosperity will eat away at social harmony and shift the political focus towards new arrangements.

## 7. Democracy at stake

It has been argued that the evolution of the European Union towards increasing power in Brussels and the imposition of technical fiscal and other rules has created a ‘democratic deficit’ within the Member States, where unelected Commission technocrats can impose harsh austerity settings on elected governments against their will. The experience of Greece during the GFC was an extreme example of this phenomenon. The role of the ECB in the Greek standoff in June 2015 was particularly illuminating in this respect.

The role of the ECB since the GFC in sustaining the currency through its large-scale bond-buying programs, yet, participating in the imposition of deep austerity policies (and being a partner in the Troika) reinforces the deterioration in the quality of democracy in the deficit nations. By threatening to shut down Greece’s banking system in 2015, the ECB demonstrated clearly that it had the power to cause the downfall of an elected government or to force them to adopt policies that they lacked a popular mandate.

Further, Streek (2015) argues that all emergency relief to Member States that are in crisis are always condition on the technocratic surveillance mechanisms introduced by the Commission, which have the capacity to override the discretion of the elected government. The peripheral nations have now entered a sort of neo-colonial relationship with the Union, where some of the leading nations and EU institutions have discretion over them and their parliaments (Alonso González, 2011). This was graphically depicted by former Spanish Premier Zapatero, who recalls how in a one of the summits dedicated to the Greek crisis, that the ‘text was forged in closed meetings in which usually Germany, Greece, France, the European Commission, the President of the Council, and, on occasions, the president of the ECB were represented. The bulk of the Governments patiently awaited the results of this peculiar work method … before the formal council meetings’ (Rodríguez Zapatero, 2013: 224). A more recent example of this phenomenon was the downfall of the Five Star and Lega Nord coalition in Italy and its replacement by Mario Draghi (Fazi, 2021).

The EU is far from being a true federation. The German Constitutional Court (*Bundesverfassungsgericht*) defines the EU as a ‘Staatenverbund’; a special type of multilateral organisation ties the Member States through strict legal and administrative structures, but maintains their territorial sovereignty (Medina Ortega, 2014: 58-62). The Constitutional Court, in a landmark ruling regarding the compatibility of the Treaty of Lisbon with Germany’s basic law, made some clarifying statements.

The extent of the Union's freedom of action has steadily and considerably increased, not least by the Treaty of Lisbon, so that meanwhile in some fields of policy, the European Union has a shape that corresponds to that of a federal state, i.e. is analogous to that of a state. In contrast, the internal decision-making and appointment procedures remain predominantly committed to the pattern of an international organisation, i.e. are analogous to international law; as before, the structure of the European Union essentially follows the principle of the equality of states (Bundesverfassungsgericht, 2009).

In a federation, the central government is democratically elected, and its parliament is empowered by a constitutional process (formally or otherwise). It controls the national fiscal function and monetary policy. It is accountable to the voters for the consequences of that policy, which gives the national government democratic legitimacy. Further, it has the capacity to make permanent fiscal transfers to the states that are part of the federation. There is a sense of nation defining the way these Member States participate within the federal system.

It could be posited that the European Parliament provides the sort of democratic legitimacy that other EU governance institutions lack, but the German Constitutional clarifies that neither

as regards its composition nor its position in the European competence structure is the European Parliament sufficiently prepared to take representative and assignable majority decisions as uniform decisions on political direction. Measured against requirements placed on democracy in states, its election does not take due account of equality, and it is not competent to take authoritative decisions on political direction in the context of the supranational balancing of interests between the states (Bundesverfassungsgericht, 2009).

The important point is that the fiscal and monetary functions that normally reside in the national government (through its treasury and central bank) are severed in the European Union, even though the Member States retained both fiscal policy functions and their central banks. However, monetary policy is determined by the ECB Governing Council, and transmitted through the European System of Central Banks. There is no democratic accountability in this process, although the individual Member State central banks are members of the System and the ECB has to appear before the European Parliament regularly.

Further, while the Member States retained their fiscal functions, the EU treaties place significant constraints on the discretion of any government through the various fiscal rules and surveillance mechanisms.

A true understanding of democracy implies that it relies on institutions capable of managing the inherent conflicts present in any society between social classes and territories and within the capitalist class. It is unlikely that such clashes between interest groups can be managed without effective monetary and fiscal sovereignty or through multilateral organisations such as the EU. Without European level political parties, trade unions, media and civic organizations real democracy at the EU level can only be an illusion.

A restoration of currency sovereignty for the Member States in the Eurozone would enable more scope for *repoliticisation* of the economic governance of European member states (Mitchell and Fazi, 2017). The accountability for economic policy performance would be again closely integrated with the election process. In the EMU, the neoliberalism has been embedded in the very structure of the legal framework – the treaties. That makes it very hard for an alternative political perspective – such as socialism or social democratic values – to thrive because the neoliberal constraints are always in play. The restoration of Member State sovereignty means that rival ideologies can once again contest the political terrain and the government can then better reflect the will of the people. We saw in 2015, how quickly the European institutions trampled the elected government of Greece, which had just been endorsed by the people via a referendum to reject neoliberal austerity.

There is still a rationale for Europe-level institutions based on intergovernmental agreements, which would pursue activities that are best achieved through international cooperation either because the challenges exceed a nation’s border, or its resources are insufficient to execute them in isolation. Examples include agreements on reduction of greenhouse gas emissions, human rights and migration, and similar. But trying to force all the Member States of the EMU to share a common currency has not proven to be successful.

## 8. The road to Brexit

Each step taken in the process of European integration made it increasingly difficult to reverse. The fact that the common currency and the rules surrounding it are embedded in the very legal structure of the European Union (the treaties) means that there is a high degree of rigidity in the arrangements because it is very hard to change the treaties. It is not as though a change of government will bring a new ideological focus to policy.

The theorists of European integration speak of a functionalist approach that was well summarised by Jean Monnet, considered one of the founding fathers of the EEC: every decision should create a problem that would oblige leaders to take another decision always in the right direction toward a more perfect union (Estella de Noriega, 2014).

But the momentum for integration observed in the 1980s and 1990s seems to have ground to a halt as a result of a series of crises and a heightened sense of dysfunction in the basic architecture of the EMU. Several countries such as Denmark, Sweden, Poland, Hungary and the Czech Republic have declined to adopt the euro. Poland and Hungary, governed by right-leaning governments, have clashed regularly with the European Commission regarding the protection of LGTBI rights (Than and Baczynska, 2021) and the rule of law requirements to gain access to the NGEU funds (BBC News, 2020a). At no point since the end of World War Two, have Europe’s Member States confronted each other with so much discord and hostility nor the concept of European unification been so imperilled. For the first time since inception, we have seen a Member State, the United Kingdom, exit the Union after its historic Brexit referendum of June 2016.

Brexit terminated Britain’s awkward membership in the European project. Brexit became a Conservative Party project, while the Labour Party largely assumed a Remain stance, which was one of the contributing factors in its December 2019 general election loss. Such positions were not always so. The UK entered the EEC in 1973 under the conservative government of Edward Heath. The left-wing branch of the Labour party, under the leadership of Michael Foot and Tony Benn, had opposed entry into the EEC precisely on the grounds that they understood that it made a socialist programme unfeasible. Leading into the first 1974 general election, Labour promised that there would referendum to determine Britain’s on-going membership of the EEC. The referendum, which was held in June 1975 split the Labour Party, with its more conservative leadership, who had come under the influence of Milton Friedman’s Monetarism, using it as a wedge to reduce the influence of the left-wing in the Party. The referendum “provided the opportunity for the leadership to inflict a comprehensive and decisive defeat on the Left” (Mitchell and Fazi, 2017: 65).

The Conservatives, who were initially pro-Europe, increasingly became Eurosceptic, under the leadership of Margaret Thatcher, who perceived the EEC as promoting excessive bureaucracy, statism and interference in the market and opposed to the laissez faire policies she preferred. She vehemently opposed the Maastricht Treaty and saw the process of integration as a betrayal to the original project of a loosely regulated association of states set up to facilitate free trade moving towards a bureaucratic form federalism under the control of the Franco-German axis.

In 1990, Thatcher was also opposed to joining the European Exchange Rate Mechanism (ERM), the system which established narrow fluctuation bands around a central exchange rate for each European currency and was designed to address the failures of previous exchange rate fixing mechanisms in Europe. Thatcher was aghast that the Chancellor of the Exchequer, John Major, whom she saw as falling prey to a pro-European lobby, was becoming increasingly excited about integration within the ERM and Delors’ monetary union plans. The issue, ultimately, forced the resignation of Thatcher, and, her successor, Major pressed ahead with participation in the ERM (Thatcher, 1993). However, when George Soros’ Quantum Fund begun a speculative attack against the pound and other European currencies on September 16, 1992, an episode known as ‘Black Wednesday’, the Bank of England struggled to support the exchange rate after spending more £10 billion of its foreign reserves. Germany, responsible for triggering the episode by raising interest rates to counteract the perceived risk of inflation arising from the annexation of the German Democratic Republic, was not supportive of the beleaguered currencies. The Bundesbank refused to prop up those currencies or lower interest rates. Ultimately the Bank of England let the pound float and depreciate by 13 per cent and never joined a European exchange rate regime again. For many ‘Black Wednesday’ became ‘White Wednesday’ because it was the day Britain regained its policy independence (Mitchell, 2015).

Growing Euroscepticism amongst the ranks of the Conservative Party was catalysed by the creation of Nigel Farage’s Eurosceptic party UKIP, which made a dent in Conservative Party support. The UKIP threat seems to have tipped the balance in favour of Prime Minister Cameron’s decision to hold a referendum which he hoped would validate Britain’s membership in the EU (Mason, 2016).

The 2016 Brexit referendum and its aftermath have proven to be extremely divisive. Both sides have made acrimonious accusations of lying about the issues. The Leave campaign referendum’s victory was represented by Europhiles, either as the result of xenophobic deceits encouraged by the Eurosceptic press or as a populist reaction to the government’s fiscal austerity policies and general discontent about the economy. On the other side ‘Remainers’ were reproached for using ‘Project Fear’, which attempted to raise anxiety about the future of the UK outside the EU using, so-called independent economic reports that were sensationalist in their predictions of doom. None of the predictions subsequently transpired.

The ‘Leavers’ were strongly associated with the population that had endured significant material losses as a result of globalisation and the neoliberal overlay. They had seen their communities fractured through high unemployment, loss of government services and declining public infrastructure. The issue of migration was a significant determinant of the decision to vote Leave, but these concerns are always accentuated when there is persistent mass unemployment and economic hardship.

However, opposition to EU membership was always high in the UK and support for exiting the EU never fell below 30, with a minimum in the late 1980s, polling consistently above 40per cent thereafter (Ipsos Mori, 2014). Nearly two-thirds of Britons do not identify as European, one of the lowest percentages in Europe. Further, the EU barometer showed that mistrust of the EU was among the highest in the British population (Dennison and Carl, 2016). A survey conducted on participants in the referendum showed that the Leave vote won by wide margins in the older cohorts; the unemployed; the retirees especially those on a public pension; council and housing association tenants; those with secondary education or less; and whites. In contrast, “the AB social group (broadly speaking, professionals and managers) were the only social group among whom a majority voted to remain (57 per cent). C1s divided fairly evenly; nearly two thirds of C2DEs (64 per cent) voted to leave the EU” (Ashcroft, 2016).

It was clear that the hollowing out of the regions caused by neoliberal economic policies in an increasingly global world, had created divisions within British society, with the high-income urbanites predominantly supporting the Remain position and the regions, who had been left behind, supporting the Leave vote. Many of the latter had historically voted Labour, and while most Labour voters were in the former camp, the majority of Labour MPs were elected in constituencies that had voted to Leave. That point was ignored by the Labour leadership going into the 2019 general election and was a decisive factor in their eventual loss.

We consider Brexit is better seen as an indictment of neoliberalism as represented by the EU than as an expression of ‘small England’ nationalism, even though the latter influences were clearly of influence in the outcome.

## 9. Aftermath of Brexit; opportunity

It is still too early to assess the consequences of Britain’s decision to exit the EU. It will ultimately depend on the on-going policy response of the British government and early announcements indicated that they were aware that they would have to address the hollowing out of the Midlands and the North of England as a matter of urgency (the so-called ‘levelling out’ storyline.

However, the onset of the pandemic has complicated any straightforward analysis and we will have to wait some time before the impacts of the Brexit, separate from the pandemic are able to be fully appreciated.

What we know to date, however, is that the aftermath of the Brexit referendum saw a badly handled withdrawal agreement negotiation that was extended beyond the two-year period mandated by the EU treaties and twice voted down by the House of Commons in unprecedented defeats that led to the resignation of the Theresa May cabinet (BBC News, 2020b). The 2019 General Election called by Boris Johnson, in effect, became a second Brexit referendum and returned him to power with a ‘get Brexit done’ mandate and the poorest electoral turnout for the Labour Party since 1935 (BBC News, 2019). Jeremy Corbyn’s ambivalent stance, driven by deep divisions within the Labour Party, turned away many Labour voters.

The final withdrawal agreement was signed with minor changes to the Theresa May agreement regarding the more contentious issues such as the Northern Ireland backstop and fishing rights.

More than a year later the predictions of collapse of the British Economy by the Remain camp have failed to materialise. While growth in the UK has been lacklustre the Eurozone has not fared any better, especially during the pandemic. But the bitterness and rancour rage on. Any piece of bad news will likely be attributed to Brexit by Europhiles. A drop in foreign trade figures observed in January 2021 was construed as the forecasted doom augured by ‘Remainers’ (Inman, 2021) but the Office of National Statistics made it clear that as the economy adjusted to the changed circumstances, volatility was to be expected. Indeed, foreign trade experienced a robust rebound in April 2021 and monthly imports from non-EU countries were the highest since records began in January 1997. Clearly some trade partner substitution has been observed. Factors such as stockpiling before the country departed from the customs union and fallout from the pandemic also distorted the trade figures. (Office for National Statistics, 2021a).

Analyst Wolfgang Münchau has decried that the ‘forecasts of unmitigated gloom, however, have been wrong and deceitful. When economists failed to predict the global financial crisis, they did not so out of malice or political bias. But their Brexit forecasts were not an innocent mistake - nor will they be remembered as such’ (Münchau, 2021).

What should we make then of Brexit? Clearly a nation can prosper and trade outside the aegis of the EU. Whether Britain prospers in the post-Brexit era, will depend largely on the decisions taken by the British government in relation to domestic spending and taxation. If it truly pursues a nation-building exercise (including its ‘levelling up’ promises), invests in revitalising public infrastructure, strengthens regulative frameworks in relation to the major services (energy, transport, water, etc), preferably reversing the damaging privatisations, improves funding to local council authorities, and targets job creation, then the prospects are that Brexit will not hold back the material progress of the economy. But if the Government reverts to the neoliberal austerity mindset that has marked most of its current tenure (since 2010), then it is likely that Brexit will compound the damage already caused.

With the pandemic blurring the situation since Britain formally left the EU, it is hard to see the clearly separate out the impacts of Brexit and we will have to wait for some time to fully appreciate the costs and benefits. The ONS has tentatively concluded at the time of writing, that the Government seems to be acting with more flexibility than the Member States of the European Union. The general government deficit (or net borrowing) was £65.3 billion during the December-quarter 2020, equivalent to 11.9 per cent of GDP; this is 4.9 percentage points above the average of the 27 EU member states for the same period (Office for National Statistics, 2021b)

Brexit has created an opportunity to depart from the neoliberal policies that have dominated the country since the Thatcher era. Exit from the EU was a necessary but not sufficient for the implementation of a more progressive agenda. As a monetary sovereign the UK can now decide how it utilises its resources and has the potential to secure levels of prosperity beyond reach for many of the EU’s peripheral nations. EU fiscal deficit rules embedded in treaties such as the SGP may be ignored, even though it is true, that the European Commission had no real disciplinary mechanism available should Britain defied the rules while a Member State. Further, it is also true, that the British government had been a major influence on the neoliberal direction that the Commission has taken over the last several decades. But now, Commission preapproval of general fiscal settings in Britain is a thing of the past and the European Court of Justice is no longer able to overrule legislation introduced within the British parliamentary system.

The ball is now in the British government’s court, and it can no longer claim it is constrained in its policy settings by European Union membership. That freedom provides more scope for progressive parties to articulate a path forward in terms of dealing with climate change, the pandemic and restoring the scope and quality of public services.

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