

## EMU Enhanced Integration and the Challenge of a “Two-Speed Europe” for the Western Balkan Candidate Countries

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### Abstract

In recent years Europe has faced many economic and social difficulties, with continued financial troubles, fear of sovereign defaults, rising unemployment and social tensions in several European economies. These concerns have led many to question the very viability of the euro and have raised the need to rethink the European Union project itself. The economic priorities of the EU have changed substantially. One of the main goals of the EU has become the achievement of a genuine Economic and Monetary Union. However, EMU enhanced integration may possibly create new dividing lines within EU and at least a “two-speed Europe”. After decades of integration, the EU is far from being a homogeneous entity. Large disparities exist among Member States and the differences in economic development are growing. Currently there are several different circles of European integration, such as: the EU and the Eurozone; the European Free Trade Association; and the Schengen zone. The process of reforming the EMU is not directly linked with the EU accession process. However, many politicians at an EU or a national level have started to make a connection between the two and to emphasize the “trade-off” between widening and deepening, arguing that the first would obstruct the second. The current paper will address the following interlinked questions: Does current EMU enhanced integration mean that Candidate Countries will not join a “first class” economic membership in the EU? Can the challenge of the potential establishment of a “two-speed Europe” be turned into an opportunity for the Western Balkan Candidate Countries to speak with one voice?

**Keywords:** Economic and Monetary Union, economic boundaries, accession, two-speed Europe.

## Introduction

After the recent economic and financial crisis that emerged in 2007-2008, it became apparent that the current architecture of the Economic and Monetary Union should be revised for the euro to remain stable in the future and the whole EMU project to remain sound and sustainable. Therefore substantial efforts have been invested in recent years and more efforts are planned in the years to come in order to establish a genuine Economic and Monetary Union. These efforts, however, increase the differences between the Euro area Member States and the non-Euro area Member States of the EU. The current status of the EMU and the expected reforms may substantially change the economic and institutional environment and possibly create new boundaries within the EU and with respect to the accession of new members.

Although, recently the enlargement process has relatively slowed down, EU enlargement continues to be a priority and sooner or later the EU will be composed of more Member States than today. However, current developments in the EU may lead to a situation where the current Candidate Countries join a quite different EU, a potential “two-speed EU”.

In this paper we analyze first the projects and prospects of establishing a genuine EMU in the coming years. In the second section we discuss the interaction between the deepening and widening of the EU and the alternative strategies and scenarios for the EU with a focus on the EMU. In the third section we provide information for some recent references and discussions about the need for a “two-speed Europe”. Finally, we focus our attention on the challenges before the Candidate Countries given the state of the EMU and the revived voices in favor of a “two-speed Europe”.

## Projects for Establishing Genuine EMU

The architecture of the EMU was designed in the 1990s when the global economic and financial world was quite different and when the establishment of the single currency was considered as a major success. It still remains a great achievement. However, as it has been admitted by EU leaders, the EMU continues to be a “house that was built over decades but only partially finished” (European Commission, 2015a). The single currency coupled with the single monetary policy performed via a single monetary institution, namely the European Central bank, which functions together with the close cooperation and coordination of economic policies among Member States. EMU is far from having a single economic policy. This creates disequilibrium between the monetary and economic “legs” of the EMU.

The first strategic documents from EU institutions that aimed at the achievement of a more genuine EMU were published in the second half of 2012. These are the European Commission Blueprint (European Commission, 2012) and the so-called Four Presidents Report (European Council, 2012), a report by the President of the European Council, prepared in collaboration with the President of the Commission, the President of the Eurogroup and the President of the European Central Bank. The final Four Presidents Report was published in December 2012 but it was preceded by first and interim reports that were published in June and October 2012. They outlined strategic but relatively realistic goals for ensuring further financial, economic and fiscal integration among Member States. The European Commission Blueprint was even more ambitious, including some measures that will be very difficult to realize not only in the medium but also in the long term.

The next milestone for EMU reforms is the so-called Five Presidents Report (European Commission, 2015a) that was published in June 2015. This time the lead is on the President of the European Commission, Jean-Claude Juncker and the fifth new president added to the group of contributing presidents is the President of the European Parliament. The other presidents are again the President of the ECB, the President of the European Council and the President of the Eurogroup. The Five Presidents Report aims to outline the reforms needed in order to achieve four main targets:

The establishment of a genuine *Economic Union*. There are several measures that are planned in this direction: the encouragement of Member States to establish national Competitiveness Authorities and a Euro area system of such authorities; the further strengthening of the Macroeconomic imbalance procedure; putting stronger focus on employment and social performance; and, achieving stronger coordination of economic policies.

The building of a *Financial Union*. This pillar of the EMU reforms would be based on the completion of the Banking Union and the necessary measures to create a Capital Markets Union. The Banking Union is designed for the Euro area Member States but it is open for the non-Euro area Member States through the so-called close cooperation mechanism (so far, there is no a Member State outside the Euro area that has established such a close cooperation with the ECB). The Five Presidents Report outlines the main objectives for the completion of the Banking Union, such as: the full transposition of some recently adopted directives; the implementation of the Single Supervisory Mechanism; the entry into force of the Single Resolution Mechanism (that became effective on 1 January 2016); the need for a European Deposit Insurance Scheme to be proposed and established; and, the improvement of

the effectiveness of the bank recapitalization mechanism at Euro area level. The Capital Markets Union, in contrast to the Banking Union, is currently designed for all 28 Member States of the EU.

Aiming for the establishment of a *Fiscal Union*. This is the area where the Five Presidents Report is less concrete, possibly due to the sensitivity of the issue and to the fact that EU Member States, including those from the Euro area, are not ready to give up their sovereignty in that sphere. The report proposes in short term the establishment of an advisory European Fiscal Board, having similar goals and objectives as the already established national fiscal boards. The report recognizes the need in the long term perspective of a future fiscal stabilization function for the Euro area.

Achieving a gradual *Political Union*. Economic, fiscal and financial integration would gradually lead to a more integrated political union among Member States. The key objectives are to achieve greater democratic accountability, legitimacy and the institutional strengthening of the EU.

The process of building a genuine EMU would comprise three stages in accordance with the Five Presidents Report. The first stage is in the period 1 July 2015 – 30 June 2017 and is named “deepening by doing” without any amendments to the basic EU Treaties. The second stage is called “completing EMU” and would take place in the period between mid-2017 and 2025. The stage after 2025 is called the final stage and would begin with all the envisaged measures already in place. The transition between first and second stage would be marked by the issuing of a European Commission White Paper in spring 2017 outlining the next steps until the end of second stage on completing the EMU.

In October 2015, the European Commission published a Communication outlining the measures for the first stage of EMU reforms after mid-2015 (European Commission, 2015b). This Communication was accompanied with some concrete legislative proposals. Among the concrete measures, proposed by the European Commission, are the recommendations for establishing national competitiveness boards, the proposed decision on the European Fiscal Board, the measures for achieving Financial Union, and the improvement of the economic governance tools.

It may be questionable how the EMU will be efficiently finalized with so many new national and EU-level institutions. The prospects for achieving a genuine EMU may also be questioned in terms of substance – even if all the measures envisaged in the Five Presidents Report are duly and timely adopted and implemented, this will not lead to a complete EMU. Nevertheless, the enhancement of the integration process in

the Euro area is building not new walls but at least new boundaries across Europe. After the EU accession of the current Candidate Countries, it may become much more difficult in the future to enter the club of the Euro area.

### **Interaction between Deepening and Widening of the EU. Alternative Strategies and Scenarios for the Future of the Single Market.**

The European crisis has made evident and deepened the problems related to the mode of integration in the European Union. This has caused growing divergence and increased inequality between different social groups, countries and regions in Europe. Alternative perspectives are necessary in order to foster cohesive developments in Europe. However, the processes which may promote worthy advances of cohesion are not yet on the horizon. On the contrary, divisions at different scales and of different types are still on the increase.

This new—quite explosive—background doesn't signal the end of the EU, but shouts out that its core features must be redesigned and receive broad popular support. The question is how.

The step-by-step-approach to integration “invented” in the 1950s has worked because it was based on the common assumption of a lacking pre-determined, “ideal” or optimal end state of regional integration in Europe. With this in mind, the future of the EMU may not be as open and unpredictable as the current state might suggest. After more than 50 years of successful co-operation and integration in Europe, it seems highly unreasonable and unlikely that the member states will simply completely “give up on Europe”.

We cannot give a complete picture here but we will sketch out a few implications of four possible future directions of the integration process with special regard to the implications for the EMU. These scenarios developed and updated by academia are not new but they are still relevant.

*a. Maintaining the Status-quo:* This scenario implies that there would be no major institutional or constitutional (EU Treaties) reforms. However, there may be an intensive use of the Treaty on European Union, including a renewed financial perspective for the EU. This general direction for the future development of European integration starts from the assumption that the EU has now reached its limits and a stable equilibrium. In other words, it has found its fundamental political and institutional order for the foreseeable future. As a result, the EU would be “floating” or “muddling through” at and around what was defined by the Treaty. That implies that there would be no tendencies towards disintegration. It does not

seem unreasonable to expect that an extended period of stabilization and consolidation might follow before the accession of new members. Nevertheless, the EMU might be forced to change considerably (institutionally and constitutionally) over the next decade in order to accommodate future enlargements.

*b. Spillover:* There are different strategies for this scenario:

- the “(federal) community strategy”, or deepening prior to and in order to enlarge;
- the “linear enlargement strategy” which foresees enlargement including minimal institutional adjustments, but no fundamental institutional and constitutional reforms requiring a treaty change;
- the “coupling option”, representing a close connection between enlargement and deepening, with deepening and enlargement both proceeding step by step (or new member state by new member state).

“Spillover” implies that there would be substantial step-by-step reforms and new projects in all policy areas leading to a greater visibility of the EU as an actor in external relations or the establishment of European economic governance in the Eurozone. The Union, in becoming bigger and wider, would simultaneously reform its institutional structures and enhance their efficiency. New aspects of economic policies would be moved to the European level; existing European policies would be further integrated and intensified. Member states would accept sharing more sovereignty in different policy areas. The legal output of the EU would grow constantly, covering more and more policy areas and replacing national regulations.

*c. Spill-back:*

- an intergovernmental approach, which leads to an enlarged, yet less integrated Union;
- the establishment of intergovernmental cooperation between three, four, six or more big member states outside the treaty framework;
- the evolution of a *Europe à la carte*, in which groups of interested member states practice limited functional or sectorial cooperation.

“Spill-back” therefore represents a reduction of the legal as well as of the living constitutional basis of the Union by a *de facto* or by a *de jure* retreat from the present treaty. “Spill-back” implies that there would be highly differentiated forms of cooperation emerging from the current EU-28. While in some policy areas the establishment of a *directoire* of few, big member states may extend the present scope and level of cooperation substantially. As a result, the EU might turn into a large free trade area with selected additional, flexible sectors of deeper integration.

This general direction for the future development of European integration seems very unlikely for the EU as a whole though the current “Brexit” prospects show the attractiveness of this scenario for some Member States or for some political factions. . In addition, with the economic and financial crisis, we have seen a mushrooming of initiatives and institutions trying to fix the financial architecture of the Eurozone; whereby new treaties have been signed, such as the Treaty on Stability, Coordination and Governance (the so-called Fiscal Compact), the Euro Plus Pact, the Two Pack and the Six Pack. All these agreements apply to different member states. The Treaty of Lisbon builds on the possibility of permanent structured cooperation or enhanced cooperation introduced by the Treaty of Amsterdam followed by the Treaty of Nice: a group of countries willing to cooperate further in a certain field are allowed to do so within the framework of the Union’s non-exclusive competences. (This type of cooperation is different from the EU opt-out that is a form of cooperation between EU members within EU structures, where a limited number of states are allowed to refrain from participation (such as the EMU, or the Schengen Area). Nevertheless, we are of the opinion that though such initiatives and grouping might continue to exist, they will not redefine the main structure, the spine of the EU integration.

*d. The re-invented EU (“two-speed Europe”):*

- “core Europe”, representing institutional (and constitutional) deepening within a group of “willing” and “able” member states;
- “variable geometry”, representing a network of parallel groups of member states which pursue sectorial integration in different policy areas.

This direction of a re-invented (or newly invented) Union is represented by the reduction of the scope of the Treaty (TEU) that means a reduction of the number of member states for certain policies. Thus, the Union could develop into a multi-level system of governance with overlapping spheres of competence which could, although making the EU (even) more complex, lead to the emergence of innovative instruments and procedures for problem-solving. Further deepening and widening are not excluded, but become more and more unlikely and difficult to achieve for all 28+ member states simultaneously. The institutional structure would be re-established to fit the demands of its 28+ member states. States that are ready for deeper integration of their strong economies would be able to move forward by creating a strong union which could be based on federalism. On the other hand, members like Denmark who are not willing to join the Euro-zone would remain in the EU within a second group with less powers but with all the benefits of the single market. New forms of differentiated integration could be suggested as solutions for the emerging dilemma between widening and deepening. The obvious problem in connection with the

introduction of new forms of co-operation and integration is that new dividing lines would evolve.

Going from theory to real developments, we may now pose the question: Is a “Two-speed Europe” a mirage or a reality?

### **“Two-speed Europe” – Mirage or Reality**

The clearest dividing line within the EU lies between the Euro area and non-Euro area Member States. One of the main reforms that are currently being discussed at EU level is the need to establish a finance minister and a sort of treasury for the Euro area. This may be one of the main measures towards establishing a genuine Fiscal Union in the Euro area. This measure will require some joint decision making on fiscal policies at the EU level, although currently it is not possible to think about a complete lifting of national sovereignty in budgetary and tax issues. Any steps in that direction would be difficult to make, taken into account the need to amend the founding EU Treaties and to achieve unanimity among current Member States. It is remarkable that not only the leaders from EU institutions have called for such a move towards Euro area treasury but even the Presidents of the central banks in France and Germany.

Other national policy-makers have also called recently for at least a “two-speed Europe”. One of them is the Italian State Secretary on EU affairs. He has voiced concern about the need for the current EU to continue to exist as a large area where there is single Internal Market and freedoms. However, he stresses that there is also a need for a smaller and better integrated circle of Member State that would apply more integrated policies, namely the policies of renewed and genuine EMU. He admits that a future Minister of Finance of the Euro area should be elected by and should be accountable to the European Parliament (Vesti, 2016).

It is controversial, but this possible “two-speed Europe” approach is an argument employed by the pro-EU oriented people in the United Kingdom who advocate the preservation of EU membership status for the UK and are against Brexit. A “two-speed Europe” may be regarded as an opposition to the principle that many British citizens do not like - the principle of laying the foundations of an ever closer union among the peoples of Europe (Institute for European Policies, 2016).



## **Challenges before Candidate Countries Given the State of the EMU and the Revived Voices for a “Two-speed Europe”**

The European Union started 2015 with a newly elected European Parliament, a new Commission, a new permanent President of the European Council and a new High Representative for Foreign Affairs and Security Policy. The EU ambitions for the coming period are set out in the ‘Strategic Agenda for the Union in times of change’ adopted by the European Council in June 2014 and in Commission President Jean-Claude Juncker’s Political Guidelines, which he presented to the European Parliament in the same month. These ambitions subsequently found their way into the Commission’s Work Programme for 2015, which was published in December last year.

In 2015 the EU found itself in a complex world. MS economies are showing tentative signs of recovery, but it is still brittle. EU security and values are under pressure, from both inside and outside the EU.

Many argued that if the Eurozone survives the crisis it will plainly require deep reform of the EU Treaties. In addition, many politicians and EU citizens perceive the enlarged EU as increasingly ineffective. Trust in EU enlargement policy significantly declined in EU Member States and in candidate countries as well.

The process of reforming the EMU is not directly linked with the EU accession process. However, many politicians at both an EU and national level have started to make a link between the two. Surprisingly for some people and disappointing others, especially those aiming for EU accession, in his first public announcement as elected President of the European Commission, Jean-Claude Juncker stated that in his mandate until 2019 there will be no accession of new Member States to the EU.

Later, he developed his strategy, explaining that after future enlargement, the EU would be on two speeds. That changes even the long-existing debate in the EU on the deepening integration process (including, through EMU, establishment and improvement), *vis-à-vis* enlarging the European Union. This changes the debate into a new concept – “enlarging and dividing within the EU”. EU accession will abolish some economic boundaries with the inclusion of the new Member States in the EU Internal Market and the EU common policies. However, the Euro area Member States and politicians started to build boundaries inside the EU, meaning that the current Candidate Countries will join quite a different EU in the future.

If there were any doubts about properly understanding the current Commission President, during his speech at a conference in Brussels in November 2015 he made his ideas much more clear: “I think that, eventually, it will no longer be possible that

33, 34 or 35 states will proceed with the same speed and the same momentum in the same direction ... The community shall rethink its structure, in order [that] Member States are able to be included in the different policies at different speeds, if they wish so ... One day we should rethink the European architecture with a group of countries that will do things, all things, together and others who will position themselves in an orbit different from the core” (Reuters, 2015 and Dnevnik, 2015).

The above marks a major change in the position of the EU Commission - the guardian of EU treaties, since 2011 and a new or at least, a spoken-out, “threat” that enlargement will only be possible at the price of a “two speed Europe”. Speaking in Berlin on 9 November 2011 former president of the EU Commission, José Manuel Barroso, spoke firmly against the raised voices for “two speed Europe” and in particular to the then French president Mr. Sarkozy: “... a split union will not work. This is true for a union with different parts engaged in contradictory objectives; a union with an integrated core but a disengaged periphery; a union dominated by an unhealthy balance of power or indeed any kind of directorium [sic]. All these are unsustainable and will not work in the long term because they will put in question a fundamental, I would say a sacred, principle—the principle of justice, the principle of the respect of equality, the principle of the respect of the rule of law. And we are a union based on the respect of the rule of law and not on any power or forces. It would be absurd if the very core of our project—and economic and monetary union as embodied in the euro area—so I say it would be absurd if this core is treated as a kind of “opt out” from the European Union as a whole.” (Jose Manuel Barroso, 2011)

In our opinion, the EU’s deepening (supranational integration) and its further enlargement (expansion of membership) may hardly be considered a “trade-off”. The alleged “conflict” of widening versus deepening must be dismissed as such. As these two aspects are intertwined, it would be wrong to consider them separately. What is at stake is not their conflict but their interaction.

In recent years many scholars and politicians have overemphasized the “trade-off” between widening and deepening, arguing that the first would obstruct the second. But the long and winding road of the EU demonstrates the contrary: deepening and widening go hand in hand. Enlargement has constantly affected the EU’s own functioning and has produced a systematic deepening of supranational policy-making capacities. As the governance and structures of the euro area undergo significant change, more should be done to engage candidate and potential candidate countries so that the changes—and the demands that will ultimately be laid on them—are clearly understood.

## Conclusions

The creation of a more flexible EU of variable geometry, if done properly, by keeping the euro open to countries that want to join and deepening the single market for those that do not (like Britain), could ease many of the existing tensions. But done incorrectly, this would be a recipe for the breaking up of Europe. We would start talking about two separate Europes instead of a “two-speed Europe”. Because of this, we do not regard the formal establishment of “two-speed Europe” as a positive move and new Member States such as Bulgaria, Romania and Croatia should stand against policy changes in this direction. Furthermore, the current Candidate Countries should not be in favor of the legalization of “two-speed Europe” regardless of the voices that this may be the only way to open the door for their accession. It is true that Candidate Countries do not have a formal voice in the setting of the current EU policies and objectives. However, a mechanism should be found for them to at least have a say in what kind of EU they would aim to be a part of. Recently, the Serbian Prime Minister declared that his country is less interested in the European Integration process, possibly because of this second class membership status but also because of the potential United Kingdom exit from the EU.

The challenge of the potential establishment of a “two-speed Europe” should be turned into an opportunity. This should be the opportunity for the current new EU Member States and the future new Member States (currently Candidate Countries, especially the Western Balkan countries) to speak with one voice in Europe and to better defend their priorities and interests. In response to such uncertainties, some countries in Europe suit their own grouping in formal and informal alliances, which are supposed, *inter alia*, to formulate and express their joint and thus stronger opinion. The Visegrad, Baltic and Scandinavian group of alliances were renewed. From these events, the Balkan countries seem to be missing. The possible formation of a formal or informal group of the Balkan countries may serve as the vanguard of or at least persuasive evidence for their further integration into the EU.

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