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Georgios Maris[a] & Pantelis Sklias[b]

[a] School of Law and Social Sciences, Neapolis University Pafos, Pafos, Cyprus

[b] Department of Political Science & International Relations, University of the Peloponnese, Corinth, Greece

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France, Germany and the New Framework for EMU Governance

GEORGIOS MARIS[a]* & PANTELIS SKLIAS[b1]
[a]*School of Law and Social Sciences, Neapolis University Pafos, Pafos, Cyprus,* [b]*Department of Political Science & International Relations, University of the Peloponnese, Corinth, Greece*

ABSTRACT *The European crisis is the best case study for examining both the vulnerabilities of Europe's framework for economic governance and the very process of European integration itself. This statement is true for several reasons: first, because the European crisis is the most serious crisis the European Union has faced to date; second, because of the crisis, limits on the process of economic integration in Europe have been put to a real test; and third, because the main causes of the crisis are tied into the framework for economic governance that has been developed over the last few decades and therefore are connected to the very process of European unification itself. The primary aim of this paper is to demonstrate whether and to what extent the new framework for economic governance in Europe is largely a result of interstate bargaining and consequently whether national preferences continue to play an important role in the framework's general transformation. The economic crisis showed that important issues in economic policy concerning the change in economic governance and the role of the nation-state, which were 'swept under the carpet' in recent decades, must be resolved to make the European venture viable.*

KEY WORDS: intergovernmentalism, EMU, governance, integration, crisis

1. Introduction

The European crisis, which manifested itself through the Greek economic crisis, is the best case study for examining both the vulnerabilities of Europe's framework for economic governance and the very process of European integration itself. This statement is true for several reasons: first, because the European crisis is the most serious crisis the European Union (EU) has faced to date; second, because of the crisis, limits on the process of economic integration in Europe have been put to a real test; and third, because the main causes of the crisis are tied into the framework for economic governance that has been developed over the last few decades and therefore are connected to the very process of European unification itself. The primary aim of this paper is to demonstrate whether and to what extent the new framework for economic governance in Europe is largely a result of interstate bargaining and consequently whether national preferences continue to play an important role in the framework's general transformation.[2] Although the process of European integration is too complex to be comprehended from one single theoretical

**Correspondence Address*: School of Law and Social Sciences, Neapolis University Pafos, Pafos, Cyprus. Email: g.maris@nup.ac.cy

viewpoint, the crisis has raised old questions about European integration concerning the centrality of the state and concerning interstate interactions. Does intergovernmentalism triumph over supranationalism? It is clear that the issue of how the framework for economic governance has transformed is no longer an issue of ‘low politics’ but rather a major issue of ‘high politics’, because the autonomy and sovereignty of national governments within the realm of economic policy are now at risk. In other words, the nature of the changes currently being suggested in the context of economic governance in Europe is no longer in line with a less confrontational environment. At the level of the Economic and Monetary Union (EMU), as the integration process advances, there is less room for transferring national sovereignty to supranational bodies, and the importance of an intergovernmental stance increases. The economic crisis showed that important issues in economic policy concerning the change in economic governance and the role of the nation-state, which were ‘swept under the carpet’ in recent decades, must be resolved to make the European venture viable. In other words, as long as no alternative radical economic policy mechanisms, options, or ideas are proposed, the prominent German ordo-liberal and austerity-focused approach will continue to dominate the agenda of EU politics (Clift and Ryner 2014).

This paper also claims that intergovernmentalism has been the key factor of changing economic governance in Europe. To understand the process of change in economic governance in Europe, it is first necessary to understand the role of interstate bargaining at a European level primarily due to the national preferences and interests of Member States. Moreover, it is essential to stress the role of other factors that could interfere with this change. Therefore, in addition to evaluating the new framework for economic governance in Europe, one also must examine the conditions under which the specific changes were developed, adopted and supported at the European level. In fact, to comprehend the old and the new political economies of economic governance in the EU, one must highlight not only the conditions under which economic policy actions and economic governance frameworks were developed but also the visions of the main actors (Clift and Ryner 2014). It would appear that although a series of other factors are involved in the process of transformation of the framework for economic governance in Europe, the interests of national governments, which reflect the preferences of various socio-economic actors, largely continue to affect outcomes. This paper stresses that important intergovernmental elements largely lie behind any decisions concerning the further unification of economic policy within the EMU. Thus, the process of transforming the framework for economic governance continues to be primarily an intergovernmental game based on the interests of Member States.

Of course, this observation does not mean that we should downplay the role of political and moral arguments primarily developed after the end of World War II about the creation of the EU. Moreover, the Community Method continues to affect the framework for economic governance in Europe in its own way. This effect is most clear in the case of the monetary dimension of the EMU. Thus, the supranational decision-making method plays an important role in the process of changing the framework for economic governance in Europe. However, in the economic dimension of the EMU from 2010 onwards, primarily Germany and France have attempted to change the framework for economic governance in Europe. Their efforts are based on an intergovernmental approach focused on the sovereignty of the nation-state compared with supranational players and on the intergovernmental method instead of the Community Method. In this regard, our aim is to examine in depth the behaviour of France and Germany in changing the new framework for economic governance in Europe. We have taken these two countries as examples because they are the EU Member States that decisively influence the development and transformation of this framework. These two countries are prominent in the process because, as Heipertz and Verdun have argued, 'when Member States' governments bargain with one another, the largest countries have the greater influence' (Heipertz and Verdun 2010, 20). Over the years, Franco-German relations have driven the integration process to a significant degree (Cole 2010). Unless the views of these two countries converge, no important issue of 'high politics' can advance in the EU. To a major degree, in regard to transforming economic governance in Europe, as more restrictions to do with the interests and sovereignty of those two countries are introduced, the limits on the process of European unification clearly emerge, and the EMU appears more likely to remain in a prolonged stated of imbalance.

This paper is structured as follows. Section 2 elaborates the theories of European integration that constitute our theoretical context. Section 3 describes the conditions under which the initial framework for economic governance in the EU emerged. Section 4 shows not only how the EU responded to the crisis but also how Germany and France affected the transformation of the new framework for economic governance in Europe. Section 5 concludes the paper.

2. Theories of European Integration

This section of the paper attempts to synthesise the various viewpoints about the creation of the EMU into a wider theoretical framework. This step is necessary because the EU and the process of European integration are too complex to be viewed from any one single theoretical perspective (Rosamond 2000). The literature contains a series of references as the key factors that have shaped the European monetary framework. This paper will primarily focus on the long-standing debate between neofunctionalism and intergovernmentalism. We argue that the European crisis resurfaced old questions about European integration. In our view, what plays—and will continue to play—a dominant role is the nation-state and its interests.

The reasons why the EMU was established can be classified in various ways. The political science literature to date has largely presented two approaches. The first refers to Amy Verdun's attempt to classify the reasons why the EMU was established by examining a set of political theories of integration that tie together hypotheses and forecasts (Verdun 2002). Verdun argues that we can group the factors that play an important role in the development of European monetary unification into three main categories: (a) the role of actors and institutions, (b) mechanisms and (c) international structural factors. The second approach presents the framework within which monetary integration emerged by examining four different levels of analysis: global, European, national and domestic levels (Sadeh and Verdun 2009). According to Sadeh and Verdun (2009), the EMU is the result of a European reaction to global challenges that was feasible because European institutions had been established and that was primarily suggested by the Franco-German pact. As a result, if we suppose that the Member States place their interests on a scale, as the theory of instrumental rationality argues for humans to do, then they attempt to satisfy as many interests as they can, beginning with what they consider their most important issue. In this case, the

Member States prefer to remain protected in the global political and economic environment.

It is very difficult to analyse the process of economic integration of Europe from realist or neorealist perspectives either because theorists have not given these perspectives particular importance (Stone 1994) or because theorists are faced with important theoretical problems (Grieco 1995). The same also appears to hold true for Marxist analyses. Furthermore, although early theories of European integration significantly affected the subsequent course of development in European studies, these theories were called into doubt because of empirical developments within the EU. In effect, almost all early attempts are theoretical constructions designed to eliminate international conflict (Rosamond 2000).

Under those conditions, attention must be given to theories that were developed from the 1950s onwards. The first is neofunctionalism, which was primarily developed in the works of Haas (1958, 1964) and Lindberg and Scheingold (1970, 1971). Neofunctionalism stresses that integration is the result of functional pressures exerted because of integration in low-politics sectors. An important role is played in this process by higher supranational actors that have been established for this purpose and that contribute a great deal to the unification process. Under these conditions, wider social groups transfer their loyalty to the new supranational institutions. Neofunctionalism can explain the first attempts to unify Europe from the Treaty of Paris onwards to a significant degree because integration in one economic sector [the European Coal and Steel Community (ECSC)] created functional pressures that led to the European Economic Community (EEC). However, it cannot explain the creation of the EMU with the same degree of cogency. From 1985 to the end of 1990, following a period of extreme criticism, neofunctionalism began to be revived because of changes that were occurring at that time (Tranholm-Mikkelsen 1991). The key elements of this revival were, *inter alia*, the White Paper on Completion of the Internal Market, the Single European Act and the Delors Report. Neofunctionalism seems unable to explain why the EMU has not yet advanced to a more integrated stage of unification. This inability is largely because the supranational institutions that have already been established do not have the appropriate jurisdiction to proceed with the economic integration of Europe on their own. In other words, the transition to a supranational level is not such a reasonable dynamic, automatic and depoliticised process because a political union could not be developed without considering the views of European citizens (Schmitter 2005). Despite that limitation, there is an element of neofunctionalism that has become worthy of further attention in recent years: supranational decision-making has become increasingly more technocratic (Rosamond 2000).

The response to neofunctionalism came quickly from the intergovernmental approach. Intergovernmentalism stresses that in areas of high politics in which either the autonomy of governments or important issues of national identity are at risk, unification is difficult to achieve (Hoffmann 1966). Although Hoffmann's view that states are the key players in global politics reflects realistic positions, he considers that national interests are the result of domestic forces (Hoffmann 1995), which sets his views apart from the stance taken by realists. Therefore, one of the most important elements of the theory of intergovernmentalism is that it emphasises the supremacy of interstate bargaining in setting the pace and degree of European unification (Τσινισιζέλης and Χρυσοχόου 2007). According to intergovernmentalism theory, supranational institutions, such as the European Commission and the European Court of Justice (ECJ), do not play an important role in the process of European integration. The same holds true for the role and influence of international players and coalitions and the extension of functional objectives (Τσινισιζέλης and Χρυσοχόου 2007).

Intergovernmentalism played an important role in the subsequent development of Liberal Intergovernmentalism (LI), which is thought to be the most important example of an attempt to theorise European integration (Rosamond 2000). In effect, Moravcsik (1993a, 1993b, 1998) constructed a two-level game model that consists of a liberal theory of preference formation and an intergovernmentalist analysis of strategies for Member States reaching agreement. Therefore, LI, which relies on the interaction between domestic and international politics and attempts to explain the EU as a successful example of an intergovernmentalist regime, also includes elements from realism and from neoliberalism (Cini 2007).

LI is a model comprising three different stages. These stages combine (a) a liberal theory to explain how national preferences are formed, (b) an intergovernmentalist bargaining model at the EU level and (c) an 'institutional selection' model that places emphasis on the role of institutions and on the provision of reliable commitments to the governments of Member States (Pollack 2005). Therefore, LI emphasises both the role of economic interests and the importance of institutions in the process of European integration and stresses the central role of the state, the importance of domestic economic interests and negotiations between national governments (Gilpin 2001). The principles on which the theory of LI rests argue that political integration is the result of Member States' interests, which transfer various competences and powers to European supranational institutions only if they can take control of various policy sectors (Jensen 2007). For integration to advance, the economic or trade interests of the Member States must overlap. According to intergovernmental theory, the most important historical intergovernmental agreements, such as the Treaty of Rome or the Treaty of Maastricht, were the result of a periodic process of preference convergence among the most powerful Member States. These states offered incentives to the smaller states and transferred limited powers to European supranational institutions, which effectively remained the servants of the Member States (Pollack 2005).

Both the neofunctionalist and intergovernmentalist approaches have been severely criticised in recent decades primarily because they cannot explain day-to-day European politics, as the EU is inundated daily with the actions of non-state actors. For this reason, in recent decades, theorists of European Studies have shifted their focus to medium-range theories; neofunctionalism and intergovernmentalism cannot explain the full complexity and dynamism in which politics is conducted within the EU (Rosamond 2000). For example, one cannot ignore that in recent decades, supranational institutions such as the Commission or the European Parliament have come to play an important role in EU affairs. Moreover, the ECJ has traditionally acted as an engine of integration even in times when the consensus between states for further integration was lacking. Under these conditions, in recent years, a series of new approaches has emerged in the attempt to theorise the EU. For example, multi-level governance attaches importance to the existence of a set of super-imposed multi-level coalitions (Marks, Hooghe, and Blank 1996). According to Marks, Hooghe, and Blank (1996), the sovereignty of nation-states within the EU has been reduced because of collective decision-making and supranational institutions. Alternatively, the new institutional approach treats institutions as tools for developing and shaping political behaviour that go beyond typical governmental bodies and introduces well-established operating procedures for action (Bulmer 1993).

This paper advances the intergovernmental aspect of the factors that change economic governance in Europe to explain in depth the recent developments of the framework for economic governance in the EMU. In contrast with other important contributions that follow LI's tripartite analysis (Schimmelfennig 2015), this contribution follows a more eclectic approach, as it focuses on the political economy of the new framework for economic governance in the EU and the conditions under which autonomous economic policy is narrowed. In this regard, the initial and the new developments in economic governance in the EMU are combined with the current crisis and the theory of European integration. In this regard, we analyse not only whether and to what extent the new framework for economic governance can be understood through the prism of intergovernmentalism but also to what extent interstate bargaining and national preferences are reflected and shaped within the new framework for economic governance in the EU.

3. Conditions Under Which the Initial Framework for Economic Governance in Europe Emerged

The initial framework for economic governance in Europe was created by the Treaty of Maastricht. The Treaty of Maastricht was not the result of straightforward, unproblematic negotiations. Wyplosz (2006) argues that during the negotiations that led to the Treaty, it became clear that France's views did not match those of Germany. Germany placed emphasis on the importance of economic policies and of convergence, whereas France stressed the creation of new institutional tools. Thus, the strategy adopted in the Treaty of Maastricht emphasised the importance of two principles: gradual transition and convergence (De Grauwe 2009). Due to the differing approaches taken by France and Germany, which reflected the old dispute between 'economists' and 'monetarists',[3] the Treaty of Maastricht included both supranational and intergovernmental decision-making features. The main role in the supranational approach was first played by the European Central Bank (ECB) and subsequently by the Commission, the ECJ and the European Parliament. Conversely, the intergovernmentalist method is associated with the increased role of the European Council in the unification process (Puetter 2013). Thus, the EU's governance system is a *sui generis* system that is characterised by both community and intergovernmental methods (Delors 2013).

In effect, during the negotiations for the Treaty of Maastricht, the Member States agreed to transfer significant aspects of their sovereignty to the supranational level only if national governments could control decision-making capabilities (Fabbrini 2013). In other words, in addition to being technocratic in nature, economic governance in Europe is above all political because it includes political agreements that satisfy the strategic interests of the Member States and their governments (Dyson 1999b). Thus, the convergence of interests and preferences at the European level produced two heterogeneous consequences relating to the initial framework for economic governance: (a) Europe acquired an unstable form of economic and social governance (Begg 2010), and (b) a stable and differentiated context of economic policies was put in place (Dyson and Marcussen 2010). The result was the creation of the EMU with strong elements of asymmetry under which more wide-ranging economic governance was rather impossible (Verdun 1996, 2000).

What were France and Germany's stances during the negotiations for the Treaty of Maastricht, and under what conditions was an agreement reached? The Treaty of

Maastricht was the result of a bargaining game that is best explained by the principles of LI. For that reason, during negotiations, the two European leaders of France and Germany kept the European Commission at a distance. As Dyson (1999a, 27) noted, 'The French favoured this rule from arguments rooted in national sovereignty and democratic legitimation; the Germans from arguments related to preserving the independence of the ECB.'

For Germany, the creation of the EMU was the best means to support the country's economic growth based on the neoliberalist principles of the open market, free trade and deflationary monetary policy.[4] Moreover, the establishment of the independent ECB and the subsequent Stability and Growth Pact (SGP) was a means of promoting those objectives established by the monetarist revolution and its domination over Keynesianism (McNamara 1998). After monetarist ideas were adopted, these objectives would be best promoted through an independent central bank, price stability and fiscal discipline (currently, fiscal austerity) without the possibility of coordinating fiscal policy in the medium term (Hall and Franzese 1998). Through this process, Germany favoured its business interests. German businesses would enjoy advantages from the EMU-mandated ban on the devaluation of national currencies as an opportunity to increase exports (Hall 2012). However, at the same time, other states would lose their ability to devalue their currencies and thus a chance for their businesses' products to remain competitive. In addition, if these countries were to follow different policies based on a more outward-looking strategy, the expected results would not accrue because of deviations existing in the institutional structure of the peripheral states (Hall 2012). Under the aforementioned conditions, one could argue that Germany sacrificed the German currency to introduce a culture of economic stability based on specific rules across the entire EMU (Jamet 2011). German political parties and the CDU in particular strategically used the stability culture, which is related to low inflation and fiscal consolidation, to legitimise different strategic choices in Germany (Howarth and Rommerskirchen 2013). As Clift and Ryner (2014, 140) state, 'ordo-liberal notions of appropriate macroeconomic policy institutions and settings, prevalent in Germany and to some extent reflected in the ECB and the European Commission (EC), constitute the ideational parameters within which macroeconomic policy makers must operate.' Thus, it was clear from the outset that Germany would not accept the euro if monetary rules were not designed based on the German model of economic growth[5] (Mussler 2011) within the contemporary market-constitutional context (Clift and Ryner 2014).

Conversely, for France, the creation of the EMU was a means to compete against Germany on an economic level and to use the EMU to allow France to come closer to its own economic model by increasing public spending, increasing wages, and inflation, to stop the foreign exchange crises and debt crises of the 1970s and 1980s (Moravcsik 2012). France attempted to balance its relationship with Germany by reducing the credibility of the German economic model (Dyson 1999a). However, that change required a compromise with Germany and with other countries that was never achieved. This omission is considered the EMU's greatest failure (Moravcsik 2012). In addition to being a political plan (Dyson 1994; Dyson and Featherstone 1999), the creation of the EMU also incorporated a 'Bind Leviathan' that represented an immense challenge to French views about the sovereignty of the state and legitimacy (Dyson 1999a).

Overall, the new global financial and monetary system that was created almost four decades ago limited autonomous economic policy, left no room for radical manoeuvres and influenced the development of economic governance in the EU (Clift and Ryner 2014). For Schimmelfennig (2015, 192), this ideational path also affects the current decision about more integration. Under the aforementioned conditions and as the theory of LI explained, Germany would not have established the EMU if the other European countries did not agree to adopt the German economic model at Maastricht (ordo-liberalism), because Germany—in contrast to France—was the only country that could persuade the EU of the superiority of its model of economic growth. France's economic (in)effectiveness in the 1970s and 1980s left no doubt about German economic superiority (Dyson 1999a). However, Germany overlooked that the other Member States did not meet the political, economic and cultural requirements to adopt Germany's model in reality. Although it was debated occasionally, the EMU's ability to achieve real convergence was overlooked because the EMU never became an Optimal Currency Area and never acquired the necessary mechanisms for fiscal transfers and for the rescue of Member States in times of crisis.

4. Addressing the Crisis

4.1 New Framework for Economic Governance

Until 2008, any reactions to the global economic crisis originated from the expectations and interests of each individual state and varied widely (Schirm 2011). The size of the global economic crisis, however, increasingly prompted actions at the European and global levels. However, the challenge proved to be exceptionally difficult for Europeans, particularly outside the field of monetary policy, in which there was already a well-organised supranational decision-making system in place centred on the ECB (Quaglia, Eastwood, and Holmes 2009). For example, although there was a need to create a new supranational regulatory and supervisory financial system, the Member States did not appear to have the necessary determination to carry this through and limited themselves to making merely pronouncements about these matters (Begg 2009). Despite announcing coordinated policies, the EU Member States preferred to follow separate paths in terms of both reforms and packages designed to bolster their economies as they sought to combat the crisis (Schirm 2011).

For the major part of 2009, on the one hand, the European crisis in the eyes of EU leaders was still primarily a banking crisis. The problem with this situation, according to Pisani-Ferry and Sapir (2009, 21), was

> the management of the crisis has taken place according to the assignment of competences that exists in the EU: the ECB and national central banks outside the euro area have acted as liquidity providers, national governments have dealt with financial stability, and the European Commission has enforced competition disciplines. Although some of these players, notably the ECB, have gone beyond the pre-existing script, none has gone beyond its pre-existing role. Especially, there has been no EU-financed bail-out of ailing transnational institutions.

On the other hand, particularly for the cases of Greece, Ireland, Portugal and Spain, the crisis was a result of irresponsible governments (Scharpf 2013).[6] The Greek debt crisis officially became a European problem for the first time on 8 December 2009, and from then on, there was only one topic of discussion at the European level: how can the European crisis be solved? In a speech he gave to the Centre for European Policy in April 2010, then-European Commissioner Olli Rehn stressed that within the EMU, there was no political push to strengthen the coordination of economic policy; therefore, 'M is much stronger than E in the EMU. It is high time to fill the E with life'.[7] In effect, Olli Rehn stressed that the economic dimension of EMU had to be bolstered to be able to deal with the crisis and to create the conditions for the long-term viability of the EMU. Of course, that did not mean that changes would be made to the monetary framework, but rather that changes would be primarily supranational. In light of that point, from early 2010 to 2013, the crisis was the main reason for the creation of significant policy responses in the monetary and fiscal fields, and a new, highly complex framework for economic governance was implemented (Buti and Carnot 2012; Van Rompuy 2010).

At the Euro Summit of 7–9 May 2010, European leaders announced that all European institutions were duty bound to combat the economic crisis and ensure the Euro Area's economic stability. They characteristically said, 'All the institutions of the Euro Area (Council, Commission, ECB) and all Euro Area Member States agree to use the full range of means available to ensure the stability of the Euro Area'.[8] From that time on, in addition to the bailout packages for peripheral countries, quite a few important changes have been made to the framework for economic governance in Europe in relation to both the monetary and economic dimensions of the EMU. Due to the supranational character of the monetary dimension, changes that were made in most cases were far removed from the intergovernmental decision-making method. Conversely, the changes made to the economic dimension of the EMU were primarily intergovernmentalist in nature, but, of course, there were exceptions to that rule.

Regarding the economic dimension of EMU, the main changes to economic governance include

(a) Creation of an interim programme in May 2010 for the emergency financing of the European Financial Stability Mechanism (EFSM) and a special-purpose vehicle called the European Financial Stability Facility (EFSF).[9]

(b) Approval of the European Semester process in September 2010, a comprehensive, multilateral system for economic and fiscal supervision to coordinate evaluation of the fiscal and structural policies of Member States.[10]

(c) At the European Councils held on 24–25 March and 23–24 June 2011, the SGP was amended via the Six-Pack,[11] which included six legislative proposals to bolster economic governance through more wide-ranging and improved supervision of fiscal and macroeconomic policies and an attempt to improve economic cooperation and mutual supervision on issues of economic policy via the Euro Plus Pact.[12]

(d) The Treaty Establishing the European Stability Mechanism (ESM)[13] was signed for the first time in July 2011. This is a permanent mechanism to deal with crises and safeguard the financial stability of Europe, and it was intended to replace the EFSM and EFSF.

(e) The Treaty on Stability, Coordination and Governance in the EMU (the Fiscal Compact) was signed on 2 March 2012.

(f) The report 'Towards a Genuine Economic and Monetary Union' was presented on 5 December 2012. It contained a roadmap to strengthen the EMU by creating a unified financial framework, a unified fiscal framework and a unified framework for economic policy, although it also ensured the necessary democratic legitimation and accounting in decision-making.

(g) The central supervision of national budgets was improved via the Two-Pack.[14]

Conversely, concerning the monetary dimension of the EMU, the situation was somewhat easier given the pre-existing supranational framework and the role the ECB had played.[15] In that sense, the ECB's main strategic objective was the 'sustainability of EMU as such' (Torres 2013, 297). Considering exhortations from the European Council to do whatever it could to restore stability to the euro area, the ECB took a series of measures to address serious problems in the financial market.[16] These problems not only included conventional monetary policy measures but also the purchase of Greek debt from the secondary bond market via the Securities Market Programme. Moreover, in 2011, the ECB began to change tack, reacting in a more substantive manner to the challenges. This change was partly due to a change of the guard in the upper echelons of the ECB. The ECB's new president, Mario Draghi, managed to win over the markets almost immediately by introducing the long-term refinancing operation, which gave European banks more than € 1 trillion in the form of cheap 3-year loans (Hodson 2013). Moreover, on 26 July 2012, the president of the ECB stated at a conference in London, 'Within our mandate, the ECB is ready to do whatever it takes to preserve the euro. And believe me, it will be enough'.[17] On 2 August, he stated, 'The Governing Council, within its mandate to maintain price stability over the medium term and in observance of its independence in determining monetary policy, may undertake outright open market operations of a size adequate to reach its objective'.[18] One month later, in September 2012, there were another two important developments. The first related to the option for ECB to purchase bonds from the secondary market through the so-called Outright Monetary Transactions programme.[19] The second related to the Commission's proposal to set up a single banking supervisory mechanism by assigning new powers to the ECB in the context of the banking union.[20] However, although the ECB is without a doubt the institution that has reinforced its role and its political influence most in the last six years, it is doubtful whether the ECB can act as a Lender of Last Resort without further fiscal and banking integration[21] (Hu 2014).

All the aforementioned developments in both the monetary and economic dimensions of economic governance in the Eurozone constitute a series of complex typical forms of integration that are the result of an intergovernmental approach in most cases. These typical forms of integration can only save the Eurozone from collapsing. They cannot resolve the Eurozone's problem. Concerning the issue of the transformation of economic governance in Europe, the introduction of additional restrictions to do with interests and sovereignty clarifies the emerging limits on the process of European unification and suggests that EMU will remain in a prolonged stated of imbalance.

4.2 The Conditions Under Which the New Framework Emerged

Under what circumstances was the new framework for economic governance in Europe established? What factors primarily affected this transformation? In a speech in Cologne on 13 September 2011, the President of the Bundesbank, Jens Weidmann, stated that there were two paths the new economic architecture of Europe could take; either return to the principles set out in the founding treaties or move towards a federalist transformation of the system, with everything that entailed.[22] The second solution is quite clearly a move towards political union. Weidmann's statement hides the essence of the process of European integration, whose most important aspect affects developments in the transformation of economic governance. That element is the issue of transferring national sovereignty to European supranational institutions. In other words, when the European crisis occurred, although Member States declared they were willing to accept greater control over economic policy at a national level, the majority of them proposed solutions that were based on the intergovernmentalist game (Fabbrini 2013). In this regard, the European Council role was placed at the centre of the EU's political and economic transformation (Dinan 2011; Puetter 2012; Schwarzer 2012). It is no coincidence that even in the Treaty establishing the ESM, the European Commission only played an advisory role, which further reduced its credibility[23] (Liddle, Cramme, and Thillaye 2012; Puetter 2012; Menz and Smith 2013). Furthermore, the European Parliament appears to have found itself in an even worse position (Fasone 2012; Schwarzer 2012; Manoli and Maris 2015). According to Fabbrini (2014, 9), the 'deepening of the euro crisis has led to new treaties that do not recognise the EP as a policy making actor'. Under these conditions, the new framework for economic governance in Europe (which, to some degree, emerged from the economic developments after the crisis) in effect came about more from an intergovernmental procedure rather than from the Community Method. This supports the LI hypothesis that supranational organisations play only a limited role in European integration (Schimmelfennig 2015).

Almost all attempts at reform designed to improve and bolster the framework for economic governance, even the bailout plans for the Member States or the politics of austerity, fall within the same framework of analysis. However, we should remember that in recent decades, one important factor has changed. France and Germany are the most powerful EU Member States, but their global and peripheral economic power and influence has not remained stable and equal. Thus, France's bargaining power has been narrowed in recent decades. Consequently, French economic policy was dominated by the powerful German rationale (Clift and Ryner 2014). Moreover, in addition to being an imperfect economic and political framework, the EMU is also a zone within which major divergent interests have emerged in recent years, particularly between France and Germany (Tombazos 2011). These divergences appear to have created an utterly confrontational environment concerning EMU issues. As we explained in the previous section, initially, France and Germany interpreted the euro crisis in two completely different ways. Similarly, in the last years of the crisis, the two sides and the outcome were influenced by two contrasting economic schools, namely, Keynesianism and ordo-liberalism (Young and Semmler 2011).[24] However, it is currently unclear whether the austerity rules of ordo-liberalism can promote growth in the EU (Young and Semmler 2012).

Both France and Germany saw the crisis as an opportunity to promote changes in the economic governance of Europe based on their separate interests and preferences. However, neither France nor Germany had clear-cut plans about that transformation. The views of both countries overlapped because the Euro and the Eurozone somehow had to be rescued. However, even within Germany, as Schimmelfennig (2015, 182) states, 'the preferences of Germany, a core actor, on Grexit, a core policy question during the crisis, were not unitary, fixed or internalized but resulted from calculation of negative interdependence and risk in a situation of high uncertainty.' Moreover, there was a disagreement about how to bail out Member States and how the framework for economic governance should be transformed. Germany argued that it had to be done based on already agreed principles and rules, whereas France stressed that the process of economic integration in Europe had to be advanced to create economic governance (Jamet, Mussler, and De Corte 2011). This does not mean that both Germany and France had strict and definite policy ideas. Rather, both sides had ambiguous and flexible policy ideas and responses to the crisis (Van Esch 2014), but their intergovernmental preferences remained fixed during the last few years (Schimmelfennig 2015). However, in the last 6 years, two competing strategies emerged that, although not contradicting one another, differed in 'emphasis and sequencing' (Krampf 2014, 314).

To be more specific, it is clear that Germany has 'used the intergovernmental mode throughout the crisis negotiations' (Young and Semmler 2012, 16). Initially, the German reaction to the crisis was 'hesitant' and 'slow' because they were reluctant to take the leading role in collective actions (Schweiger 2014, 297). According to Bulmer (2014), Germany's international legitimacy and increasing domestic constraints have diminished its leadership role. The German side considered the European crisis a consequence of the fiscal condition of the Member States. At the outset, the European crisis for the Germans lacked a European dimension. Separate and unique fiscal and banking crises existed within the Member States. To address these crises, Germany suggested the same tried and tested recipe previously employed. That approach is based on three principles: (a) the independence of the ECB based on the monetarist approach, (b) the application of stricter rules in relation to SGP and the Excessive Deficit Procedure (EDP), and (c) fiscal consolidation of the Member States via harsh, oftentimes catastrophic, austerity and structural reforms. Why, however, did German Chancellor Merkel accept the French idea of creating economic governance for Europe? As Jamet (2011) argues, this move was purely tactical, i.e. to win a leadership role for her in this debate, to mark the goalposts about rule-based governance and to prompt France to suggest more specific, practical ideas about what economic governance would entail.

Because Germany has reaped the most benefits since the moment the EMU was created, even if Germany was to wait until the last moment, it would do everything necessary to stop the Eurozone collapsing, although keeping many peripheral Member States in a 'coma' due to its unwavering and intransigent policy. Germany only makes compromises when it knows that doing so will not negatively affect the interests of German businesses or if, in practical terms, disaster is only one step away. Germany stands to lose the most from a collapse of the Eurozone because its export sector would be irreparably hit. According to a Bertelsmann Stiftung (2012) report, default on Greece's part and its exit from the EMU might not have major effects on the Member States because Greece only represents a very small part of the European economy overall. However, because of the domino effect that would very likely occur, withdrawal could provoke the collapse of the money markets in Spain, Portugal and Italy and reduce the overall GDP in the world's 42 largest countries by approximately € 17.2 trillion. Conversely, to be fair, it is essential to stress that Germany has contributed the most to financing bailout packages for Greece, Ireland, Portugal, Spain and Cyprus, with its participation in the programmes and the country's simultaneous exposure to EFSF and ESM solidarity obligations of 27% (Bibow 2013) and the initial potential cost of approximately € 79.4 billion (Broyer, Petersen, and Schneider 2012).

At the same time, from the onset of the crisis, Germany has been in the most advantageous position compared with other Member States. This position not only generates immense economic benefits for Germany but also provides (as the theory of LI states) a major comparative advantage in negotiations at the European level. For example, Germany initially disagreed with the bailout plans for the peripheral states and the establishment of the EFSF or ESM because they violated the Treaty of Maastricht and were in conflict with ECB policy on the purchase of bonds on the secondary market from deeply indebted states. However, in the end, Germany made certain concessions that, in a refined manner, did not undermine German interests. Among other things, Germany did not want to pay the bill alone. Germany refused to rescue Greece for a long time, so that the issue of the Greek crisis was left hanging by a thread. As a result, Germany reduced the negotiating power of the other European players and limited the ability to present alternative forms of bailout to a minimum. Clearly, Germany appears to have adopted this strategy so that it could lay down its own terms and conditions in the new framework for economic governance and to optimally safeguard German economic interests. In fact, during that period, Angela Merkel persuaded the French President and European officials to involve the IMF further (Young and Semmler 2011). The bailout plans of indebted Member States not only became characterised as an *ultima ratio* (Young and Semmler 2011) but also resulted in the EU offering,

> the most cost-effective and politically expedient way for Berlin to ensure that German banks and bondholders get paid back for their imprudent international loans. It is no surprise then, that strong support from German business has been decisive in ensuring a multiparty majority in the Bundestag behind committing resources to defend the euro. (Moravcsik 2012, 61)

From 2010 onwards, Germany stressed the need for changes to the framework for economic governance that needed to be based on robust legal foundations. The alibi of the German Constitutional Court was always very credible. For example, during the Euro Summit of 9–10 May 2010, Germany reacted to a much more ambitious attempt at bailout suggested by the European Commission and, in particular, to its proposal to establish a Bailout Fund to purchase the bonds of indebted Member States (Gocaj and Meunier 2013). Germany refused the creation of the Eurobonds or the possibility of debt mutualisation (Schimmelfennig 2015). The German delegation argued that if such a proposal were to be adopted, there would be problems with the Constitutional Court (Barber 2010). According to the German Chancellor, the main changes should be made in three areas: (a) better fiscal discipline via the SGP, (b) improved coordination of economic policy and (c) the establishment of a crisis management mechanism. For the German authorities, '(a)' was based on very clear-cut views, whereas the framework for changes in the other two areas was not quite so clear-cut. When it came to setting up a framework to encourage competitiveness and growth, Germany stressed that any changes should be made so as not to affect the German export sector. Moreover, the German government did everything it could to avoid setting up a 'European transfer union' along the lines proposed in the French approach. In September 2010, a German non-paper stated the need to accelerate fiscal consolidation procedures by putting in place automatic sanctions on states that violated the SGP. Thus, the German approach stressed the need to set up a much more de-politicised fiscal sanctions procedure. Any sanctions ought not to be a matter of the

European Council's discretion but ought to be imposed automatically. In effect, all these developments brought the Franco-German dispute about rule compliance and governance policy to the fore (Mussler 2011). In fact, Germany wanted not only to make the sanctions under the SGP automatic and thus depoliticise the EDP but also to make European fiscal supervision more compact via the European Semester (Schild 2013). At the same time, it introduced multilateral supervision based on specific metrics and sanctions on non-compliant states via the new Excessive Imbalance Procedure. In addition, Gocaj and Meunier (2013) argue that how the EFSF operated reflects the German attempt to control the new institution and to segregate it from the European technocratic management approach because EFSF is a company based in Luxembourg and does not belong to either the Commission or the Council. The same argument can be made for the creation of ESM. In addition, the creation of the EFSF and the agreement for the creation of the permanent ESM identified with the promotion of the German stability culture in Europe (Howarth and Rommerskirchen 2013). In that sense, German political leaders legitimised their choices in the European level domestically and tried to heal the vulnerabilities of economic governance in Europe by imposing the stability culture in the EMU. It is thus clear that, even with the establishment and running of the EFSF and the ESM, there were political moves in play that affected the outcome. Germany also appears to have supported the French proposal concerning the Euro Plus Pact because it was effectively based on the intergovernmental process and not on the Community Method. In fact, most European Councils from 2010 to 2012 entailed an asymmetric bargaining game between Germany and the other Member States. None of the measures suggested appears to have negatively affected German economic interests despite being condemned numerous times by various interest groups within Germany. It is also clear that, as Young and Semmler (2011, 20) argued, 'in the competitive struggle of globalization, however, the country has turned increasingly inward and pursues self-interested policies'. As a result, in the last five years, Germany was the only country that possessed the power to influence and change economic integration in the EU.

Did France react at all to this? Back when the EMU was being designed and planned, France supported the idea of creating a so-called '*gouvernement economique*', albeit one based on an intergovernmental mode. The idea of economic governance had been raised by Mitterrand during the negotiations for the Treaty of Maastricht. Moreover, France supported the idea of creating the ECB and the SGP primarily to prevent French governments from recklessly increasing public debt and public deficit. However, it refused to accept the blind nature of the economic governance rules that Germany imposed because it also wanted to ensure that it was possible for French governments to intervene in times of crisis (Howarth 2007). From the French perspective, the establishment of a framework for economic governance in Europe should be based on four principles: (a) suitable coordination of EU economic policy and the development of a suitable economic policy mix by the ECB, (b) a more active role of the EU in stimulating economic growth and job creation, (c) more reliability and legitimation for the EMU and (d) a challenge to the objectives and independence of the ECB (Howarth 2007). Of course, this did not mean that the French had taken a clear-cut, firm line about how the new framework for economic governance should look. The French had for a long time been stuck on the questions of whether and to what extent aspects of national sovereignty should be surrendered (Arnaud 2000; Drake 2001). As Howarth (2007, 1075) stresses, 'the most common feature of French communicative discourse on economic governance has been the absence of any concrete proposal of transferring real economic policy competences from the national to the European level.' That is perhaps why, even today, France has not fully clarified what the concept of economic governance in Europe means.

In recent years, France's approach to the creation of economic governance in Europe has not radically changed because it always appears to be closer to an intergovernmental rather than a supranational approach (Jamet 2011). Although the current French approach to addressing the debt crisis initially differed considerably from the German approach because of the fear that France would remain unprotected on the global markets, France came to accept Germany's stance on implementing a restrictive economic policy (Fabbrini 2013). Of course, that does not mean that the French authorities stopped attaching importance to issues of economic growth, of fiscal stimulus and wider coordination and of a degree of latitude concerning fiscal and monetary policy (Pisani-Ferry, Sapir, and Von Weizsacker 2008). It is clear that France currently prefers a 'weaker' euro to bolster the competitiveness of French businesses, whereas Germany wants a 'stronger' euro so it does not acquire European competitors in the global economy. For this reason, the French focused their attention on macroeconomic imbalances and the problems of competitiveness faced by the Member States.

In particular, in contrast to the German insistence on stability, France took the view that the focus should be on growth. The proposals to bolster European economic policy, to revitalise the European single market and to develop a single European investment strategy are all focused in this direction. France proposed that a Eurobond be created—a proposal Germany rejected based on moral hazard. France also supported the plans of the Commission's president for joint European borrowing to finance investment plans. In relation to the financial framework, France stressed the need to increase financial supervision and promoted the creation of the European Systemic Risk Boards and three other European authorities (Jamet 2011).

On the issue of setting up a crisis mechanism, France initially agreed with Germany on the establishment of a permanent crisis resolution mechanism. However, it did not suggest detailed proposals about how such a mechanism would operate. In March 2010, Germany proposed that a European Monetary Fund be established to provide direct cash injections to Member States and to eliminate the risk of default. However, France blocked such a development. There were two main reasons for this. First, France did not want the European Monetary Fund to be considered a regional competitor of the IMF in the context of the presidency of the G-20. Second, given a potential default, the markets would look for higher returns on sovereign bonds, and European banks would weaken (Jamet 2011). That is why France turned its attentions towards supporting the creation of the ESM, which was promoted by Germany. It should be stressed that the French President Sarkozy also proposed that the EFSF should have unlimited access to ECB funds and that the ECB should intervene (as it did) by buying up the bonds of deeply indebted Member States from the secondary markets. This provoked major reactions from German officials at the ECB. On the issue of the Greek bailout package, France initially favoured providing direct assistance to Greece and rejected any IMF involvement. In contrast, Germany examined the prospects of a 'Grexit', refused any bailout plan, and stressed that any bailout of Greece must be decided on with the active involvement of the IMF. The results are now known.

Concerning the fiscal supervision framework, in October 2010, France reached agreement (after expressing considerable opposition) with Germany on the reinforcement of fiscal rules and on the imposition of potentially strict sanctions on any Member States that violated the SGP. These penalties are rigged with qualifications that the French imposed. They even went so far as to agree to ban Member States that violated the fiscal framework from taking part in votes at European Councils, but this proposal was not ultimately accepted. France also promoted the strengthening of multilateral fiscal supervision via the adoption of the Euro Plus Pact on 25 March 2011. It added the idea of taking coordinated action against countries with excessive surpluses to a debate in order to support the effective demand of national economies. However, as one might have expected, that proposal was rejected by Germany, which stressed the need for structural reforms.

All the aforementioned argumentation indicates the limits of the potential change of economic governance in the EU. Under these conditions, it will be very difficult to take the next necessary steps towards a political union in the EU. It seems that the Community Method has reached its limits, as long as the interests of Europe's powerful states do not allow it to advance (Kundnani 2013). Although, significant new elements of the new EU architecture of economic governance (such as the European Semester, the Six-Pack and the Two-Pack) were partly the result of the Community Method, the last developments in the economic and monetary dimensions of the EMU fostered the role of the European Commission and bolstered the supranational aspect of the EMU (Craig 2015). According to Schweiger (2014, 293), even the Fiscal Compact highlights the collapse of the Community Method and the rise of a 'more differentiated form of intergovernmental policy coordination between groups of member states'. At the very least, most of the measures that were realised through the Community Method were initially promoted by intergovernmental institutions, notably the European Council and its President (Puetter 2013). In other words, 'the major crisis management and reform deals' such as, for example, the bailout packages, the EFSF and the ESM and the Fiscal Compact, 'have been reached in intergovernmental negotiations' (Schimmelfennig 2015, 187).

5. Conclusion

The EMU is a 'major political issue' that touches upon the very 'heart of the issue of national sovereignty' (Τσούκαλης 1998). The economic crisis showed that important issues in economic policy concerning the change in economic governance and the role of the nation-state, which were 'swept under the carpet' in recent decades, must be resolved to make the European venture viable.

Since 2010, immense changes have occurred in relation to the economic and monetary aspects of the EMU, creating a new, complex system of economic governance. At the same time, the euro crisis brought up old questions about European integration concerning the centrality of the state and transnational interactions. As this paper has argued, the new framework for economic governance in Europe is largely the result of an intergovernmental approach. This shift towards the intergovernmental method undoubtedly shows not only that the process of economic unification in Europe is advancing one step at a time but also that it can be affected by the interests of the Member States. In fact, as the process of integration proceeds, issues of 'low politics' are substituted by the significant issues of 'high politics'. However, this process is how the possibility of the transformation of economic governance in Europe becomes weaker. As the process of integration advances, the margins for transferring national sovereignty to supranational institutions narrow, and the importance of the intergovernmentalist stance is highlighted. For this reason, many important issues concerning the transformation of economic governance in the EU were debated for a long time but were not solved (Mourlon-Druol 2014). Of course, Europe currently appears to have the will to overcome barriers and to surpass itself; however, the outcome of this process is not predictable.

As this paper has suggested, from an institutional point of view, the crisis is the result of the structural choices made at Maastricht as a corollary of the convergence of the interests and preferences of the powerful Member States. Even today, the creation of a new framework for economic governance appears to continue to be a bargaining game. Although supranational actors have played or continue to play an important role in developments concerning changes in the framework for economic governance in Europe, particularly in relation to the economic dimension of the EMU, the intergovernmental approach has remained prominent. Sovereignty and the centrality of nation-states appear to be unchallenged, although in some cases, they could be contested. Under these circumstances, any future changes in the framework for economic governance are not expected to significantly affect the centrality and importance of the nation-state to such a degree that one could talk about the importance of intergovernmentalism diminishing. Therefore, the process of European unification and of transforming the new framework for economic governance can only advance to the extent that the interests of the strong Member States permit it.

Without any doubt, the international and European bargaining game over economic relations is currently much more complex than it was in the past (Eichengreen 2012). However, the key factor affecting both bargaining and the outcome of negotiations on the new framework for economic governance is the interests of the Member States. Both Germany and France turned to the intergovernmentalist approach to find solutions to the crisis. The basis of that approach is the sovereignty of the nation-state over supranational players, that is, the intergovernmental method over the Community Method. Therefore, the changes and necessary adjustments required at the EMU level, such as changes in the labour market, the establishment of fiscal transfer mechanisms, the introduction of Eurobonds or the promotion of banking unions, will not be the result of some automatic or depoliticised process. Critical changes are not suggested unless there is convergence between the economic interests of the strongest Member States, namely France and Germany. This conclusion is consistent with the core of the theory of LI. However, in a globalised world, 'state interests' are no longer only determined by the domestic context. One could argue that the Member States place their interests on a scale, as the theory of instrumental rationality argues that humans do. From there, the Member States try to satisfy as many interests as they can, starting from what they consider to be their most important interests. However, this argument connects European integration with rational choice and international interdependence as the theory of LI assumes (Schimmelfennig 2015). In this regard, LI provides a reasonable exegesis of state preferences, and the Eurozone's countries are 'in favour of deepening economic integration to manage the high actual and potential negative interdependence created by the debt crisis' (Schimmelfennig 2015, 183). Therefore, even within such a diverse union, integration can be promoted because all Member States recognise that in any event, it is not in their interests to be isolated and to face the globalised environment on their own. However, that would not appear to change our basic conclusion, which is that as long as restrictions relating to interests and sovereignty are included in the context of transforming economic governance, the limits on the transformation and on the general process of economic integration will become clearer, and the EMU will, it seems, remain imbalanced for a long time to come. In this regard, it is highly doubtful whether the Member States may use the crisis as an opportunity; thus, it appears that the EMU will remain in a prolonged state of imbalance.

Disclosure statement

No potential conflict of interest was reported by the authors.

Notes

[1] Email: pantelis@uop.gr

[2] For other excellent contributions, see Fabbrini (2013), Chang (2013), Bickerton, Hodson, and Puetter (2015), Clift and Ryner (2014), Crespy and Schmidt (2014), Schimmelfennig (2014) and Schimmelfennig (2015).

[3] 'Economists' believed that before the creation of the EMU, the economic and financial conditions for its long-run viability should already exist. Thus, economic convergence is a precondition for monetary integration. This view was adopted by Germany and the Netherlands. 'Monetarists' believed that the process of monetary integration could create the necessary economic conditions for the EMU's long-run viability. This view was largely adopted by France, Belgium and Luxembourg. See Tsoukalis (1977) and Kruse (1980). Those who designed the EMU were not clear about which approach to follow in establishing it. See Verdun (2007b). In other words, the key players were not in agreement about whether and to what extent the convergence of economies ought to come before the transfer of sovereignty over monetary policy to a supranational level. See Verdun (2007a).

[4] Germany's negotiating position in the discussions about the Treaty of Maastricht was influenced by the economic philosophy of *ordo-liberalism*—see Dyson and Featherstone (1999)—which is tied into a political approach based on the rules of *Ordnungspolitik* in which the state only lays down the legal framework within which private players can act as freely as possible. See Mussler (2011). For a general overview of the main reasons for conflict between France and Germany up to the signing of the Treaty of Maastricht, see Maes (2004).

[5] For excellent contributions on the German model of economic growth during the Eurozone crisis, see Bonatti and Fracasso (2013) and Jessop (2014).

[6] For alternative views see Kotios and Roukanas (2013), and Sklias and Maris (2013).

[7] See Olli Rehn Speech in European Policy Centre Brussels, 15 April 2010, 3.

[8] See Statement of the Heads of State or Government of the Euro Area, 7 May 2010, 2.

[9] Decided on 9 May 2010 at the Extraordinary Council Meeting.

[10] Adopted at the European Council, 7 September 2010.

[11] The proposals for the Six-Pack were presented by the European Commission in September 2010. The Six-Pack was adopted by the European Parliament on 28 September 2011.

[12] Adopted by the European Council on 24/25 March 2011.

[13] Decided on 28 November 2010.

[14] The two regulations were adopted at the European Council on 21 February 2012.

[15] For the ECB's early response to the crisis, see Trichet (2010).

[16] See the ECB's press release on 10 May 2010.

[17] See Mario Draghi's speech at the Global Investment Conference in London, 26 July 2012.

[18] See Mario Draghi's introductory statement to a press conference, 2 August 2012.

[19] See the ECB's press release at Technical Features of Outright Monetary Transactions, 6 September 2012.

[20] See the European Commission proposal for the new ECB powers for banking supervision as part of a banking union IP/12/953, 12 September 2012.

[21] For the ECB's role as a Lender of Last Resort, see Buiter and Rahbari (2012).

[22] See Jens Weidmann's speech at the Association of Family Enterprises in Cologne on 13 September 2011.

[23] In contrast, scholars have argued that 'the Commission's importance in the European Economic integration process has not diminished, but its role has shifted' (Bauer and Becker 2014, 227). For Bauer and Becker (2014), it is very difficult to distinguish the intergovernmental and supranational models of economic governance in Europe because the EU is characterised by different modes of governance in all relevant policy areas. For Andrews (2013), the Commission's commitment in relation to the nature and direction of European integrations has remained constant.

[24] For excellent contributions, see Young and Semmler (2012), Bulmer (2014), Siems and Schnyder (2014), Van Esch (2014) and Young (2014).

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