



HOUSE OF LORDS

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Financial Affairs Sub-Committee

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COMPLETING EUROPE'S ECONOMIC AND MONETARY UNION

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Witnesses: Professor Paul De Grauwe and Alex White

Members present

Baroness Falkner of Margravine (Chairman)
 Lord Butler of Brockwell
 Lord Davies of Stamford
 Lord Haskins
 Earl of Lindsay
 Lord McFall of Alcluith
 Lord Shutt of Greetland
 Lord Skidelsky

Examination of Witnesses

Professor Paul De Grauwe, John Paulson Chair in European Political Economy, LSE, and
Alex White, Director, Country Analysis, The Economist Intelligence Unit

Q179 The Chairman: Good morning, Professor Paul De Grauwe and Alex White. Thank you for agreeing to give evidence to this European Union sub-committee's inquiry into Europe's economic and monetary union. You have a list of the interests which have been declared by Members of the Committee. This is a formal evidence session and a full transcript will be put on the public record in printed form and on the parliamentary website. You will be sent a copy of the transcript so that you can revise any minor errors. This session is also being webcast live and will subsequently be accessible via the website. With your permission, I suggest that we do not go into introductory remarks but move straight on to the session. Could both of you give an assessment of the Five Presidents' Report and the short-term actions it proposes, as well as longer-term sustainability?

Professor Paul De Grauwe: Thank you very much. First I want to say how pleased and honoured I am to be here. I appreciate that the Five Presidents' Report is certainly a move forward, but only a small one. It is a tiny step which indicates the direction in which the eurozone will have to go, which ultimately in my view has to be towards some kind of political union. Some indication is given in the report about how to do that, but it falls far short of what is necessary. There are a couple of interesting ideas in it, in particular the proposal from the European Commission for competitiveness boards, which some member states already have. It is a good idea but there is also a potential drawback. By focusing too much on competitiveness in its narrow sense, such as the development of wages, one can easily become trapped in a deflationary spiral where everyone watches national wage developments and then tries to reduce them relative to their neighbour. In no time you are in a deflationary spiral that prevents countries' economies growing. We have already seen some of

that. So while I think that there are positive elements in the proposal, there are also dangers. What is lacking in the Five Presidents' Report is some form of institution that can take a bird's-eye view and function as a stabiliser at the level of the eurozone. If something like that is not in place, the net effect of these competitiveness boards might well be further low growth and stagnation in the eurozone. That is why I have a guarded view about it. The proposal for a banking guarantee in the form of a bank deposit insurance mechanism for deposits is a good idea, but it will be very difficult to implement.

The Chairman: We will come on to that shortly.

Alex White: Thank you very much for the invitation to appear before the Committee. I agree with much that Professor De Grauwe has said, but we have a slightly different nuance of view about the overall direction that the Union is attempting to take here. In essence, Professor De Grauwe is correct to say that this is not a solution. This does not take us to an end point that looks sustainable and fit for purpose over the very long term. At the same time, however, it is our view that this is pushing too far in terms of the political capacity of the Union and its member states as regards the delivery perspective over the short to medium term. More broadly, if we look back at the journey that the Union has taken since the introduction of EMU, we can see from the vantage point of today that its introduction at the time that it took place and in the manner that it was done, and with the institutions that were in place at the time, was an error. It was an error in terms of the economics, and that error has been much discussed. It was also an error in terms of the politics for two reasons. It created a set of expectations and institutions that were without clear leadership, which goes to Professor De Grauwe's point about a lack of leadership at the European level. It also moved too quickly before there was a European demos to support a lot of the initiatives that lay behind what was imposed in 1999 and 2000. When we look at the Five Presidents' Report and at some of the initiatives which preceded it, they appear to us to be an attempt to correct the first error, which was the economic error of the timing and the institutions involved in the creation of EMU, and they do so at the risk of conflating and worsening the political error: moving too fast and going beyond what the European politics and voters are prepared to accept and implement.

The Chairman: Professor De Grauwe, perhaps I may come back to you briefly in terms of European leadership. What do you envisage?

Professor Paul De Grauwe: Leadership here, in my view, means more than having a strong president or strong people in place.

The Chairman: Institutionally?

Professor Paul De Grauwe: It means something institutional.

The Chairman: Something like a eurozone Treasury?

Professor Paul De Grauwe: Yes, in the true sense of a Treasury, which is an institution that has the power to tax and to spend and is embedded within a democratic decision-making process. That is what a true Treasury is, not some kind of institution where Ministers of Finance come together and talk to each other. That is not what we need. We have enough institutional features to make all this possible, so it really should be about some form of transfer of sovereignty. I am aware, of course, of what Mr White is saying, which is that the political background to this is not in place to make it possible, but as an academician I would say that these are the necessary conditions to make it sustainable in the long term. There is today an illusion in Brussels that we have now achieved or we are close to achieving the institutional framework that would allow us to have a sustainable eurozone. That is a big mistake. We do not have it. We have to move forwards much more radically, and that is precisely the problem because no one wants to do it.

The Chairman: Because of treaty change.

Professor Paul De Grauwe: No. I agree that it requires treaty change, but the political will in all of these countries is just not there to make that move. In the previous discussions about Eurobonds or even the deposit insurance mechanism, there is no willingness to move in that direction, let alone towards a true Treasury.

The Chairman: That brings me neatly to Lord Butler's area.

Q180 Lord Butler of Brockwell: Professor De Grauwe, you said at the outset that you think that banking union is a good idea, but that you are sceptical about whether it can be delivered. I do not want to put words into Mr White's mouth, but I think that you are also sceptical about whether some of the developments in the Five Presidents' Report can be delivered, probably including this one. If it cannot be delivered, is there some alternative form of insurance or support that could take its place in the short term?

Professor Paul De Grauwe: Of course there are many different insurance schemes, but the banking union is key to maintaining stability in the eurozone. We have some elements of a banking union today, as you know, but parts of it are not yet workable. In particular, as we mentioned earlier, the common deposit insurance mechanism has gone nowhere, while the resolution mechanism lacks credibility. I would like to stress another element about the banking union. A real banking union presupposes some kind of fiscal union. At some point, you need an institution with deep pockets that in a time of crisis is capable of resolving it. If you do not have that, a banking union has no credibility. Some people say, "Okay, let's have a banking union so that we don't need a fiscal union". I say no to that. A banking union can

function only if it is embedded in or part of a fiscal union. That is what you need in a time of crisis: someone who has the capacity to raise taxes and fund rescue operations. We now have the resolution fund, but it lacks credibility because its capacity to act in times of crisis will be limited.

Lord Davies of Stamford: But surely the European Central Bank can provide protection for the banking system.

Professor Paul De Grauwe: The ECB can certainly do that, but of course here one likes to make a distinction between liquidity problems and solvency problems. The ECB is the right institution to step in at times of crisis in order to take care of liquidity problems, not solvency problems, at least in theory. I know that it is difficult to make that distinction in practice, but we should not overload the ECB and make it responsible for dealing with banking crises, including saving banks by recapitalising them. That does not seem to me to be the role of a central bank. A central bank is there just to make sure that when solvent banks are hit by illiquidity they receive the right liquidity. Again, we need a Treasury that is capable of doing all the other things.

Lord Butler of Brockwell: Before bringing in Mr White, you said that you cannot have a banking union without a fiscal mechanism. Can I put the question the other way around? Would a stability mechanism be sufficient and make a banking union unnecessary?

Professor Paul De Grauwe: Do you mean the existing ESM?

Lord Butler of Brockwell: Yes, I am developing the point here.

Professor Paul De Grauwe: I do not think so, because again when you face a banking crisis of the kind that we experienced, especially in 2008, the ESM is not sufficient. It is too limited and will not be able to deal with a crisis. As a result, if it were to happen again, we would face the need for another back-stop. A back-stop for the ESM would be necessary because on its own it would not be sufficient.

Lord Butler of Brockwell: Thank you. Mr White.

Alex White: I agree with much of what has been said, but I think we need to avoid taking a binary view on policy developments at the European level. It is simply not the case that we either have a fully functioning banking union with all the bells and whistles one could imagine attached to a fiscal union or we have nothing. If we look at what the Union has delivered over the past four years, since the high point of the crisis in 2012, we have the ESM and all the mechanisms around that; we have the reinterpretation or the restatement of the ECB's mandate with OMT. On the banking union side, we have the implementation of the SRM and the SSM. That is not a perfect system, and Professor De Grauwe is right to say that

a lot more needs to be done, but part of the danger of the approach that has been set out in the Five Presidents' Report is that it distracts a little from what the Union has already achieved. If we compare the progress on banking union which has been developed over the past three and a half years with the length of time it took to build the European Coal and Steel Community, the Common Market and the other major European institutions, actually the Union is doing pretty well in delivering. While accepting many of the points that Professor De Grauwe has made, we need to keep that in mind. There is reason to believe that the Union is better equipped to deal with a situation with similar issues to, while not being a repeat of, 2008 to 2010.

Q181 Lord Skidelsky: As a follow-on to the banking union question, which involves considering the role of the ECB, I want to ask Professor De Grauwe another question. Ever since Bagehot, it has been understood that a central bank should be the lender of last resort; that is, it should be prepared to lend to solvent banks at a punitively high rate of interest. The ECB is not a lender of last resort in that sense. Therefore, should it be? In order to play that role, should it also have a fiscal back-stop? That is the implication of what Professor De Grauwe is saying. Is the obstacle to developing the ECB as a lender of last resort the lack of a Treasury or are there other obstacles? How would you progress from there because there is an implication in some of what Professor De Grauwe has said that there are certain necessary conditions for making the eurozone work, but those conditions are not in place? The political will to put them in place is lacking and therefore logically the eurozone cannot survive.

Professor Paul De Grauwe: That is a very deep question which I have also been struggling with. Recently I read Ben Bernanke's book which goes into great detail about what was done in the US.

The Chairman: Is that the one about the Great Depression?

Professor Paul De Grauwe: No. This is his more recent book, but I have forgotten the title. What struck me was the degree of co-operation between the Federal Reserve and the Treasury.

Lord Skidelsky: And in the UK as well.

Professor Paul De Grauwe: That is right. Of course in theory it is easy. I mentioned the central bank taking care of the liquidity problems and the Treasury taking care of the solvency problems, but in practice when you look at this you just do not know; you guess—this bank may be solvent and liquid, but it could also be insolvent. Therefore, since you have this uncertainty, the central bank and the Treasury must work together because each time one does something it has implications for the other. As you mentioned, Lord Skidelsky, that is lacking

in the eurozone. We have a central bank, which I would argue is quite powerful, but there is no comparable Treasury with which you can decide in a crisis what to do with a particular bank and who will do what to handle the uncertainty about liquidity versus solvency. That is one of the weaknesses of the eurozone: the absence of a common Treasury that has the capacity to deal with solvency issues, and we will continue to struggle with that problem. It also leads to a situation where the actions of the central bank lack credibility because we are never sure whether it will be able to act. Take the OMT programme, which was a great thing in 2012 when Draghi came out with his promise to act in times of crisis in relation to government bond markets. Then last year came the Greek crisis. The ECB said, “We don’t want to use OMT”, and we had a new crisis. Here we have something and we are not really sure whether the central bank will be willing and able to act in times of crisis.

Alex White: My interpretation of the OMT and President Draghi’s statement at the time was that it was a commitment to defend the euro. It was not necessarily a commitment to defend the existing composition and membership of the euro area. That is an important difference and something which came out in the Greek crisis last year.

Lord Davies of Stamford: It was based on sustainable and realistic policies being adopted by the member states, when Greece was adopting irresponsible policies or rejecting the restructuring. It was not sensible for the ECB to buy its bonds.

Professor Paul De Grauwe: Somebody must judge whether it is responsible or not. You might say that it was not an existential problem, but if some countries exit it then becomes an existential problem.

The Chairman: Mr White, you were interrupted.

Alex White: There is certainly a very interesting debate to be had about whether the exit of an individual member leads to a broader collapse of the Union. It is not our view that it does; it is our view that it creates a severe challenge but it does not lead to the end of the Union.

More broadly, with respect to Lord Skidelsky’s question on the ECB and the lack of a common Treasury, we like to ground our analysis in reality, and the reality of the situation is that the prospects for a eurozone Treasury appearing in anything like the foreseeable future are effectively de minimis. We need to start from that point and from the acceptance of that political reality. Obviously that puts the ECB in an invidious position, which we have seen throughout the crisis. There is no obvious solution to that. We exist in a world where the ECB backstop through the OMT is there on the table, but the conditionalities around it, its usage and its terms are ill defined. We have the steps that we have spoken about with respect to banking union. This helps, but obviously it is not a full solution.

Lord Skidelsky: Just one last thing. The implication of what you are saying is that there is no realistic possibility of a Treasury, but there is a realistic possibility of the eurozone shedding members.

Alex White: There is no realistic probability of a Treasury in the near term absent a further systemic shock, which potentially might be delivered by the exit of one or more members. That could in theory generate the political capital necessary to take further steps towards more substantive integration.

Lord Skidelsky: There are lots of ifs there.

Alex White: Yes, lots of ifs.

The Chairman: Professor De Grauwe, the miracle of Professor Begg and the internet combined tell me that the Bernanke book is called *The Courage to Act: A Memoir of a Crisis and its Aftermath*.

Q182 Lord Davies of Stamford: Professor De Grauwe, you are saying now that the euro really is not viable without a common Treasury, as you put it, as part of the fiscal policy. That has not always been your view, has it? At the time of Maastricht treaty you wrote a good and influential book that I read and enjoyed which said that the project was perfectly viable without it.

Professor Paul De Grauwe: Did you read my book?

Lord Davies of Stamford: Yes. You said in it that the project could go ahead without the necessity for fiscal union.

Professor Paul De Grauwe: I think I said in my book that without a political union, it was a high-risk project. Are you referring to my textbook on the economics of monetary union?

Lord Davies of Stamford: I think so, yes. It was the one you produced at the time of the Maastricht treaty.

Professor Paul De Grauwe: The first one was published in 1992 and the conclusion in that book was that we are taking a big risk in doing this because it is unfinished business, in particular if political union is not part of it. That was my analysis at the time and I do not think that I have changed it that much, although of course the detail has evolved.

Lord Davies of Stamford: My memory is that you thought it was perfectly responsible to go ahead with the project without fiscal union, knowing that it was a desirable thing that might come later, but that it was not necessary as a prerequisite for a successful monetary union.

The Chairman: Perhaps you could direct us by saying what you think about it now.

Lord Davies of Stamford: Yes, let us talk about what you think now. Do you think that the reason for having this common Treasury, or fiscal union as you have just described it, is in

order to have a mechanism for dealing with asymmetric shocks, or is there a need for permanent structural transfers within the Union greater than we now have through the structure funds and comparable with those that exist within individual member states?

Professor Paul De Grauwe: The traditional view has been that a common budget functions as an insurance mechanism. You centralise the budget and as a result, when there are asymmetric shocks, you have automatic transfers from countries or regions that are experiencing good times to those experiencing bad times. That is one part of it, but for me it is not the most important one. The more important part is that we need a budgetary union so as to be able to consolidate at least a significant part of national debt into common debt. What we have seen with the crisis is that when we move into a recession, financial markets typically get nervous about some of the member countries. A recession hits different countries in different ways. Some will be hit very badly with increasing budget deficits and accumulated debt while for others that is less so. That was the pattern we saw in the sovereign debt crisis. In those conditions the markets become very destabilising. They dump the bonds of those countries they are suspicious about and they move on to countries which they consider to be safe havens. As a result, instead of markets stabilising during a recession, they typically will be destabilising the system, forcing some countries into excessive austerity precisely at the moment that you do not want that and moving other countries into good times, thus intensifying conflicts within the Union. That is the more fundamental reason why we need a fiscal union. We have to consolidate national debts so that these destabilising capital flows within the Union are eliminated. That, in my view, is the more fundamental reason why we need it. The financial markets cannot be trusted to stabilise a system like the eurozone during recessions when everyone is nervous. In the boom times, everything is fine, but markets become fearful and panicky in recessions, which destabilises the system.

Lord Davies of Stamford: I think we all understand that argument. How do you deal with the moral hazard aspect of that?

Professor Paul De Grauwe: Moral hazard can be dealt with only if you have a system of controls, which means another step towards political union. You cannot do it if you maintain full sovereignty at the level of the member states; then you cannot solve the moral hazard problem. It makes no sense to consolidate debt and keep national sovereignty because then you maximise the problem of moral hazard. In order to solve that problem, you have to move towards political union.

Lord Davies of Stamford: Since that is unlikely to happen, the eurozone faces the inevitability of a fatal existential crisis. Is that your view?

Professor Paul De Grauwe: I do not want to be a doomsday thinker, but that is indeed a conclusion that one may draw.

Lord Davies of Stamford: I am going to look at your book again because I do not remember getting that impression when I read it some 20 years ago.

The Chairman: We need to move on.

Professor Paul De Grauwe: I too will re-read my own textbook.

Alex White: I was just going to say for the record that that is not our view. While the Committee may not like this, our view is: continue to muddle through for as far as the eye can see. Those who are saying that the eurozone will inevitably collapse need to make a case for the context in which that collapse will happen and the context in which more muddle-through will not be available to policymakers. It is very hard to think of the policymaker who is going to take the decision to unwind the Union or to take an irrevocable step that has the effect of unwinding the Union. Our perspective is “more muddle-through” with some of what is discussed in the Five Presidents’ Report happening over time, but measured in periods of decades.

The Chairman: Can I ask for clarification that, when you refer to “our view”, you are talking about the Economist Intelligence Unit?

Alex White: Yes, that is correct.

Lord Butler of Brockwell: Could the collapse happen through a political route because parties get into government for whom the Union and the results for unemployment are not acceptable?

Alex White: Yes, that is certainly a risk. Obviously the political experience in Greece has been a salutary lesson, but even in Greece we have seen a Government that presented themselves as radical while in opposition and being prepared to consider the possibility of exit in extremis, but ultimately they buckled under pressure from the rest of the Union. It is worth bearing in mind that even in the countries worst affected by the crisis, like Greece, support for membership of the euro area is still above 70%. In the medium term the country we have the greatest degree of concern about is Italy. Italy is the country where dissatisfaction with euro membership is the highest. It is an advanced and complex economy that would have choices outside the eurozone and it has a political system that is fragile, to say the least. That is a core area of our concern, and absolutely it is a risk.

Q183 Lord McFall of Alcluith: Adair Turner has been talking today about a possible Brexit. He said that it would cause major destabilisation at the global level and would have implications for Europe. What is your view?

Alex White: On the implications of Brexit, our view for the record is that it will not happen, although we think it might be narrow.

Professor Paul De Grauwe: You are an optimist.

Alex White: An irrevocable optimist, yes. We think that the consequences would be serious for the UK and very serious for the rest of Europe. The implications for Europe are effectively that the spell would be broken, as it were. The idea that a member can exit is similar to the logic around exit from EMU. It creates that possibility in the minds of policymakers elsewhere in the region. Obviously the UK is an important contributor to the European project, to the single market, and to everything that goes with that. An exit of the UK would provoke some very large existential questions for the EU. I do not think that within that we believe that EMU and the issues we are talking about now would be particularly affected; it is the EU itself that is more under threat from a British exit.

Professor Paul De Grauwe: I agree with most of what Mr White has said. I certainly would not make a forecast about whether Brexit will happen because it is too difficult. My view on the political and economic implications is as follows. The economic implications of a Brexit will be limited. As soon as a decision is made to leave the European Union, the UK Government will have to start negotiations with the EU to come to an agreement on trade relations which would not be that different from what exists today. In that sense, economically it might not make much difference. Politically, of course—the point that you made—it makes a lot of difference because it would be the first time that someone has pulled out of the European Union, and that of course has huge political implications which may destabilise the Union. In that sense it is more of a political problem than an economic one.

Alex White: Perhaps I may come back very briefly on the economics. The distinction we like to make is between transition costs and steady-state costs. An exit from the Union will impose significant transition costs because of the uncertainty around what the trading relationship would look like. Those transition costs will be imposed over a number of years and they will be meaningful. But they are separate from steady-state costs. If we were to take a UK that was outside the EU in 20 years' time, there is no reason to suspect, given proper market access, that it would be economically in a worse position than a UK that was in the EU. It is the transition process that is problematic.

Lord Davies of Stamford: Two other factors might be mapped out. One is that by being members of the EU we have access to around 45 other trade agreements with countries and groups of countries around the world. We would lose those, so there would be a trading gap. Secondly, investors, both British and foreign investors here—American and Japanese—have

made it clear that they do not like investing in a capacity directed at the single market except in a country that is a full member of the Union and therefore has an influence over ongoing legislation and can take part in changes in regulation and so on. Otherwise they have no influence over the process of legislation and regulation that affects their businesses.

Alex White: Those are both good points.

The Chairman: Before we go any further, this is not particularly pertinent to our inquiry. I am conscious that you will both have to leave shortly and it is also highly political. So unless you have very brief and cogent answers relating to the Five Presidents' Report, let us move on.

Lord Skidelsky: Have we reached question 5?

The Chairman: I want to get to it, so I suggest that we move on.

Q184 Lord Haskins: The question is whether the European Semester procedure has done any good. We have heard different views about it. Some people are rather disappointed in it because it is a process in which countries arrive at a meeting, speak warmly to each other, and then go away and forget about it when they get home. In other words, it has not achieved the co-ordination of fiscal policies that it was meant to achieve. Is that fair or unfair?

The Chairman: Professor De Grauwe, why do you not start first on that one?

Professor Paul De Grauwe: Surely it has been a disappointment. Let us look at the economic performance first. Members of the eurozone have been worse off on average in terms of macroeconomic performance than the EU countries outside the eurozone. That is just something that one observes. Especially since 2008, there has essentially been stagnation in the eurozone. Real GDP in the eurozone is now, eight years later, at the same level as it was in 2008, while in the UK and the rest of the European Union we have had growth—not fantastic, but certainly a recovery—which has been totally absent in the eurozone. That is something that one should worry about. Is it something structural? Is it because of bad policies? One can also argue that it just so happens that those who were in power did the wrong things, but I believe that it has something to do with the way macroeconomic policies are set up—the fact that there is no institution which can work as a stabiliser at a level of the eurozone and everybody is doing their own thing. As a result, we have not seen any recovery. That is the problem. If we do not get away from this, in the end it will turn round public opinion. You mentioned that 70% are still in favour, but if we go on doing this, public opinion will change. When the others deliver better than we do, in the end people will say, “That is not what we were told would happen”.

Alex White: I agree with all of that. On the specifics of the European Semester, let us put this in the context of what the Union has been doing more broadly. We have had a range of initiatives—the European Semester, the two pack and the six pack—but none of these is perfect and they have not produced strong outcomes in terms of fiscal discipline, co-ordinated fiscal policies or any of the things that would address the problems that Professor De Grauwe identifies. Having said that, the discipline of having to review budgetary procedures and fiscal policy with other members is helpful. We need to get away from constantly comparing the current environment to a fully perfect Union. We are simply not in that world. Having that there is better than nothing and having a process in which countries are “named and shamed” is helpful. Some degree of co-ordination, while not as desirable from an economic perspective as full convergence, is better than none.

The Chairman: Briefly, before I come to Lord Skidelsky, do you both believe that the lack of national political buy-in is one of the hurdles?

Alex White: One of the great mistakes that has been made in response to the crisis is for national leaders not to own the European response and to put the blame on the European institutions. Certainly one could have seen from countries such as Germany and France a more active policy.

Q185 Lord Skidelsky: There is nothing in the Five Presidents’ Report about current account imbalances—there is no pressure there on the creditor countries. Just from an academic point of view, although this is also a realistic question—that seems to be the way in which these things are divided up—there is surely a case for revisiting Keynes’s proposal for an international clearing union, which was not accepted at Bretton Woods. However, it would impose on both creditors and debtors symmetrical sanctions, which would come into play more automatically beyond certain thresholds. It does not seem to be on the agenda, but it is an obvious thing to do.

Alex White: First, you are correct to say that it is not on the agenda. Secondly, there is a lot of sense in the proposal. The question at the European level is whether we involve European institutions and supranational institutions. For example, there might be a greater role for the IMF to play in Europe, but that is politically challenging. I think that it is a very creditable idea, but we are not there in terms of it being on the agenda.

Professor Paul De Grauwe: There is of course the macroeconomic imbalance procedure, which gives the European Commission the authority to put pressure on countries to change their policies. That is not fully symmetrical because, as you know, the thresholds for imbalances are asymmetric, in the sense that the threshold for the deficit countries is 4% and

for the surplus countries it is 6%, so it is not fully symmetrical. The more basic problem is again political. The European Commission has the authority to go to Germany and the Netherlands, which have very large current account surpluses, and tell them to do something about it, which must mean in this case, “Increase your spending”—otherwise one cannot reduce a surplus. But that is very difficult for the Commission to do, because in these countries having a surplus is considered to be a reflection of virtuous policies. Why should we, as Germans or Dutchmen, change our policies, because these have been virtuous? The Commission is powerless. We have the institutional infrastructure to deal with it, but politically the European Commission is paralysed. It can only go to deficit countries, to which it can say, “You have a deficit and that’s wrong”. It can blame them and say that they are wrong to have a deficit. It cannot go to Germany and say that it is wrong to have a surplus, as it would say, “What? We are right”.

Alex White: That political culture will only change over a period of decades, if it does at all.

Professor Paul De Grauwe: The solution should be a symmetrical one.

The Chairman: Professor De Grauwe, I am conscious that we are one minute over your Cinderella hour, so I think that we have to draw the meeting to an end. Professor De Grauwe from LSE and Alex White from the Economist Intelligence Unit, thank you very much for giving evidence to us today.