Greek rescue forces shift in thinking on E.U. rules

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Germany opens door to reshaping euro policy, even overhauling treaty

BY STEPHEN CASTLE

Jolted by the Greek debt crisis and alarmed at the prospect of bailing out a fellow member state, European Union leaders on Friday promised new efforts to coordinate policies to bring their divergent economies closer.

At the end of a two-day summit meeting in Brussels, Chancellor Angela Merkel of Germany made clear her determination to rewrite the E.U. economic rule book, even if that means a long and bruising battle to revise the treaty governing the bloc.

But the E.U.'s latest plans for greater economic coordination — which could have an impact on national governments' right to dictate policies on taxation and spending — will need to overcome practical obstacles and ideological differences if they are to become reality.

After weeks of division between Germany and France, the new blueprint began to emerge on Thursday when the two countries brokered a deal under which all 16 nations that use the single currency agreed to last-ditch refinancing for Greece if it is unable to raise borrowing on the financial markets.

As its price for agreeing to underwrite such a system, Germany has opened the door to moves to reshape the way the euro is managed.

Over the coming months, the E.U. will debate ways of intervening early to prevent economies from veering off course and more radical, long-term proposals that could even mean ejecting nations from the single currency.

"We have seen in dealing with deficits," Mrs. Merkel said, "that our procedures are simply not sufficient and that we have to draw lessons from that."

Although the E.U. has just completed eight acrimonious years rewriting its newest treaty, Mrs. Merkel said she thought it "will not be possible to bypass treaty change."

A declaration agreed to by the euro countries late Thursday promised to improve economic governance — or in the French version of the text "economic government" — but, in truth, there is no consensus on what this means under either formulation.

Prime Minister Nicolas Sarkozy of France had pressed hard for a meeting of euro-zone leaders to take place on Thursday, because he sees this as the vehicle of future integration.

But Mrs. Merkel said Friday that economic governance was for "the whole of

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27 states" of the union.

f there is no agreement on who ould improve the economic gov- nance of Europe, there is even less arity yet on how to do it.

The E.U. already has a strict rule ook, called the Stability and Growth act, which lays down a process to keep udget deficits within strict limits and ven penalties for nonadherence.

The difficulty is that it was France and ermany — the two countries behind the test declaration — that weakened the act when they breached the deficit limit f 3 percent of gross domestic product or the third successive year in 2003.

At the time, the pact appeared too ri- gid and seemed to be consigning Euro- pean economies to stagnation.

But, seven years later, the Greek crisis has shaken euro countries and forced them to accept that, if policies go awry in one country, its neighbors may have to pick up the tab. Significantly, all 6 nations of the single currency, includ- ng Portugal, Spain and Ireland — which themselves have deep financial problems — agreed to take part in a res- cue mechanism for Greece.

"Certainly the benign neglect that was going on before is no longer possi- ble," said Jean Pisani-Ferry, director of Bruegel, an economic research institute in Brussels. "You cannot just say there is no risk."

IMRE FOELDI/EUROPEAN PRESSPHOTO AGENCY

Chancellor Angela Merkel at the meeting in Brussels on Friday with Herman Van Rompuy, president of the European Council, center, and Pierre de Boissieu, the general secretary.

Though creating a system to curb future economic excesses in member states — particularly large ones — will not be easy, there are now several ways this closer economic coordination could take shape.

The meeting this week set up a task force to discuss longer-term proposals, including one from Germany for a European Monetary Fund.

Ideas that would clearly need a change of the governing treaty, like depriving nations in breach of the rules of their E.U. voting rights, will be examined. Another radical suggestion from Mrs. Merkel, that recalcitrant countries could be ejected or suspended from the euro zone, to allow them to devalue their currencies, is also expected to be examined.

Meanwhile, the E.U. heads of government, meeting in the European Council, are taking greater responsibility for economic policy coordination. On Friday, they discussed a strategy to create a more competitive economy by 2020.

Mr. Pisani-Ferry said it was significant that prime ministers were getting involved.

"The lesson drawn," he said, is that the regular meetings of euro-zone finance ministers is "not up to the job." "If you want a country to change course you have to speak to the prime minister, not the finance minister."

Meanwhile, Olli Rehn, European commissioner for economic and monetary affairs, will propose plans to tighten monitoring of economies in the euro zone.

Crucially, a tightening of the pact — for example, to allow the E.U. to flag looming problems in countries before they happen and to press governments to change course — could be achieved without changing the E.U. treaty, a long and cumbersome process.

Mr. Rehn has already proposed laws to give the E.U. statistical agency the power to audit national governments if — as in Greece — there are doubts about the data they submit.

Bringing together these strands to make the euro zone a more stable currency "won't be easy," Mr. Pisani-Ferry said, "but the big change is that there was a complacency around about the fact that every outcome was benign. That's gone and that's significant."