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# Reconsidering the Ethics of the Stability and Growth Pact: Key implications for European Debt Crisis

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Abstract

There is little doubt that European Economic Governance is currently facing a dual crisis of efficiency and relevance. Although this is openly conceived at the practical level of policy as demonstrated by the decisions of the Euro zone institutions, it is not conceived at the ethical level.

Responding to this challenge the paper analyses the ethical pillars of Stability and Growth Pact (SGP) focusing on two questions. Firstly, which is the role of ethics on the cognitive pillars of European Economic Governance (EEG) mechanism? Secondly, which are the main principles of an alternative EEG ethics? While acknowledging that SGP is partly a technically rule-based framework, it is argued that it is also an ethically-guided arrangement, not at all value-neutral or contextually insensitive. Further, it is suggested that due to EEG specific ethical concerns on monetary/macroeconomic issues, behavioral patterns are institutionalized and reinforced in Euro zone area, diffusing negative spillovers in European Debt management.

The main conclusion is that the mix of preventive and corrective arms of SGP involves specific normative contests over the balance between states and Euro zone institutions as well as over the balance between Eurozone states and markets. Thus, I argue that the new ethics of EEG are vital for effective policy coordination and sustainable Eurozone development

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## 1. Introduction

The current European debt crisis is having a clear deleterious outcome on European integration process. It is calling into question the role of European Union institutions as suitable vehicles for European sustainable economic development (Ioannou and Stracca, 2011:6; Kotios et al, 2011; Kotios and Roukanas, 2013). It further demonstrates that the existing European Economic Governance (EEG) provisions do not address the systemic/national terms of crisis (De Grauwe, 2013; Torres, 2013).

Taking into account the shortcomings of EEG mechanism (Buti and Carnot, 2012; Gros, 2012; Salines et al, 2012; Gocaj et al, 2013) crucial ethical questions exist and need to be answered, including the following: what ends should euro zone countries pursue? Is there a possibility for the apparatus of EEG to be ethically positive, negative or neutral? How should the risks, benefits and burdens of EEG be distributed in Euro zone states? What ethical and value issues need to be faced in EEG practice? What moral responsibilities if any, do rich euro zone states have towards impoverished euro zone regions? Who ought to decide these vital questions? European Commission, European Council, European Central Bank, European Parliament, a regional euro zone economic hegemony, technical experts, national states or Eurozone people? Is it possible and morally desirable to outline ethical principles of EEG if there are outstanding ideological conflicts among euro zone states with unequal economic and political power? Does neo-classically conceptualized Stability and Growth Pact (SGP) delimits or limits the potential of EMU? Finally, what type of reforms to SGP ethical pillars would be required to render an alternative SGP morally and operationally defensible?

Apparently, EEG rules / practices / norms do have ethical and valuational characteristics which should be studied and thus ethical questions should be involved in current academic debate over the future of European Economic Governance. Hence, moral principles influence the questions economists/technocrats pose as well as the answers they provide as possible and legitimate (Hazakis, 2010). Thus, it is time to ask how European Economic Governance Ethics (EEGE) could render efficient the allocation of responsibilities for economic policies through significant transformation of the operational and normative pillars of Euro zone.

By EEG ethics I mean the normative / ethical evaluation of the ends and means of EEG. More precisely, it is the structured means and well defined ends in which the divergent preferences, of European institutional/non-institutional actors, are translated into policy choices to allocate resources, values and norms so that the plurality of interests is transformed into coordinated action, attaining maximum compliance of involved agents. EEG ethics is clearly an exploration of what a good and fair European Union is and which norms are attached to such a situation. Thus, EEG ethics do not provide only a solid framework for assessing EU institutional economic action and decision making but they also provide a substantive content to alternative economic policy principles.

Of course, the key question to be answered is not only on which ethics SGP is constructed but also how can arrangements /processes of SGP be framed by rules so that euro zone states are enabled (to the largest possible extent) to pursue in mutually compatible ways national and collective (European) interests. Unavoidably, the focus is on the fundamental traits of SGP economic regime or put it in the Hayekian way (1973) on how the order of actions is influenced by the order of rules. It also concerns the practical question of how euro zone states could improve the SGP provisions within which they act by applying better rules of European Economic Integration game.

I argue that an alternative non-neoclassical concept of EEG ethics could clarify EEG as a mechanism of fundamental change, assessing different national interests and encouraging morally informed national/EU institutional actors. Such an EEG model/policy presupposes a normative answer to the question “what is the ultimate purpose of such an alternative EEG structure?” Thus, we need critical and explicit reflection on the ends as well as on the means of EEG, on the what/why as well as on the how. However, apart from this, there is a need to uncover from an ethical point of view the causal linkages and asymmetries of power between EEG structures, institutions and actors, underlining when and how national/collective/institutional intentionalities are in conflict. In that case the question is not only”what is morally right for European economic integration” but also”what is prudent for Euro zone states”. This clearly suggests that a relevant analysis is not to focus on EEG institutions per se as isolated and self-perpetuated units but it is to focus on their interactions allowing a comprehension of their dynamics and effectiveness.

For alternative EEG ethics, EEG institutions matter but what is more important is how these institutions are composed. For example six-pack, Fiscal Compact Treaty (FCT), Euro semester and Europlus are considered the most recent contributions for EEG but their interrelationships are the crucial point for evaluation of their intentionality and effectiveness. I also suggest that alternative EEG ethics consider EEG intentionality, competence and legitimacy as not abstracted from specific norms, values and path dependence. More precisely, taking into account Rawlsian analysis I argue that an alternative ethical framework of EEG employs four key principles:

a. Respect for fairness which represents the idea of a European social contract capable to promote not only long term legitimization of EEG structures and norms but also maximization of positive spillovers created by integration process.

b. Respect for eurozone states autonomy in developmental issues enforcing eurozone common group identity through participation in EEG decision making

c. Respect for eurozone people well being which represents the effort not only to limit regional/social inequalities but also to improve access of less privileged people to education, knowledge, health, social security and skills.

d. Respect for European economic integration which represents efforts to deepen integration in all issue areas of economics and politics.

The article is structured in four sections. Section one introduces the key ethical questions of current EEG. Section two illustrates the fundamental pillars of neoclassical rationale of EEG while section three highlights the content of an alternative EEG ethical framework. Finally, section four concludes by suggesting that new ethics of EEG are vital for effective policy coordination and sustainable eurozone development.

## 2. The Neoclassical rationale of SGP and the emergence of "Frankfurt Economic Dogma"

The positive/normative economics dichotomy (Rothschild 1993:16) which underlines the role of values in economics is also apparent in European Economic Governance debate and is labeled in my analysis "Frankfurt economic dogma".

Neoclassics present eurozone as an ethics-free area where transparent market conditions and free circulation of factors of production determine prices and investment choices. Monetary stability is the main anchor and its multiple policy channels the only coordination mechanism independent of discretion. Full compliance to derived EEG rules (pacta sud servanda) is a condition sine qua non for Eurozone smooth operation since if there is time lag between EEG contracting and servicing the provisions of the contract, uncertainty enters as to whether the EEG contract will be served as agreed upon. Frankfurt dogma used to be a Frankfurt consensus in early 2000s when the stability paradigm was based on interstate communication and eurozone states' preference for a linear and well defined monetary perception of EEG evolution. However, the latest debt arrangements clearly demonstrate that although Germany has bargaining power, it does not have persuasive ideas of a non fallible paradigm. Of course, current monetarist view is saved due to a combination of institutional inertia, lack of collective eurozone will for a new balance of benefits / risks / responsibilities / competences in EEG and absence of a commonly accepted cognitive framework for EEG practice. However, this does not hide the fact that "superior EEG policies" use the ends (European economic and political integration) to protect the means rather than vice versa and this is morally unacceptable. EMU succeeds only temporarily as long as its means are compatible with economic targets of the regional hegemonic state.

Further, the Frankfurt Economic Dogma of the ethical neutrality of macroeconomic management is the major reason that neoclassic EEG practitioners have been uncomfortable with and have extrapolated ethics from European Economic Integration agenda. The dogma holds as an uncritical belief that price stability is such a strong target that becomes de facto an end in itself, a self-fulfilling economic prophecy. Similarly, the dogma affirms that monetarism is ethical neutral in the meaning that euro zone states can use its tools for good or bad but monetarism itself is valuationally neutral. Consequently, price stability and monetarism are placed on the objective side and EEG ethics/values on the subjective side of the debate. It is no coincidence that the agreement on the virtues of monetary stability among technocratic and political elite became institutionalized in EMU provisions and in more recent intergovernmental reforms of EEG, providing a foundation for the operation of euro zone despite concerns and key facts about the problems of a "one size fits all" monetary policy.

Indeed, it seems that policy makers share normative and causal beliefs about means-ends of European economic integration and about the content/nature of monetary policy. This is why they incorporated neoclassic logic in EEG not only as procedural rules conducive to specific national fiscal action but also as numerical rules ( such as the criteria on debt and deficit). Moreover, it is clear that a Frankfurt economic dogma applies a series of neoclassical prescribed policies (i.e. fiscal discipline irrespective of economic/business cycle or exchange rates targeting irrespective of competitive monetary policies of USA, Japan, Switzerland and China) but also promotes cognitive routines (Eurosemester), practices (Europact+), norms and economic institutions with "political leverage" (i.e. the independence of ECB) to accommodate these policies. According to Frankfurt economic dogma poor macroeconomic performance in eurozone is due to fragile member-states which are unwilling to comply with necessary reforms or as it is often written "to do properly their homework". These states are either subjected to pressures of particular groups and populist demands or are captured by perverse ruling political/economic elite. Vested interests and strong lobbies resist reforms so as to maintain access to rents (Annett et al, 2005). In addition, the Frankfurt economic dogma holds that reforms should be applied without time/space exceptions in order to restrict rent-seeking and so as to alter rent-creating regulations and crowding out effect practices. Structural reforms are presented as welfare and equity enhancing in the long run through the dismantling of economic/political interests that allow vested interests to siphon off vital public resources. Moreover, it is argued that EU economic governance is lagging behind eurozone necessities and needs to be reformed. Based on this suggestion, the painful economic austerity package is presented as necessary process in order to achieve sustainable growth in the long term since it creates conditions for Schumpeterian creative destruction normalizing all product/labor/financial market imperfections. But, which is the theoretical background of the Frankfurt dogma?

In a pure neoclassical perception of EEG there should be no ethical assumptions or normative implications. As M. Friedman (1953:7) insists for economic science "its goal is not to tell us what ought to be the case but to describe what is the case". According to Friedman "positive economics is in principle independent of any particular ethical position or normative judgments…its task is to provide a system of generalizations that can be used to make correct predictions about the consequences of any change in circumstances…it is or can be an objective science, in precisely the same sense as any of the physical sciences" (Friedman, 1953:4). He also notes that "marginal productivity analysis of the determination of rates of return to resources does not have any ethical implication". Accordingly, the key injustice is the primary distribution of resources, "the fact that one man was born blind and the other not" (Friedman, 1976: 199-200). Obviously, moral virtues are calculated strategies for utility maximization rather than Kantian categorical imperatives. As a result, efficiency and stability play a key role in equilibrium analysis of EU markets and derive spontaneously from the action of EU economic agents.

However, as it is demonstrated in following sections, there is no value neutrality in this economic dogma and of course moral questions should be properly answered especially as far as it concerns the imposed exclusion of alternative European developmental proposal. Moreover, I insist on the term "Frankfurt economic dogma" and not on the term "Frankfurt Consensus" (like the well known Washington consensus) since its properties are not any more (as it was the case prior to 2009) the outcome of policy elites belief in the correctness of model but it is the outcome of a constructed and self-legitimating process where dogma principles are strictly linked to financial conditionality. I further argue that EEG (and recently revised SGP) is not a technically constructed rule agreement but an ethically guided arrangement since specific neoclassical principles/ norms/ practices constitute the pillars on which EU states /actors base their patterns of behavior. So, which are the major pillars of Frankfurt economic dogma?

Firstly, price stability is being given primacy (Maastricht Treaty, article 105 and article 127, paragraph 1, of the Treaty on the Functioning of the European Union concerning the corresponding role of European System of Central Banks) over all other economic targets (Papadopoulos, 2013:42) and thus low inflation rate is conditio sine qua non for smooth euro zone operation. There could be no trade off in any point of the economic cycle between inflation and unemployment or inflation and demand-led growth. In order to guarantee a sterilized stability strategy irrespective of economic/business cycles, ECB is nominated as the key independent institution to exert monetary policy. The latter provides the anchor for inflation expectations and obliges member of the eurozone area to plan their national budgets in line with SGP and from 2013 in line with FCT. Equally important, the Treaty lays down the fact that any exchange rate policy should be consistent with the primary objective of the ECBs monetary policy which is to maintain price stability. Further, article 111 of the Treaty allows the European Council following stringent procedures to conclude formal agreements on an exchange rates system for the Euro in relation to non community currencies or to formulate general orientations for exchange rate policy (see also article 119, paragraph 2 of the TFEU). However, the meta-rule of price stability provides the limits of this power and obliges that any agreement or orientation should be consistent with it. Taking also into consideration the links between productivity growth, wage levels and stability of prices, it is considered that real wage increases which are not above productivity growth trends maintain the key target of price stability. Finally, the apolitical and technocratic justification of ECB activities is considered an intrinsic part of its legitimacy and credibility. From the previous analysis, it is apparent that fiscal, financial and structural policies are subordinated to monetary policy priority in order to attain price stability.

However, taking into account the ethical criteria mentioned in introduction, it is evident that not only ”an all economic cycles inflation targeting” is not feasible but it is also non fair in collective terms. Apparently, many questions arise from the logic of the first neoclassical pillar. What constitutes an acceptable level of inflation and who is responsible to define it, taking into consideration asymmetric spillovers and structural discrepancies in eurozone regions? Further, is inflation targeting per se sufficient or is it part and parcel of a monetary targeting based only on money supply techniques? Equally important, which are the repercussions of a monetary policy not just in structurally different regions but also in regions with different crisis dynamics? How one could sustain European living standards if internal devaluation strategy concerns only wages and pensions and not the prices of basic inelastic goods and services? How one could accommodate social justice in prudent price policy if (for example) fiscal revenues from high taxes on fuels aggravate living conditions of the most vulnerable social categories in fragile euro zone regions? Finally, with either monetary targeting or inflation targeting considered ends of economic policy making which are the welfare /distributive means for their smooth social application? Unfortunately, European economic experience clearly demonstrates that price stability pursued independently of economic cycle and national developmental needs is achieved at the detriment of national output potential because fiscal contraction which accompanied it has negative procyclical effects. National savings are reduced and available capital for loans is limited with negative repercussions on capital accumulation and national investment.

The second key pillar of the Frankfurt Dogma is that budgetary stability and absence of chronic trade deficits accommodate European monetary policy and reduce public debt levels. Abiding by budgetary supervision (initially as part of the convergence criteria of EMU, later as part of SGP established with the treaty of Amsterdam and now as part of FCT, Macroeconomic Balance Procedure and Six Pack intergovernmental agreements) is necessary because budget deficits for one eurozone state create negative externalities to other eurozone states favoring free rider behavior at the detriment of stable monetary policy. Negative spillovers also emerge from the incentive of states incurring budget deficits (Morris et al, 2006:6-8) as all costs are born by the eurozone as a whole, aggravating further financial instability and interest levels of bonds. Equally important, it is argued that spending biases are strengthened by vested interests and bureaucrats who are willing to lock-in budget allocations (Niskanen, 1971) that are higher than efficient allocations. This also means according to neoclassical approach that budget deficits aggravate intergenerational burdens since the current decision making mechanism decides a non efficient and exorbitant consumption led deficit at the detriment of those who will pay it after 20 or 30 years (Cukierman and Meltzer, 1989). Frankfurt economic dogma also insists that multinational intervention may only make things even worse by posing moral hazard issues and rewarding prolonged maintenance of unsound fiscal policies. So, a debt crisis is constructed as a state failure, discrediting cooperation in the form of developmental capital or other forms of aid and legitimating reliance on austerity as the only means to adjustment irrespective of national cycle needs. This is exactly why FCT of the Treaty on Stability, Coordination and Governance (TSCG) focuses both on fiscal procedures and on fiscal outcomes forwarding four major targets which are the following:

1. There is a balanced budget rule including an automatic correction mechanism to be applied in national law.

2. The excessive deficit procedure is strengthened.

3. There is a clear enforcement of the numerical benchmark for debt reduction for member states with government debt exceeding 60% of GDP.

4. There is an ex ante reporting on public debt issuance plans to the European Commission and the European Council which allows for a better coordination of debt financing among member states, increasing the transparency of governments debt management strategy.

Finally, it is further underlined that fiscal policies are exerted with a view to limiting risks to price stability (i.e. articles 123-126 of the TFEU).

More precisely, the individual responsibility of the member states in the field of budgetary policy is explicitly underlined by the treaty’s no bail out clause (article 103) which mentions that neither the community nor any member state shall be liable for the commitments of another member state. The prohibition of monetary financing of public deficits by ECB (article 101) and of privileged access for public authorities to financial institutions (article 102) represents rigid and binding rules to the conduct of national fiscal policies (Schuknecht, 2004). Thus, it is easily understood that FCT and Six pack provisions oblige eurozone states to submit annual stability programs and balances outlining their budgetary plans in conformity with the medium term objective of budgetary positions close to balance or surplus. Evidently, sound public finances are not just another principle of economic policy making in EU (article 4, par 3) but do have a specific content (Bergman et al, 2013).

However, a number of practical and ethical questions remain unanswered. From a legitimacy point of view, the FCT obliges people to accept budgetary rules that do not result directly from the national democratic deliberation. People should accept these rules as permanent either as precondition for financial aid or as a result of intergovernmental quid pro quo to save eurozone. Moreover, any eurozone state wishing to receive help from ESM is invited to ratify the treaty and to transpose the balanced budget rule into its legislation. As it is stated in article 136 (TFEU) “the granting of any required financial assistance under the mechanism will be made subject to strict conditionality". The Treaty on Stability and Convergence in the Economic and Monetary Union also states that all contracting parties accept that their budgetary position of the general government shall be balanced or in surplus (article 3a) and that "the rule shall be deemed to be respected if the annual structural balance of the general government is at its country-specific medium-target objective as defined in the revised SGP with a lower limit of a structural deficit of 0.5% of the gross domestic product at market prices. The contracting parties shall ensure rapid convergence towards their respective medium-term objective"(article 3b).The preventive arm of the SGP further enforces member states to maintain or to adjust towards their respective medium term budgetary objectives (MTOs) while the corrective arm of the SGP ensures the correction of excessive deficits in case they still take place. Evidently, FCT becomes a self-enforceable compact through a repeated game of involved agents (governments of eurozone) which should behave cooperatively based on prescribed austerity rules since gains from following these rules always exceed gains from opportunistic behavior in net present value terms. The basic argument is that eurozone membership has such sunk costs for each member state that deterrence is out of question.

However, the problem of compliance is not solved in the long term through enforcement but through an ethical framework which once adopted (based on a strong cognitive consensus of involved states) it could provide credibility in EMU rules and principles. As eurozone experience shows, automatic stabilizers could indeed operate when eurozone economies are close to balance or when deficits are due to regular marginal ups and downs of economic/business cycles but not when needing to correct excessive structural deficits combined with high debt to GDP ratios and contraction in demand. Such a mixture of political economy conditions renders deficit adjustment without real convergence and welfare programs not only unrealistic but also dangerous for long term interstate cohesion in eurozone.

It is also clear that FCT and Six-Pack as the last version of SGP fiscal surveillance mechanism do not provide sufficient incentives for the correction of fiscal imbalances linked to productivity and growth but rather adopt a static target of fiscal discipline at the detriment of long term growth. But which is exactly (at the analytical level) the "qualities" of golden budget rule, i.e. is there a direct positive relationship between budgetary contraction and national growth or even between budgetary contraction and vested interests proportion of national GDP? Recent surveys on fiscal multipliers underline that in advanced economies stronger planned fiscal consolidations have been associated with lower growth than expected with the relation being particularly strong early in the crisis (Blanchard and Leigh 2013) and equally important that the position in the business cycle affects the impact of fiscal policy on output (Baum et al,2012).

Further, from an ethical point of view which are the long term costs of national economic adjustment and how they are distributed? Is there an agreement over the acceptable size of groups living under poverty due to automatic rules of balanced budgets? Is there a time frame for combating negative consequences of a general austerity program on people of fragile eurozone societies? I argue that the permanency of the golden budgetary rule imposes a means regardless of the target of well being of eurozone people and regardless of economic conditions. Policy makers are in the same policy trap as in the 1990s when the launching of Euro took place without a coherent and reliable fiscal policy although now the situation is the opposite. Fiscal rules are imposed irrespective not only of the necessities of business cycle but also of the fundamentals of the Euro currency.

I also argue that the problem is not only effective budgetary supervision but also budgetary solidarity targeting equally national growth and national debt. Otherwise, budgetary supervision does not bring results as GDP is reduced, unemployment soars and heavy tax burden diminishes tax revenues due to Laffer curve effect. A sharp negative demand shock does not solve debt to GDP problems but involves the country in further FCT violations making fiscal policy procyclical under the FCT/SGP rules. As fiscal adjustment involves automatic actions to do simultaneously dramatic spending cuts and reduction of personal disposable income through tremendous increases in direct/indirect taxation, it leads to inability of most households to pay their duties, to further rise of national deficit and to further automatic measures under FCT logic. This also leads to smaller propensity to save, lower national savings base putting already vulnerable (in capitalization) national banks in more problematic situation asking for more liquidity from ECB and more recapitalization from ESM. As a result both ECB and ESM throw money with no impact on real economy or on development since there are no loans to productive or export led enterprises but only capital for attaining capitalization targets. However, a constant ratio of debt to GDP could be sustainable as long as GDP growth exceeds the real interest rate and thus it is an urgent priority to concentrate on stimulating economic growth through productivity upgrading than through lowering (without any effective benchmarking) governments deficits.

The third pillar of Frankfurt dogma is that the debt ratio to GDP is a target which should be accomplished more through reduction of public expenditure and less through rise of GDP. ECB again is treated as a privileged creditor since it has to grant no debt cancellations which could jeopardize monetary/inflation targeting. On the other hand, the debtors within eurozone commit to full implementation of conditionality in exchange for ad hoc and case by case rescheduling of national debt by the creditor eurozone countries and the new mechanism of ESM. Instead of finding solutions to financing the gap between national investment and national savings (I/S gap) debt reduction deprives from national governments any possibility to respond to the particular conditions of domestic economies in a flexible manner through a mixture of eurozone and national fiscal instruments.

This clearly calls for an expanded supranational development - oriented EU budget and of course for a coinsurance scheme of national debts taking into consideration the enhancement of responsibilities of European Parliament on key aspects of EU fiscal sovereignty. Indeed, it becomes clear that euro area was characterized until 2012 by a unique combination of centralized monetary policy making and largely decentralized fiscal policy making and that the feature of “a single monetary policy and many fiscal policies” was also a problem to the smooth functioning of EMU. However, one should also ask what kind of eurozone fiscal policy do we really need and how a coordinated (or even centralized) policy making could act in both preventive/corrective way to revive sustainable economic development in all regions of the euro area. There is now enough experience from eurozone crisis to suggest that regional and cyclical divergences within the EU will not be self-correcting but rather require development measures through an enhanced EU fiscal policy. Within this logical framework, an enhanced EU budget should not be considered a redistributive money mechanism for consumption growth but a compensation mechanism to allow growth for lagged regions and permitting real and not only nominal convergence. As De Grauwe eloquently mentions “a central budget is important as a redistributive device. It also matters as a stabilizing instrument. The absence of a central budget in the euro area implies that no budgetary policy aimed at stabilizing the business cycle in the union is available” (De Grauwe, 2006:723). Moreover, higher budget flexibility for developmental purposes is needed to address country specific shocks in the absence of national monetary independence. Contrary to this, FCT discourages de facto public and private investment since there is a crowding out effect for debt installments combined with close to balance or in surplus budget position. Thus, taking into account the essence of article 99(1) of the Treaty which supports that member state of EU should regard their economic policies as a matter of common concern and shall coordinate them within the Council there is an urgent need for a coordinated developmental policy targeting at real convergence of eurozone regions.

Equally important, the fact that stabilization of inflationary pressures concerns mainly the balance between spending and taxation, decisions on the provision of public goods and on taxes content are undermined. As in the case of budget supervision critical redistributive and allocative consequences of a long term debt straight jacket are not faced. The EEG rationale is only to guarantee national loans interest rate payments and not equally to finance public and private investments so as to structurally transform low productivity economies. This clearly set the terms not for a transition from a suboptimal point of national economic production curve to an optimum point but it creates the conditions for further contraction. As European Union experience underlines, contraction provoked by a structural and long term high debt /GDP ratio in lagged economic regions did not automatically led to a more efficient allocation of resources. Greek paradigm clearly demonstrates that markets and prices refuse to adjust and thus social dichotomies and division between social groups become larger. Overall, there is a problem when deciding whether a deficit or debt to GDP ratio is excessive because non compliance after initial stages of austerity measures maybe a result of contraction per se and not of excessive consumption - led domestic growth. Finally, one should again mention that European Parliament is absent from the procedure leaving the decisive role of the evaluation to European Commission which is heavy influenced by ECB metarule of price stability. However, without a strong European Parliament the complexity of the question of the supervision from EEG institutions (who supervises the supervisors?) remains and is multiplied since rules are perfectly legal but lack considerable legitimacy and true democratic accountability.

According to the fourth pillar of Frankfurt dogma it is considered important to apply policies aimed at the micro level of economic activity (i.e. labor markets, financial markets, product markets). Indeed, textbooks on European economic integration underline that a single market in which goods, services, capital and labor circulate freely is a conditio sine qua non for integration. However, the pace of European integration is not the same in abovementioned sectors and thus there is no case for a Walrasian automatic equilibrium in all markets. Without necessary instruments to tackle the roots of the structural/economic problems (Pasterniak, 2007) namely, rigidities in goods/services and labor markets, EEG could not ensure in the long term competitiveness, sustainable employment levels and high growth rates in euro area. Thus, it is suggested that economic structures robustness should be further strengthened against adverse economic shocks and fluctuations (Issing, 2002: 354).

A number of key issues also arise in the analysis of the fourth pillar of Frankfurt dogma. If labor market flexibility and reform of employment procedures are so important steps to efficient operation of eurozone as an optimum currency area why labor market targeting is not included as a target or even as an incentive in revised SGP? Since all member states are committed to the common goal of a high level of employment (article 2 of the Treaty) why this goal is not given an equal foot? European law clearly favors employment targeting as a major pillar of European integration. Article 125 of the Treaty calls for a coordinated strategy for employment and article 128 provides the basis for employment guidelines. Moreover, the Luxembourg process obliges member states to consider employment as matter of common concern and the "Annual employment guidelines" set out recommendations and priority areas of action. Further, since 1998 the Cardiff process aims to advance reforms through monitoring analysis and peer pressure while the Lisbon Strategy for growth and jobs underlines the necessity of sustainable employment rates. Despite all these decisions, employment is considered de facto as a tool at the disposal of the price stability meta-rule. Instead of providing incentives to member states to achieve convergence in labor market, analytical and policy priority is given on specific monetary issue areas. Evidently, the focus of new EEG ethics should be on reduction of unemployment and thus ethics could not support a NAIRU framework to maintain inflation targets at the detriment of new jobs. I suggest that the neoclassic perception of NAIRU violates the right of European citizens to jobs and uses unemployment rate as an instrument to maintain price stability despite negative spillovers on social cohesion.

Apart from the problems of the four key pillars of the Frankfurt economic dogma, there are unanswered questions on the social dimension of European economic policy (for the distributional effects of fiscal consolidation see Gruner, 2013). First, when national budgets suffer from chronic imbalances what is the impact on public goods such as social security, education, health and internal security for the less advantaged social categories directly hit by austerity measures and unemployment? FCT rules oblige member states of eurozone not to use national policy instruments for generous social policies or even to sustain conditions for employment creation through targeted strategies such as reduction of VAT in certain economic sectors (i.e. in Greece VAT rate is 23% acting as a barrier to entrepreneurship). Second, which is the impact of shock therapy reforms advanced by FCT and Six-pack in eurozone states whose bargaining power and internal capacities are weak? In Greece for example civil service reforms aimed at downsizing staff size and wage expenditure without suitable forms of staff evaluation, accelerated the dereliction and loss of credibility of public institutions especially the judiciary, customs internal revenue administration and education, undermining reform dynamics. Thus, instead of a productivity to wage reform implementation, the ethics of downsizing all irrespective to performance, undermined the operational capacity of state. The solution of transitory administrative enclaves which could handle the reform package through institutional reorganization proved inefficient. Thus, it is beyond dispute that reforms only on financial issues and not on institutional and operational capacities of civil service, provides suboptimal results. High administrative burden as well as inadequate governance structures perpetuated vested interests dominance (Sklias and Maris, 2013). This means that rent seeking groups acting as "Vikings" curtailed competition, hindered transparency and increased transaction cost in order to maximize their profits at the detriment of national resources (Mitsopoulos and Pelagidis, 2012). It is also evident that in deep and structural economic crisis, institutions cannot be fruitful only through "paper reforms" because their particular arrangements credibility, degree of acceptance and rhythm of development are endogenous.

Apparently, the role of new EEG ethics is also crucial in the fourth pillar. Macroeconomic surveillance should act in a preventive manner underlining that the macroeconomic imbalances that threaten the smooth operation of EMU such as persistent losses in competitiveness, long term current account deficits derived from consumption led growth, unsustainable increase in asset prices due to construction bubbles financed by banks, extended tax avoidance and persistent rates of structural unemployment and income divergences, are the key targets. Thresholds in each of the abovementioned problems should be based on national ownership logic and thus cooperation is the tool through which the peculiarities of all eurozone states are taken into consideration. Of course, this also means that European budget should be strengthened to make it consistent with a Lisbon oriented target for productivity and sustainable employment.

## 3. Defining the new ethical basis for European Economic Governance (EEG)

Neoclassical and institutional approaches of EEG are based on different presuppositions about EU nature, normative values, EU authority structures and ultimate ends of EMU, employing different concepts to describe the nature and causes of current EEG crisis. What is clearly needed are explicit EEG ethics to answer the ethical and value questions posed by EEG theory and practice and planning, highlighting the value costs of various courses of EU economic action. A system of European economic governance values is not at all separate from the large picture of European integration but it should exist because of it, positioning issues like mutually beneficial cooperation, sustainable economic development, individual economic freedom and democratic accountability of economic regimes as positive public goods. Monetary stability disconnected from these values seems to self sustained in the short term but is in fact a free rider of European integration process taking advantage of eurozone potential and not of eurozone actual economic fundamentals. Although the Frankfurt dogma still holds a Kuhnian predominant status as economic paradigm, it cannot hide that EEG is in disarray due to severe structural/systemic problems of eurozone area, due to the lack of sustainable and consensus-led strategies to face these problems and due to the lack of ethical values to accommodate development strategies. But which are the key principles of an alternative economic approach? Alternative EEG ethics include decision making procedure of EEG, motivation of involved states within EEG, distributive results of EEG practice, developmental/contraction effects of EEG policies and autonomy of eurozone states in setting development priorities.

Firstly, EEG decision making is not about choice within price stability metarule constraints. The latter include not only budget debt and price constraints explicitly accounted from Maastricht Treaty and recently enforced by FCT and Six pack provisions but they also include the behavioral constraints defined by the norms, principles and procedures enforced in SGP. However, ethics of EEG should face not choices within undisputable constraints but choice among constraints of alternative policies. Choice among alternatives positions of efficiency-equity cannot be only technical but incorporate an ethical dimension. Obviously, tradeoffs between equity and efficiency should be accommodated within European economic integration large picture and should not be based on short term dogmatic principles. Thus, the emphasis is not on prevailing rules beyond willful change but on new rules under which eurozone states act, making European Economic Integration game, a better one. While a neoclassical European economics perception focuses on how rational agents are more successful in playing a definitely prescriptive game, a new ethical approach focuses on how eurozone states may be able to play better by adopting new metarules. The claim that SGP arrangements are beneficial for all has no other meaning that the transactions, rules and procedures of SGP are mutually beneficial to all states involved and thus eurozone countries may realize mutual gains from joint commitments if they judge that as suitable and desirable for efficient eurozone economic coordination. Thus, the first ethical principle of an alternative ethical arrangement is fairness of the new EEG contract for all involved eurozone states against the logic of a hegemonically imposed agreement.

Of course, a new ethical approach of EEG does not ignore the omnipresence of opportunities for gaining at the expense of others, nor does it ignore the temptation for self interested egoistic actors to take advantage of such opportunities. However, the central argument is that a new SGP focusing on mutually beneficial coordination is a much more sustained source of gains and that accordingly there are prudential reasons for Eurozone states to seek to improve further the SGP game by full and long term commission to meta-rules that encourage and facilitate cooperation while discouraging exploitative strategies. The new “give and take” is fair enough because it provides not simply strong punishment rules but also strong incentives to all as well as equal opportunities to drawing the new meta-rules of EEG from all Eurozone states. Cost of defection from such coordination logic is greater and thus, all Eurozone states answer more easily the question, “Why ought we agree to having certain sorts of meta-rules”. So, the principal role of EEG ethics is not ad hoc improvement of specific macroeconomic outcomes but improvement of the nature of the processes from which outcomes result where improvements means that national and collective (Eurozone) intentionality is the outcome of a strong consensus. The central question is what procedures or rules for choosing rules (metarules) are more likely to result in the adoption of rules that serve equally EU economic integration and national economic interest instead of serving the interests of some states in the core of Eurozone at the expense of others. By allowing trust between Eurozone states it makes the latter more willing to engage in cooperation that imposes certain costs but provides strong institutional/financial/structural incentives and long term stability. Thus, motivation of Eurozone states is better accommodated within such an ethical framework.

The second crucial issue is not only to modify EEG ethics (analyzed previously) but also to change the mechanisms of EEG so that they work smoothly with the new ethics. To discern what ought to be is the task of EEG ethics but to explain what is and can be in EEG is the work of EEG mechanisms. There is a strong and dynamic interaction between the two since to know what ought to be one should know what can be. As developmental economist Goulet argues (1997) we need an ethics of means as well as an ethics of limits and goals. One should evaluate which means are morally permissible, impermissible and obligatory as well which means are effective and which goals are prioritized. Further, we need to inquire empirically with respect to what concrete social and economic conditions are needed if appropriate Eurozone moral principles/metarules and development visions are to be realized in people’s lives. Clearly, we need to reflect ethically if the end justifies the means as well as given the means at our disposal which ends are prioritized and why.

Thus, the second major pillar is “respect for autonomy of involved Eurozone states” within the commonly accepted ethical/institutional framework of EEG. This is also important not only for policy tactics flexibility in national economic decision-making but also for accommodating still existing national economic structure differences in Eurozone states. So, one should provide insights into the emerging interaction between the new order of metarules and the new order of actions in EEG edifice. It is an indirect strategy for building a better EEG not by ad hoc or discretionary interventions but by changing the rules through which the system operates. In this way EEG provides the means for economic conditions that better enable the involved state to pursue European economic integration and national purposes individually and collectively using not only EEG tools but also its own specific knowledge of relevant economic/political/social circumstances. The derived national autonomy in setting development priorities outside "memorandum contracts" also reduces free rider logic and contributes to a cumulative experience - guided process of trial and error, favoring learning/adaptation within the prescribed limits of new ethical framework of EEG. In other words, the focus is on the factual working properties of procedures/rules rather than on subjective evaluations of economic policies. Of course, this second ethical dimension faces two institutional uncertainties, namely assumptions about the uncertainty or ignorance of the states involved concerning their national economic interests and assumptions about the extent of their knowledge over the problem .This also means that metarules should provide strong arguments for how the obstacles arising from uncertainty/ignorance and perhaps short term partial interests can be overcome. This is also why I argue that FCT and Six Pack is not the proper institutional context to embed EEG policy making because it does not provide flexibility and learning/adaptation mechanisms for all involved eurozone states.

The third ethical dimension is that of well being which usually represents a utilitarian principle. It revives a debate similar to that caused by the reunification and the inequality of economic development between the German Lander. It raises the issue of European solidarity and the use of public funds in this context. It further highlights the issue of living together that is the basis of any political community at Federal level. Again, the principal EEG role is not to improve outcomes by classical Keynesian type large scale transactions but going a level beyond, it is to improve the nature of the processes from which allocation outcomes result, where improvement means to better enable eurozone states involved to advance developmental purposes collectively and nationally. Well being is strengthened through developmental aid and not through unquestionable capital transactions for consumption led growth and thus it is rent seeking free. One should always bear in mind that improving EEG framework so as to enhance the prospects of mutually beneficial transactions and joint economic activities is not only a technical matter within the Optimum Currency Area theory but it is also a key ethical principle for a just and fair economic integration. Prudential economic governance without welfare basis is a camouflage for a priori bias against any public intervention for social security and social cohesion provisions.

This also means that EEG decision making should not be based on neoclassical utilitarian ethical perception according to which the total welfare of eurozone is above all other goals regardless of its quality traits and its distribution results. In contrast to self imposed operational values of market efficiency we need a Rawlsian justice principle focusing on the norms of distributing primary goods in people like social safety net, liberties and opportunities to improve their lives. Evidently, total welfare in eurozone is not a byproduct of efficiency but it is a critical functioning trait of a fair EEG mechanism and thus a new ethical framework of EEG should provide necessary capabilities and competences to properly address the qualities of such functioning. Efficiency and distribution within eurozone are interdependent because for every distribution of wealth/income there is a different allocation of resources which is more efficient. Thus, choice among alternative positions of efficiency cannot be only technical but incorporates an ethical dimension. If someone accepts tradeoffs between equity and efficiency, sterilized stability is accompanied by deterioration in distributive equity. If on the other hand someone selects an abstract definition of equity in eurozone without criteria and values, eurozone will be led to short term rent seeking with less distributive output in the long term.

Fourth, all eurozone states are assumed to be equally moral entities and thus deserving moral respect independent of their capabilities. This means that free and equal states are involved in determining EEG content and equally committed to complying with the new key properties of EEG ethics. The new EEG model provides a sense of dignity to all eurozone states and should give them a sense of belonging and of contributing to the application of European integration idea. It goes without saying that European sovereignty without European identity is placebo. Conclusively, the new EEG mechanism should focus on five fundamental targets which are the following:

1. Satisfy fundamental needs (education, health, security) of involved eurozone states.

2. Coordinate efficiently the behavior of eurozone states based on a strong cognitive framework of European solidarity.

3. Provide well defined and operational norms of conduct shared by eurozone states.

4. Act as an anchor of justice for the less developed regions of eurozone

5. Promote European economic integration in all issue areas still lagged behind informing continuously of the consequences of any value driven imperative and action.

Under which conditions eurozone states will adhere to the above mentioned principles? They will follow if they are convinced that collective European intentionality prevails and accommodates their national well being, minimizing internal weaknesses and external financial threats. Pacta sud servant is the outcome of such a group identity and will be continuously strengthened by mutual trust, credibility and a common moral ground. Thus, it is easily understood that stability of eurozone is a function of both its economic and ethical rationality across the different regions that make it up as a whole. It also follows that if economic and political terms arise within which the European values would be better served by having different currencies then support for euro would break down.

When all analytical levels are put together with necessary decision making and resources an alternative EEG emerges. The first step is the removal of the Frankfurt economic dogma from the core of EEG and the removal of misguided separation of values from decision making practices. Second, the ends of European Economic Integration are restated meaning that EEG mechanisms work against provoked inequalities as much as possible. Further, EEG effects are mutually beneficial for involved eurozone states in the meaning that some states are not sacrificed to achieve greater welfare for the remaining states. Evidently, eurozone positive spillovers are the equivalent of Rawlsian common collective assets and thus every eurozone state is equally entitled to them and to their effects.

## 4. The ethical reconstruction of EEG imperatives

EEG mechanism is suffering from the disequilibrium of stagnation. The cost of going backward is almost prohibitive and the pressures to change make it impossible to stay still. The article argues that current EEG mechanism has run out of steam. The monetary advantages are less than what was promised, are inequitably distributed, are inefficiently administered and are against a collective European vision. Practice and results of Frankfurt economic dogma demonstrate that we have not chosen the option with the highest collective expected utility or with the minimum collective opportunity cost. Conclusively, Eurozone cannot go ahead through ”compromise traps” but is obliged to reorganize long term developmental flows to allow maximization of potential output in all regions. The assignment problem and the internal competences problem should be redesigned taking into account that the eurozone debt crisis is not usual cyclical crisis but a fundamental structural crisis of the EEG mechanism. Thus, there is a need for fundamentally different social scientific axioms to express the relevant moral / ethical values. This means that economists do not discharge themselves of their academic duty by posing morally acceptable values as goals of economic action. Nor does it suffice for them to assess the economic and political instrumentalities employed to pursue these ends. Rather, economists should analyze the value content of these instrumentalities, asking for example whether monetarism favors equity or not. Ethics of EEG in this way, serve as a moral pillar, illuminating the value questions hidden inside instrumental means by those who take economic decisions.

Accordingly, four major issues arise. First, there isn’t a dichotomy between positive/normative economic analysis since values/norms are omnipresent in European economic integration theory and in EEG mechanism. Monetarism acts as a meta-preference exerting strong guidance on ranking /priorities/ choices of all issue areas in EEG. Ethical values shape the way EEG works as well as how it should work. Second, there isn’t an abstract eurozone self interest independent from European integration path dependence and eurozone states material interests. Third, motivations do influence EEG content and decision making, shaping behavior of eurozone state and non state agents. Fourth, efficiency of EEG has also a welfare dimension and is linked to collective intentionality of European economic integration. Hence, it is suggested that EEG will be efficient the stronger the consensus on its morals/ norms/ practices and the higher its effectiveness on development/monetary/prosperity targets. Which are the key policy implications derived from previous economic analysis? One should underline the following:

a. Economic growth, social cohesion and stability go hand in hand and thus bias in favor of stability (and more precisely only price stability) works to the detriment of development. Moreover, prudent fiscal rules have to be not only internally consistent but also consistent with other eurozone macroeconomic and developmental targets.

b. SGP is run by asymmetric incentives logic underlining sanctioning and downplaying incentives to behave according to commonly accepted ethical/numerical rules. Thus, there is a need to move from a sanctions oriented EEG framework towards an incentive based approach that treats eurozone member states as partners. The legalistic perspective of EEG renders eurozone management both ineffective and unethical in contrast to a needed ethical perspective that stresses ownership participation and knowledge based EMU regime. Consequently, lack of commitment on the part of member states is not independent to the nature of imposed EEG rules.

c. Reformed ethics of EEG should target not only on fiscal/developmental targets but also on proper institutions to supervise both fiscal discipline and bank exposure to non reliable investments. This also calls for an EU agency to rate banking activity and capitalization adequacy.

d. There is a need for “development and budgetary solidarity” strengthening eurozone social capital and creating a new economic regime where asymmetries and divergences between rich and poor regions are properly and timely accommodated. In this way, Eurozone regions minimally advantaged by eurozone dynamics will tend to be compensated by strong developmental inflows targeting exclusively on restructuring of capital accumulation processes and on social safety nets during painful austerity period. It also follows that eurozone ethics is not just applying balanced budgets or getting prices right. It is all of these things plus more. It is providing each citizen in eurozone economies with the ability of equally access to the complete set of Rawlsian basic goods.

Thus, it is evident that European economics should not forward dichotomy between ends and means, promoting the decoupling of eurozone market, EEG institutions and eurozone states, but rather need to reflect ethically if the means justify the end and how eurozone market and EEG institutions interact efficiently, targeting in general economic and social welfare. Obviously, for alternative EEG ethics, EEG mechanism matters but what matters more is how EEG institutions compose with each other. Overall, if one is really in favor of a legitimate EEG, the optimization of its decision making should do justice to both ethical and economic dimensions. Accordingly, as long as EEG acts in a short sight way, the veil of uncertainty over the future of European economic integration will be robust.

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