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**FIFTEEN PROPOSAL FOR ITALY'S EUROPEAN
POLICY**

by Ettore Greco, Tommaso Padoa-Schioppa, Stefano Silvestri

Paper presented at the International Conference on “Europe Beyond the Crisis: Fifteen Proposal for Italy’s European Policy”, on the occasion of the 40th Anniversary of the Istituto Affari Internazionali
Rome, January 23 and 24, 2006



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DOCUMENT SUMMARY

Despite the important achievements of the past years (the Euro, enlargement, the drafting of the Constitutional Treaty, interventions in the Balkans and the growing diplomatic role in the Middle East), Europe is at a standstill and experiencing scepticism which, combined with prolonged economic stagnation, could deteriorate into a serious crisis. In this difficult situation, Italy could suffer particularly negative consequences. At the same time, however, it could – as in the past – play a prominent role in providing the Union with new dynamism.

Italy's economic and political position and role in the twenty-first century will depend on the outcome of the European crisis in the coming years. With respect to the economy, our country has a structural weakness that will require whoever takes over the government in the next five years to take decisions to address the central problems of its development model and strengthen its position within the global system. In international politics, Italy has lost or is losing its competitive advantage and will have to re-examine its strategies to avoid being seriously marginalised in a world no longer divided between two blocs and in which large new actors (China, India, Brazil, Russia and Mexico) are coming onto the scene and pushing countries of medium importance such as ours aside.

Europe will inevitably be the framework for decisions on economic and international policy.

Italy is confronted with this delicate situation at a time when its political system is still searching for a balanced approach to the question of what should be 'partisan' and what should be 'bi-partisan' in a regime of alternating governments. When a democracy shifts from no alternation (or a single party: think of Japan, Mexico, India, France 1958-1981, Germany 1949-67, etc.) to alternating governments, the question of continuity or change in its policies – above all foreign policy – becomes acute. European policy is not only foreign policy; it is to a large extent domestic policy. But it is always conducted in an institutional framework in which "external" governments and institutions are present and in which sudden changes in direction can be particularly costly.

It is clear that we are referring to continuity or change in the base-line policy positions, not the whole range of issues on which a government is called upon to decide. Some changes are in fact dictated by events or transformations beyond a government's control.

For a long time, the bi-partisan base of the European agenda in Italy was very broad. In some respects it was even too broad, with the result that automatic support for any proposed integration project in some cases impeded serious debate on the implications of such choices for the Italian economy and economic policy. The pendulum changed direction at the beginning of the last legislature and, as frequently occurs, has perhaps swung too far the other way.

On the eve of an election campaign that is predicted to be among the hottest in recent years, the International Affairs Institute would like to draw the attention of Italian political parties and leaders to a map that it has prepared of the principal issues on the European agenda likely to be debated during the coming campaign: a survey of the various options and positions and a proposal for some stable positions in our European policy.

The goal is to contribute to creating a consensus on those points – in the three major fields of economic and social issues, foreign and security policy, and institutional reform within the Union – on which it is in Italy's (and the rival political parties') interest to maintain continuity. The assumption is that it is not only natural but desirable for the programmes of the two coalitions to differ with respect to all other aspects of European policy. The objective is to turn the IAI document, possibly in a revised edition incorporating the debate at the Conference, into a sort of handbook politicians may find useful as a reference document during the election campaign and in preparing their programmes to present to the electorate.

It should be noted that the degree of differentiation of the two coalitions' programmatic platforms is not the same in all three fields. Economic policy is the area in which the degree of acceptable differentiation is presumably the highest. Indeed, the other two fields are by their very nature, even in the 'national' policy of a given country, characterised by greater policy stability.

The analysis highlights fifteen points of Italy's European policy that, in the IAI's judgement, should remain firm no matter who wins the elections in the spring. The proposals appear to coincide with the vital interests of the country and are, in the drafters' view, essential for its relaunch – which largely coincides with the relaunch of Europe.

I. ECONOMIC AND SOCIAL ISSUES

- 1. Consolidate our participation in the Euro.** *It is not simply a matter of stopping the free-floating complaints about our entry in the Euro and the proposals to withdraw. What is needed is a clearer awareness of the underlying choices that must be made regarding the economy and economic policy in order for Italy to adapt its development model to the competition of the single market and the globalised economy.*
- 2. Observe budget discipline.** *High public debt and the objective fragility of public finances require a structural correction that can only be implemented over a period of time that spans more than one legislature. Rigorous application of the Pact is a bi-partisan element of our economic policy and must be an obligatory choice for any future government. Choices concerning the scope and structure of expenditures and revenues may, and indeed should, be partisan.*
- 3. Complete the single market.** *Precisely because it is not as efficient as other economies in the Union, the Italian economy has more to gain from completion of the European single market in the service and utilities sectors. Bi-partisan support for completion of the single market would also put the seal of approval on the market economy as the essential element of credible strategies for prosperity and development.*
- 4. Develop the community budget.** *Because it is less conditioned by predefined positions, Italy is well placed to launch at the appropriate moment an initiative to progressively overcome the logic of "fair return". The goal is to make the budget a key instrument in the relaunching of a European growth strategy, as recently proposed in the Sapir Report.*

5. ***Make the Euro Group grow.*** Italy has an interest in strengthening the role of the Euro Group both internally (greater coordination of economic policies in the Euro area) and internationally (adequate representation of the Euro area, ultimately with a “single voice” in the G7 finance, G20, and the Bretton Woods institutions). At the institutional level, this could lead to a “reinforced cooperation” among countries in the Euro area with positive political consequences of a general nature.

II. INTERNATIONAL ROLE AND SECURITY

6. ***Promote multilateralism and the role of the EU.*** Italy’s international role can only grow in tandem with the strengthening of the major multilateral organisations and the European Union. The recent return to a “nationalist” approach that tries to make up for the country’s weaknesses by seeking reinforcement through preferential alliances with external powers (such as the United States) should be rejected. It is in Italy’s interest to promote a common European policy in multilateral fora (OSCE, UN, IMF, World Bank, etc.) that reinforces the Union’s international profile and limits the nationalist tendencies emerging from within.
7. ***Re-balance Union enlargement.*** Enlargement has tipped the EU to the north and the east. It is strongly in our country’s interest to complete enlargement to the south-east and strengthen the neighbourhood policies with the Middle East and Africa. The political criteria for enlargement must be firmly maintained; the efforts to increase ties with areas of potential ethnic or nationalist conflict (such as the countries of the former Yugoslavia, Moldova, the Caucasus, etc.), must be accompanied by policies aimed at preventing these conflicts from being imported into the Union.
8. ***Increase security in the areas bordering the Union.*** Italy has an interest in maintaining a strong European Union commitment to stability and security in areas such as the Gulf, the Caspian Basin and Mediterranean Africa. These regions play a key role not only in the supply of energy but also in the fight against terrorism and organised crime, and control of illegal migratory flows; it is in Italy’s interest to promote the creation of a large extra-European area of cooperation and control that should be defined at the European level in order to harmonise it with common policies on security and the fight against crime.
9. ***Support and specialise Italian defence.*** Italy must avoid the risk of being declassified in the European defence and security area due to its difficult economic situation and the heavy cuts in the defence budget in the last five years. The Italian defence industry needs a European policy initiative designed to exploit niches of national excellence within a coherent framework of European integration. Italy should continue its process of military integration with a view to specialisation, abandoning technology areas where our partners can provide more mature products and obtaining in return the use of Italian products, where more valid, by other countries in the Union.

10. Integrate European security and defence. *The military instrument can no longer be considered as separate from other security or civilian instruments. This means doing away with the distinction at European level between commitments and expenditures "for defence" and "for security" and rethinking the European military instruments being created to ensure greater civilian/military integration. It is in Italy's interest to promote a holistic reconsideration and an advanced European debate on these issues in view of defining a new "model" that can no longer be only "for defence" but must be "for defence, security and peace-building".*

III. INSTITUTIONAL REFORM

11. Promote ratification of the Constitutional Treaty. *This is an essential prerequisite for enabling the governments to present definite positions that have been confirmed by parliament or the electorate. It is important to create a link between, and possibly coordinate actions among, the ratifying countries that today represent more than half of the population of the Union. By acting together in 2006, countries that have already ratified the treaty could effectively stimulate the two countries where the "no" vote prevailed, and that have not yet developed a strategy for recovering consensus among their citizens, as well as countries that have not yet voted or where the government has chosen to wait.*

12. Reinforce European democracy. *Relaunching institutional reform will require impetus from outside the inter-governmental arena, and this can be provided only by the European Parliament. First of all, the Parliament is the strongest expression of European democracy. In addition, the Commission has given up playing a driving role and there is no link among national parliaments, even those with a large majority in favour of reform. It will be important for the countries most favourable towards and interested in reforms, like Italy, to work to ensure that the initiatives coming from the European Parliament meet with support and are heard at the inter-governmental level. The new treaty could be submitted to the scrutiny of the electorate in a Europe-wide referendum involving all member states during the next European Parliament elections (2009).*

13. Encourage pragmatic progress. *The informal application of some of the provisions of the treaty should be encouraged. At the same time, constant attention should be paid to the impact of some of the changes, above all those that involve the institutional sphere, on the Union's overall constitutional arrangement.*

14. Support and become a part of the vanguard. *The creation and consolidation of "vanguard groups", both inside and outside of the EU can provide an important impetus not only to the integration process but also to the reform process itself. A core group of Euro countries could be particularly effective in playing this role.*

15. Ally with those who want to see Europe go forward. *It is in Italy's interest to avoid the formation of preferential axes or 'directories', and to support those who endeavour with the greatest energy to strengthen the European*

construction: common policies, a strong institutional framework, and a clear democratic basis. In following this line, Italy can continue to achieve important successes in European negotiations. Today it is likely that a convergence between Italy and Germany, which has proven advantageous in institutional matters many times in the past, could constitute the basis for relaunching the Union.

Scientific coordination by Raffaello Matarazzo

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1. ECONOMIC AND SOCIAL ISSUES

1.1 The European agenda

The main economic and social policy issues on the European agenda for the coming years can be grouped around two major themes: *i) economic stability and growth* and *ii) the Union's budget and policies*. Both have one dimension that touches on *ordinary administration* and one that involves *possible reforms* to European instruments and procedures. These issues are accompanied by another of an institutional nature: *iii) the performance of the Euro Group*.

With respect to **stability and growth**, it can be said that despite modest signs of recovery, the European economy still appears to be mired in the longest period of low growth in the post-war period. While the comparison with the United States often omits the fact that population growth "explains" roughly one point in the growth differential, one cannot but agree with a concerned diagnosis of the economic future of the EU and, in particular, the Euro area. Just as *stability* (of prices, exchanges, and public finances) was the dominant theme of the eighties and nineties, *growth* has become and will remain the dominant theme for the current decade.

Efforts to attain stability were based on the conviction – grounded both in economic theory and recent historical experience – that this was a fundamental prerequisite for maximising the economy's growth potential. The prolonged period of low growth we are experiencing indicates a weakness in growth potential and implies that the root problems are structural and cannot therefore be cured by expansive macroeconomic policies. In the medium- and long-term, it is equally clear that Europe must take the path of greater growth potential in order to ensure the sustainability of its social model and maintain macroeconomic stability, in particular the sustainability of public finances. In the short-term, the difficulties encountered in implementing the Stability Pact – in part as a result of low growth – will keep attention focused on the issue of stability.

The seriousness and duration of Europe's stagnation has meant that the impact on growth itself has tended to become the measuring stick for a range of issues that were examined from different angles in the past. **There are five principal groups of issues: the single market, the Lisbon Agenda, trade policy, the Stability and Growth Pact, and the social model.** These issues are deeply intertwined and in some cases represent boxes with different labels but the same content.

The single market. The completion and strengthening of the single market, in particular in the services, financial markets and *public utilities* sectors, will occupy significant space on the European agenda in the coming years. It is not yet clear how much the EU will want and be able to unify the market where it is still closed in separate national markets and how energetically it will defend the *acquis* of the Delors Commission's period of reform. Among the issues in question are adoption of new directives (e.g. on services), implementation of projects that have already been approved (e.g. the so-called 'Lamfalussy process' for financial integration), and enforcement of competition policy directly by the Commission or by Member States.

The Lisbon Agenda. This refers to the project for intensifying policies for structural reform of product and input markets. The Lisbon method – which means agreeing on a set of objectives that each country pledges to pursue with its own policies – has proven

ineffective so far. An effort is now underway to relaunch the Lisbon strategy by redirecting it towards growth and employment and by emphasizing national responsibility (*ownership*) for reforms. The responsibility of the EU is limited to those areas in which community intervention offers value-added with respect to national action (redirection of structural funds, reform of state subsidies, completion of the single market, competition policy, trans-European networks, etc.).

Trade policy. Globalisation is both a challenge and an opportunity for the European economy. On the one hand, it increases the pressure of American competition in the high-tech and financial services markets, of Asian competition in the manufacturing and textile sectors, and of competition from the South in the agricultural sector. On the other hand, the opening of markets provides new opportunities for development, above all in sectors with highest added-value. Trade issues arise both during normal relations (periodic disputes with the US, China, etc.) and in the major negotiations of the Doha Round.

The Stability and Growth Pact. Following the reform approved in the spring of 2005, the Pact faces the challenge of practical application. With the gradual adjustment of the French and German accounts, Italy has found itself in a more exposed position. At the same time, the new Pact can constitute an opportunity to reach greater coherence between budget discipline and growth stimulation only if – also as a result of the reform – there is genuine adherence to the new rules. If, on the contrary, a collusive approach prevails whereby the high-deficit countries cover each other and the increased complexity of the rules becomes an opportunity for evading them, then the credibility of the economic policy of the Monetary Union will be seriously undermined.

The European social agenda. A number of circumstances have brought the social question back into the European debate. Among them are the accusation of ‘ultra-liberalism’ launched against the Constitutional Treaty by some of the supporters of the “no” vote in the French referendum, the social malaise underlying the crisis in The Netherlands and the riots in the French suburbs, fear that the oft-invoked structural reforms will mean dismantling the welfare state, and competition from economies – such as those in Asia – where labour safeguards are minimal. Acceptance of the principle whereby the market and development fall primarily under the aegis of the Union, while solidarity and assistance correspond primarily to national governments, seems to be widespread. But “primarily” does not mean “exclusively,” and a Union apparently insensitive to social issues would not only not reflect the facts but would also risk being extremely unpopular. In the past, the special attention paid to the substance and the image of a European community attune to social issues led to the development of certain fundamental elements of the European social model: the social charter, fundamental labour rights, structural and cohesion funds, and the social dialogue method. For the policies discussed in the three preceding groups of issues (single market, the Lisbon Agenda, and trade policy) to move ahead effectively and enjoy the necessary level of acceptance in public opinion and political parties, new impetus and visibility has to be given to the role of the EU in safeguarding the shared body of institutions, practices and provisions that, despite differences between countries, can be called the European social model.

The second big issue concerns the **budget and community policies**. This should be the key moment in the debate on the possible active role of the Union in economic

policy, above all during a phase in which the priority is to provide new impetus for growth. In this light, the EU budget should be the community flywheel for the Lisbon strategy. Unfortunately, the recent negotiations were once again dominated by minimalist positions and by the focus on ‘what I give, I should receive’ (the so-called ‘fair return’), further accentuated by the controversy over the UK rebate. This is a prospect that strips the common budget of both its political significance and its economic purpose. No country, except in part Germany, has deviated from the logic of ‘fair return’, waiting for some other country to make the first move.

The recent negotiations on the budget were marked by a short-term perspective, dominated as they were by a highly restrictive approach to the overall scope of spending, polarisation over the size and mechanisms of reimbursement to the United Kingdom and an unwillingness to consider the European budget as an active instrument of common policies, in the economic field or beyond. A refusal to consider further reform of agricultural policies, following the one undertaken during the Prodi Commission, was also predominant. This attitude of closure is also the reason why *other community policies* envisioned in the Treaty (research, but also energy and transportation) have never received adequate resources for implementation.

Over the next five years, it is likely – and to be hoped for – that the issue of the Union’s budget be tabled once again, above and beyond the current arrangements established by the 2007-2013 Financial Perspectives. The Union budget is not meant to be responsible for either cyclical stabilisation policy or social policy; both of these belong to the national sphere, and here one can only hope for greater coordination and affinity. But the Union budget could be entrusted with powers of allocation for development. In addition to regional policy, already underway, interventions for industrial policy could be envisaged as could the allocation of resources to turn policies like defence and security into common policies.

These objectives do not require a large budget, like that of a mature federal state. In the European model, Union resources are tied to an efficient use of regulatory powers; in addition, co-financing models make it possible, even with limited resources, to exercise an effective leverage on other types of projects, both public and private.

A Union budget in the order of 1.5-2% of Product may be sufficient in the immediate term; it should not be difficult to find this amount of own fiscal resources clearly tagged as to the content and the benefits expected of a programme of spending for Union development and construction. There are taxation areas where the principle of subsidiarity could apply (where raising fiscal revenues could be done more efficiently at the community level) and areas where the applicable principle could be the attribution of a “dividend” on the benefits obtained through the policies implemented. The idea of an EU tax, discussed many times in the past, could be brought forward in a new context and linked to the active role that the Union could be given in economic policy.

An important institutional issue is the **performance of the Euro Group** and potential new initiatives to strengthen it. The Euro Group is the key place for political negotiations and preparatory work for Ecofin decisions in matters such as coordination of economic policies and governance of the Stability Pact. It is also a potential place in which to work out and launch new initiatives. One matter that has been discussed periodically for years and on which an initiative could be undertaken concerns the external representation of the Euro.

1.2 Alternatives and positions within the Union

For a number of reasons, it is particularly difficult at the moment to identify the positions of important governments on the issues briefly summarised above. Above all, it is likely that the position of France, the key country for major European developments, will remain unclear for some time. This is due to the upcoming presidential elections in 2007 and the still uncertain response – in terms of economic and European policy – to the "no" vote in the referendum and the riots in the suburbs. Second, as revealed in the management of its semestre presidency, the “British alternative” to the traditional Franco-German axis does not present a credible option, given the UK's lack of participation in the “heart” of the EU (the Euro), but also the progressive decline of Blairism on the domestic and international scene. The sluggishness with which Great Britain managed its presidency and in particular the line it followed on the community budget may also have undermined the sway Great Britain appeared to exercise for some time over some of the new Union members. Third, these new members are themselves an element of uncertainty as they are still undergoing a kind of apprenticeship in the European game. Finally, and more generally, the methodology that will characterise European negotiations in a Union of twenty-five (informal consultations, management of procedures, exercise of leadership and alliances among countries with common interests) is still being defined.

It is for these reasons that only broad-stroke hypotheses can be formulated about the scenario in which Italy will find itself.

In the short term, the most plausible scenario is the **continuation** of the current phase of **uncertainty and lack of major initiatives**. This could last for a few years, until after the French elections and the first test of the French presidency. Contributing factors include not only political uncertainty in France, but also the weakness of the economy and the fact that each country is primarily engaged in national policies, both to attempt structural reforms to increase growth capacity and to respect budget discipline.

The most plausible, and not necessarily incompatible, scenarios for ending this phase can be summarised as follows:

- **An attempt to renew the Franco-German partnership.** The above uncertainties notwithstanding, at some point France and Germany may attempt to recover their *leadership* of the Union. It is difficult to imagine this occurring before the presidential elections in France. It is also difficult to predict whether the attempt will be primarily a defensive move or an effort to relaunch. The Merkel government's first European steps would seem to indicate that Berlin may take on a stronger role than Paris. It is likely that some initiatives will come from the countries in the Euro area through a strengthening of the Euro Group.
- **Continuation of the minimalism-activism conflict.** The conflict between the minimalist and activist positions concerning the role of the Union in economic policy will continue to mark the Union. The conflict has two aspects. The first sets economic policies based exclusively on spontaneous market forces against policies that give public authorities a role of stimulus. The second is between those for and against reinforcement of Europe's role in economic policy, for example in public investment, research and energy. For several years, Great Britain has exercised the most effective *leadership* of all European countries in

both aspects of the minimalist approach. Today, however, the weakening of Prime Minister Blair on the domestic scene, along with the flagging economic *performance* of the United Kingdom, are beginning to undermine the predominance of the minimalist approach. The question for the coming years is whether the supporters of reinforcement of the European construct will reassume a position of *leadership*. A *sine qua non* precondition for this will be the popular perception of high quality economic proposals for jump-starting growth. Over the last decade, countries traditionally most in favour of European integration (continental and Mediterranean) have not been able to offer a convincing economic policy model, while the countries favouring the minimalist approach (Anglo-Saxon and Nordic) have had an easy time arguing the superiority of their economic and social system.

- **Increasing competition among countries.** By now, the major chapters on cooperation have been written and constitute an institutional framework in which economic dynamics were largely entrusted to competition, not only between businesses but also between the different nations' economic and social policies. This type of competition should be considered an element of strength, not weakness, of the European construction. In this phase, the primary task of the Union is to consolidate its economic constitution: complete the single market, implement a serious competition policy, rigorously apply the new Stability Pact, guarantee genuine competition rather than "economic war" or "collusion to avoid competition". The Lisbon Agenda should remain a form of soft coordination based on the definition of reference models, emulation and the exchange of information on best practices.

It is impossible to predict the course of events within this general framework. The ability and determination with which each country, including Italy, formulates its own European policy will perhaps be the decisive factor.

It is likely that a **decantation phase** will precede any major initiatives. In the past, highly innovative steps like the single market or the monetary union were preceded by actions aimed at clearing the table of old conflicts that had paralysed the European Council's capacity to adopt initiatives. Looking to the future, relaunching the coordination of economic policies by strengthening the role of the Euro Group could start a new phase consolidating the major advances of the past years. This could be achieved through specific initiatives, not necessarily of high political visibility but significant from an operational point of view (for example, a common agency for public debt and the synchronisation of budget calendars).

1.3 Italian constraints and interests

Today, Italy is the country with the worst performance in terms of growth, as it was in terms of stability over the twenty years that led up to the adoption of the Euro. But while nobody at that time blamed our deviation on Europe, today some insistent voices attribute low growth to the European straitjacket: the Euro, the Stability Pact, trade openness.

These voices must be countered with acknowledgement of the fact that the history of Italy's participation in the EEC (and then the EU) is fundamentally a **history of**

economic successes. Through participation in Europe, Italy received the decisive impetus needed to overcome its lagging development through exports, to modernise its apparatus for economic governance, to restore monetary stability and balance public finances. During the fifties and sixties, Italy was in the forefront for growth and stability, and the macroeconomic stabilisation of the nineties (inflation and high deficit), which allowed for adoption of the Euro, was exemplary.

It should also be remembered that **difficulties in participating** in Europe and discouraging voices coming from within the country are not new to Italy: just think of the many clauses deferring application of community directives, the debated entrance into the ERM and the wide band with which it entered, the delay in entry into the Schengen area, and so forth.

Therefore, a broad consensus on the strategic significance of Italy's participation in the economic and monetary Union must be re-established. The consensus should be based on **two key arguments** that are difficult to ignore:

- a) the challenge posed by globalisation and the emerging new economies is inescapable and would be even more difficult, not easier, to meet without full insertion in the European framework;
- b) Italy has the resources required to meet the challenge.

Since the early nineties, Italy's *growth* has been inferior to that of the rest of the Euro area and the difference has continued to increase. In particular, the failure to renew the structure of its productive apparatus, the weakness of its financial system, and inadequate discipline in production costs have caused a progressive *loss of competitiveness* on the global market. An exceptional effort is required at the national policy level to make the Italian economy dynamic and competitive once again.

At the same time, it is difficult to imagine a relaunching of the Italian economy that is not anchored in a strategy for community growth. Here, definition of a *bi-partisan* base seems to be an essential prerequisite for maintaining credibility and negotiating power in Brussels. Of course, it is normal and useful to express the various elements of different positions and to compare and assess different approaches within this common framework.

In light of the preceding analysis, the following would seem to be the pillars of a shared approach:

- ***Participation in the Euro.*** Recent governmental statements critical of Italy's participation in the monetary union and ministerial proposals for withdrawing from the Euro have shaken the markets and financial analysts. A major international bank suggested that such a possibility should not be excluded. These statements are mere 'words in the wind'; in reality no government would have the will and determination to take such a decision and would immediately face ruinous political and financial consequences if it did. But it is not simply a matter of stopping this kind of talk; what is needed above all is a greater awareness of the choices the Italian economy and economic policy will have to make to adapt its development model to the competition of the single market and the globalised economy.

- **Budget discipline.** High public debt and the objective fragility of public finances require a structural correction that can only be implemented over a timespan of more than one legislature. Without a European anchor, this effort would be even more arduous. The pressure from financial markets, anaesthetised by participation in the Euro, would reemerge with devastating effects. With the highest public debt in Europe, well above the 100% of GDP threshold, and with an unfavourable demographic profile, fiscal prudence will remain an inescapable duty of Italian economic policy for many years to come. It is in this field that community rules have helped Italy the most over the past decade and will be of greatest service in the future. During the debate over reform of the Stability Pact in the last few months, in which a slackening of the rules loomed large, Italy was immediately identified as the weak link by the markets and *rating* agencies. Rigorous application of the reformed Pact, including the part that envisions greater emphasis on public debt stock rather than on budget deficit, is an obligatory choice for any future government coalition; in this sense, this is a *bi-partisan* element of economic policy. Economic and social policy choices concerning the size and structure of revenue and spending can and should be *partisan*.
- **Completion of the single market.** The Italian economy has more to gain than other Union economies from the completion of the single market in the services and *utilities* sectors, precisely because it still has a longer way to go to reach the threshold of efficiency. At the same time, the protected sectors that would be exposed to foreign competition by market opening constitute well-organized interests capable of influencing government choices. In final analysis, economic policy must choose between the interests of the producers and those of the user-consumers. Past experience in Italy and other countries suggest that these opposing interests divide both the left and the right. *Bi-partisan* support for completion of the single market would also put the seal of approval on the market economy as the essential framework for credible strategies for prosperity and development.
- **Development of the community budget.** Because it is less conditioned by predefined positions, Italy is in a better position to put forward a proposal to do away progressively with the logic of “fair return”. The goal is to make the budget a key instrument for relaunching a European growth strategy, as recently proposed by the Sapir Report.
- **Euro Group.** Italy has an interest in strengthening the role of the Euro Group both internally (greater coordination of economic policies in the Euro area) and internationally (adequate representation of the Euro area, ultimately with a “single voice”, in the G7 finance, G20, and the Bretton Woods institutions). At the institutional level, this could lead to a "reinforced cooperation" among countries in the Euro area, which could have more general positive political consequences.

2. INTERNATIONAL STATUS AND SECURITY

2.1 The European agenda

The European Union is a prime international actor: a protagonist in global trade negotiations, an autonomous monetary actor, a party to negotiations such as the Road Map and nuclear non-proliferation with Iran as well as present both politically and militarily in many crisis zones. Although it does not have a seat on the Security Council (where there is only weak consultation among EU countries), it has established important operational ties with the UN.

Enlargement of the Union's borders has been the most powerful expression of the Union's strong force of attraction. In only a few years, the EU enlarged to include all of the former communist European countries, including three former Soviet Republics (Estonia, Latvia and Lithuania). The states born of the dissolution of Yugoslavia, with some difficulties and delay, have also started down this road. This rapid enlargement has brought to light some problems with respect to institutions and efficiency, but it has also been an enormous success in terms of international politics because it allowed for the transition from communism and planned economies to democracy and the market in a framework of stability and security.

Enlargement has strengthened the Union's international image and role, increasing its influence and strengthening its status in areas beyond Europe. Enlargement has however also posed several problems. The first and perhaps most important of these is that **no one knows when and where this process should end**. To date, the Union (which has recently opened accession negotiations with Turkey) has avoided defining what its final borders will be. In fact, it is believed that to do so would lead to a loss of credibility and efficacy in its policies for stabilisation and promotion of democracy in critical areas, such as the former Soviet republics, and would generally weaken the EU's force of attraction. The Union has therefore held itself to the letter of the Treaty that leaves the door open to all "European" countries that respect democratic principles and the rule of law, taking care not to define what is meant by "European". This does not pertain so much to Turkey (which has already been implicitly accepted as "European" from this point of view) as to Russia (which extends to Vladivostok), the other former Soviet states in the Caucasus and Central Asia that are already part of the Council of Europe and the OSCE, Israel, and perhaps even others. The EU is both a positive factor for development and stability and a magmatic reality whose limits are as yet undefined and whose expansion may be difficult to contain. It is therefore seen as both an opportunity and a threat.

The EU's international reach goes well beyond enlargement. From its first years, the Union established a preferential relationship with *African nations* that has, in different ways and forms, been consolidated and deepened, not only in the economic arena, but also in the political and security areas. Ten or so years ago, the Union attempted to formalise its various forms of dialogue and cooperation in the *Mediterranean* area by institutionalising a framework for multilateral relations with all of the countries in the area. More recently, it launched the European *Neighbourhood* Policy, which has more operational flexibility and targets all countries that, at least for now, are not in line to receive an offer of full accession. Other initiatives, such as the dialogue with the *Gulf* Cooperation Council, also fit into this framework. Bilateral and

multilateral agreements on the management of migratory flows, border controls (which enjoy significant financing from the EU), and the fight against organised crime and terrorism increase the importance of a wide and complex network of international relations centred in the EU.

The Union has **inadequate institutional instruments** for facing the implications of the enlargement of its borders and its international reach. Failure to ratify the Constitutional Treaty has had particularly damaging effects because it has prevented the creation of a European Foreign Minister (who would also have been the Vice-president of the Commission), thereby eliminating the possibility of conducting truly common policies (given that the decision-making centres, responsibilities for the budget, the procedures, etc., remain different and autonomous). Internal conflicts between the policies and agencies under the Council and those under the Commission are looming over competencies and the budget, to the detriment of unity and coherence. This is particularly damaging with respect to issues such as crisis management, *state-building* and security and defence.

The efficacy of pre-accession, neighbourhood and crisis management policies is limited by a **lack of adequate resources**. The conflict between internal and external priorities will increase unless there is reform and a budget increase. It is likely that relations with the European former Soviet republics will tend to be more favourable than those with countries in the Mediterranean area. This difference could become increasingly decisive as the Union takes on, as appears likely, more commitments on its eastern borders. This could create significant disagreement over the destination of available resources.

There has been progress in the area of European Security and Defence Policy (ESPD) despite the stalling of the Constitutional Treaty. The *European Defence Agency* has been established. Lacking a strong political reference point (like a president of the Union or European Foreign Minister) and adequate financial resources, however, the Agency is obliged to engage in a sort of permanent guerrilla war with Member States and the Commission. Efforts to follow the path outlined in the ECAP (*European Capabilities Action Plan*), including the establishment of *European Combat Groups*, are expected to be completed by 2007. The *European Military Police Force* has been created and both the *European Military Committee* and the *Military Staff* are now operational. Accords have been reached between the EU and NATO for future European use of Shape (NATO's Supreme Headquarters Allied Powers Europe) capabilities. Despite this important progress, however, still lacking are **a coherent and integrated** European Grand Strategy, as well as certainty about the lines of political command of the various missions.

The **defence industry** has made an effort to rationalise in recent years with the creation of *EADS* in the aerospace sector as a sum of parts of the French and German industries, and the birth of *MBDA*, which pools the resources of the principal European missile producers. This has been a '*bottom-up*' process with initiatives coming from the entrepreneurial level and political approval arriving *ex-post*. What is lacking is an overall framework that evaluates and combines diverse capacities and optimises resource use; if it is true that, overall, Union countries invest less than half what the US does in military research and supply, it is equally true that the efficiency of this

spending is undermined by the almost total lack of coordination, with resources dispersed in countless directions and much duplication.

Research on **advanced technologies for defence and security** is particularly important and requires a rational and effective European industrial policy. A few timid steps have been taken, thanks above all to the establishment of the above-mentioned European Defence Agency, but for the time being the issue remains firmly in the hands of individual national agendas.

2.2 Alternatives and positions within the Union

The majority of Union Member States recognise the need to proceed with a **strengthening of the common foreign and security policy (CFSP) and the European security and defence policy (ESDP)**. The prospect of further enlargement in the short and long term, the launch of the new Neighbourhood Policy, and the EU's increasing commitment in crisis management situations (the Balkans, Darfur, Aceh, Rafah, etc.) as well as the need to face difficult cases such as Moldova, China, Iran and others still, merely compound the demand for a more active European presence already felt for the UN and the OSCE.

In the new global scenario, internal and international security governance (military, but also political, juridical, economic, environmental, etc.) requires a multiplicity of instruments and policies that must be managed in a coherent fashion. Various competencies already exist in the community sphere, but are not always applied effectively with a common vision. There is a growing need for a **European Grand Strategy** based on the strategic document approved at the Thessaloniki European Council to unify “communitarian” and “inter-governmental” competencies and capacities and to ensure effective integration among the various “pillars” of the “communitarian” reality. A document is needed to define the strategic objectives to be pursued, indicate the time-frame and geographical scope, and specify the type of missions to undertake beyond the Petersburg declaration. A logical course of action must be adopted that leads on the one hand to a definition of the necessary military resources, and on the other to the identification of the modalities and mechanisms of reciprocal support between ‘*hard power*’ and ‘*soft power*’ instruments. Growing commitments in Africa, the Middle East, the Balkans, the Caucasus, and Central Asia, in non-proliferation, the fight against terrorism and organised crime, as well as interventions in countries in crisis, etc., cannot be taken on without more effective ways and means and without being able to manage the global consequences of these commitments.

Enlargement constitutes an important part of the common strategy for the Union’s international status. A part of public opinion seems to be opposed to further enlargement even though this does not appear to be motivated by a desire to strengthen (*deepen*) common institutions. On the contrary, the hostility to further enlargement seems to be accompanied by hostility to or at the very least a lack of trust in the Union, its cost and its policies. Unfortunately, the last “great enlargement” achieved before ratification of the Constitutional Treaty (which may never enter into force) started, severed the **connection between enlargement and deepening**, thereby upsetting the EU's political-institutional equilibrium.

This makes it more difficult to oppose further enlargement for purely institutional reasons or to protect the internal coherence of the Union, but it makes it all the more urgent to find a solution to other political problems, such as the **definition of a common foreign policy** with bordering nations, and above all Russia. The basic lack of European consensus on EU relations with *Russia*, despite the growing doubts raised by Putin's actions, is an element of weakness. It is also a potential security risk factor given that country's significant military capabilities. Enlargement to *Turkey* also raises important problems for foreign and security policy in terms of relations with the Caucasus, the Middle East and Central Asia. Enlargement should imply a greater European commitment in these areas.

The need to define these policies has been recognized but not yet implemented. The **Constitutional Treaty** envisions a broad array of possible commitments, ranging from terrorist attacks to natural disasters (in both cases a specific solidarity clause among Member States is included), that broadens the so-called "Petersburg missions" to include, among others, disarmament, military assistance, post-conflict stabilisation operations and the fight against terrorism. It would introduce forms of operational flexibility (formally excluded from the Treaty of Nice, currently in force), such as tasking a group of Member States with European missions, creating permanent structures for reinforced cooperation among certain countries on the basis of precise commitments and criteria, closer forms of bilateral and multilateral military cooperation, some budget forecasts, etc. In effect, all of this would only regulate and include in the community framework formulas that have already been tested externally.

The absence of the new normative framework envisaged by the Constitutional Treaty has fuelled speculation about possible **alternative models for managing CFSP and ESDP**. A certain number of countries (including many recent Union members) advocate formal respect for the Treaty of Nice, by which nothing can be done in the ESDP area without unanimous consent of all Member States. Others, and in particular the two major European military powers (France and the United Kingdom), with the frequent support of Germany, argue for a sort of "*directoire*" of the biggest countries, without which it would in any case be difficult to commit to any security and defence endeavour. A more nuanced and politically acceptable option than a directory is establishing (in keeping with the Constitutional Treaty) a nucleus of reinforced cooperation among countries that are "*willing and able*": those that have both the political will and the means to make a significant commitment. Other ideas focus on activating CFSP and ESDP through groupings such as the Euro Group or the Schengen countries.

The **future of transatlantic relations** constitutes another central issue that is intertwined with the above-mentioned institutional debate. There are clear differences between European and American positions in terms of interests and perceptions that call upon Europe to focus its attention and take responsibility. The US decision to attack and occupy Iraq provoked serious divisions within the EU and accentuated the difference in views on what role the United States should be given in Europe. This view usually corresponds to the importance the different countries attribute to their bilateral relations with Washington, seen as the ultimate guarantor of their security, political ally, counterweight to other Union Member States, etc. The highly ideological tone, striking interventionism and marked unilateralism brandished by the Bush administration have aggravated European divisions.

It is unlikely and undesirable for Europe to unite around an anti-American position or one of major conflict with the US. At the same time, the position traditionally held by Italy that, with possible minor exceptions, what is good for the US is good for Europe and vice versa, also increasingly lacks credibility. The end of the Cold War significantly eased the military threat to the world and to Europe that cemented transatlantic solidarity. Today Europe is no longer the essential ally of the United States, and the United States is no longer the necessary protector and guarantor of European security.

Nevertheless, there are broadly shared analyses on both sides of the Atlantic about the **new set of threats and risks**, though it lacks the same aggregating force as in the past. The fight against international terrorism and organised crime, countering the proliferation of weapons of mass destruction, management of the serious problems posed by “failed” states (ranging from kleptocracies to areas lacking acceptable levels of governability or those falling apart), defence of human rights, control and reduction of mass migration and illegal immigration are at the top of the agenda of all major industrialised nations and form the basis for a broad and significant “shared view” both at the transatlantic and global level. Moving from this analytical level at which problems are identified to the practical level at which agreements are reached on the priorities for intervention and the strategies to be adopted has proven far more difficult.

In Europe, the fight (not “war”) against **terrorism** and **organised crime** and the issues of **mass migration** and illegal immigration are predominant problems. Growing attention is being turned to the *control of common borders* (in particular those of the Schengen area) with a specialised Agency established to this end. Cooperation on *home affairs, justice, police and intelligence* has been reinforced. The EU also operates internationally in these fields, with multilateral and bilateral agreements, as well as financial and technical cooperation designed to establish a wide area of control over areas beyond the Union and for joint response to crises. Significant political differences between Member States remain, however, and these are further complicated by the fact that the relevant competencies are held at the national decision-making level. This is particularly evident in judicial matters, but differences also pose significant obstacles in the field of intelligence cooperation, despite the new figure of a European coordinator.

It is essential that the political leadership take up its prerogative to define **defence industrial and technology policy** to prevent industrial leaders from taking a kind of vicarious action. Steps in this direction would lower the barrier between the Council and the Commission, which should definitively abandon the now purely virtual distinction between research for civilian and for military uses. This would also encourage businesses to undertake genuine rationalisation and would contribute to resolving the old questions about intellectual property rights and a single defence market, which continues to be precarious, if not impossible, due to the use and abuse of Art. 296 of the treaty (which makes it possible to get around internal market rules for means and services relating to national security). Decisive impetus is required. So far the European Defence Agency has not gone beyond a voluntary non-binding ‘Code of Conduct’ that some countries have already rejected.

There appears to be a tendency to develop *à la carte integration* forms among **variable groups of countries**, more or less directly tied to the common institutional setting. In the absence of strong guidance from the Council and/or the Commission (made more difficult by the continued existence of the rules established by the Nice

Treaty), the inclination of the largest countries to exercise *leadership* finds expression in the formal or informal creation of **directoriums** that are presented as restricted mechanisms for prior consultation. This does not resolve the problems of consensus within the Union, nor does it guarantee strategic coherence in the many European initiatives because the veto right remains and the large countries are in turn divided amongst themselves. Hence the risk of paralysis in Europe's international initiatives. If ways were found to make these mechanisms work, however, the EU could act with notable efficiency and serve as a multiplier of national capabilities.

2.3 Italian constraints and interests

Italy has asserted its international role in parallel with the strengthening of the major multilateral organisations and the alliances in which Italy is a member. At the same time, the more strictly bilateral aspect of Italy's foreign policy has certainly played a significant role, for example in the opening up of trade with the USSR or in its autonomous energy policy conducted through ENI. But it has never taken on the characteristics or the importance of great power policies due, perhaps, to the insufficient dimensions and capacity of a country that has neither the resources nor the ambition to compete with the major powers. On the contrary, Italy's greatest successes have been achieved when it was able to influence important multilateral choices in a decisive manner (for example, the European declaration of Venice on the Middle East in 1980 or the decision to proceed with the deployment of Euromissiles in the same period). Italy's most important international profile in the field of crisis management and security has generally been achieved within well-defined multilateral frameworks.

This reflects a realistic view of the interests and capacities of a medium-sized European power that has the dubious honour of being the smallest of the "big" and the biggest of the "small". Italy had to struggle for a long time to overcome such strong initial handicaps as its status as a "defeated nation" (which excluded it for many years from the United Nations) or its nature as both a European and a Mediterranean nation, industrialised but still developing, characterised by the presence of the strongest Communist Party in Western Europe.

Its "**long march**" **within the multilateral institutions** has certainly met with success in terms of increasing the country's international role and status and affording it a position of respect within the major international decision-making bodies, so much so as to create opposition. Today the greatest risk, linked to the globalisation of international politics and the emergence on the scene of many other large countries, comes from the attempt to redefine the role of "medium" or "borderline" powers – like Italy – to make room for new actors such as China, India, Brazil and others. A creeping process of "re-nationalisation" of international politics, exemplified by the new American unilateralism or the rediscovery of a national dimension in German politics, makes this risk even greater.

Most of Italy's politicians realise that Italy has no hope of competing successfully on this "nationalist" scale and that its chances lie instead in the relaunching and improved efficiency of multilateral organisations and, in the final analysis, in the progressive assertion of a solid governance *of globalisation*.

Yet there has been a return to nationalist discourse in Italian society as well, which appears to take past successes for granted and sees them as capital to spend in asserting greater independence from the very multilateral organisations in which those successes were achieved. This tendency is also influenced by the process of globalisation of international politics, but it is far more sceptical about (if not opposed to) the role of international institutions and multilateral alliances. Those who subscribe to this analysis apparently do not lay any weight on a model of system governance different from that which may be temporarily achieved through **power politics**. Indeed, this “nationalist” tendency takes into account the country’s weaknesses and deficiencies by looking for assurances and reinforcements from an external power (preferably the United States).

It may be difficult to reconcile the direction and choices of these two different tendencies in Italian politics. However, it is certainly possible to conceive of points of convergence for those who intend to pursue, albeit with differing emphasis and tone, the traditional route of multilateral engagement. Here we limit ourselves to indicating a few of the major guidelines for those who fall into this category.

- ***Promote multilateralism and the EU.*** Italy’s international role can only grow in tandem with a strengthening of the major multilateral organisations and the European Union. Nationalist tendencies among European powers that could weaken the EU and isolate Italy should be opposed and the recent return to a “nationalist” approach that tries to make up for the country’s weaknesses by seeking reinforcement from preferential alliances with external powers (preferably the United States) should be rejected. It is in Italy’s interest to promote a common European policy in multilateral fora (OSCE, UN, IMF, World Bank, etc.) that reinforces the Union’s international profile. The bitter debate about Security Council reform has opened wounds that should be healed by relaunching the idea of the so-called “European seat” (which could take different forms), or at the very least the need for a greater and more cogent coordination of ESDP in multilateral fora.
- ***Re-balancing Union enlargement.*** Enlargement has tipped the EU towards the north and the east. The political direction emerging in France, Germany, The Netherlands, etc., could block important future enlargement in the Balkans (with the possible exceptions of Bulgaria and Rumania) and Turkey. This would weaken the position of southern European countries and could fuel a political dynamic of confrontation between North-South, Christianity-Islam, Europe-Mediterranean and Middle East that would be very dangerous for the EU and for Italy in particular. It is therefore of significant interest to our country that enlargement to the south-east be completed and that neighbourhood policies towards the Middle East and Africa be strengthened. Here it is essential that political criteria for enlargement be strictly enforced. As enlargement moves towards areas of potential ethnic or nationalist conflict (such as the countries of the former Yugoslavia, Moldova, the Caucasus, etc.), it is paramount to stop the logic of conflict from being imported into the Union. The formation of sub-regional coalitions or preferential axes should be avoided, as these could not only harm Italy but are also incompatible with the harmonious development of the European integration project and weaken its security.

- ***Increase security in areas bordering the Union.*** Italy has an interest in maintaining a strong European Union commitment to stability and security in areas such as the Gulf, the Caspian basin and Mediterranean Africa. These regions play a key role not only in the supply of *energy* but also in the fight against *terrorism*, organised *crime* and illegal *migratory flows*. It is therefore desirable that our foreign policy seek to promote the creation of a large area of cooperation and control in the regions surrounding the Union. This cooperation should be determined at the European level in order to harmonise it with common policies on security and the fight against crime. As concerns *energy* supply in particular, security can no longer be based on preferential bilateral accords but must be based instead on the maintenance of stability and security in transport and extraction areas. An increased Union commitment in these areas and with respect to Russia should be encouraged despite the difficulties posed by the Iraqi and Iranian crises and the uncertain developments in the Russian regime. These are also the regions where the fight against terrorism and organised crime, and efforts to improve control of illegal migratory flows are being played out. It is difficult to negotiate on the basis of bilateral accords in these areas, as they risk being negatively perceived by the other party and may create dangerous differences between EU countries. There is therefore a strong interest in moving these negotiations to the European level in order to define a reference framework and guidelines for additional bilateral instruments and to harmonise them with common policies on security and the fight against crime.
- ***Support and specialise Italian defence.*** Italy must avoid a diminution of its influence in the European defence and security field brought about by the heavy cuts in the defence budget, in order to maintain a significant role in Europe. At the moment we enjoy a “residual advantage” that permits us to remain in the most important groupings (Occar, LoI, Mic etc.). However, the likelihood of greater cooperation among the larger European countries following a “Saint Malo logic” will have immediate financial consequences and will accentuate the gap between commitments that have been undertaken and real national capacities to meet them: thus the risk of decline for Italy. One response could be to make the best of a bad situation, to give greater political priority and a greater budget share to the defence sector, or to make selective decisions about present and future commitments based on a clearer and more coherent industrial and technology strategy. The worst scenario would be constant oscillation between different options resulting in the lack of any strategic choice. National decisions must in any event be accompanied by **consistent behaviour in the European arena** in order to reinforce their impact and limit the negative consequences. In a country like Italy that is not used to debating these issues, this could inevitably lead to certain divisions and to different positions in the majority and the opposition. The Italian defence industry has a notable capacity but it must resolve the strategic dilemmas posed by the thorny dialogue with the French and Germans, the effort to establish a base in Great Britain (Finmeccanica has over 10,000 employees in the United Kingdom), and its long collaboration with US industry, which has been very positive in terms of employment but less so in terms of technology. The inability of the internal market to ensure competitive production levels makes

it essential to adopt a European political initiative designed to exploit the **niches of national excellence** in a coherent framework of European integration. Thus far, the emphasis has been on large multinational programmes that have produced valid products, but with unacceptable costs and time-frames. It would be preferable to pursue an integration process with a **view to specialisation**. This would imply abandoning areas of technology where our partners can provide more mature products and obtaining in return the use of Italian products, when more valid, by other Union countries. No more compartmentalisation and fragmentation of individual programmes, but rather a competition policy accompanied by public choices to avoid duplication.

- ***Integrate European security and defence.*** It is no longer possible to view the military instrument as separate from other civilian and security instruments. Experience from all the missions undertaken over the past twenty years has revealed both the inadequacy of a solely humanitarian or “observation” approach and the impossibility of resolving a crisis solely by military means. The Armed forces have had to adapt themselves to security and state-building tasks, and have developed increasing and important ties to civilian intervention structures. It does not even seem possible to separate, strategically and operationally, the two phases of “war-winning” and “peace-building” in order to provide specially trained forces for each phase because, in reality, they form a political and operational continuum. Such a distinction would not only create irresolvable “threshold” problems (When do you go from the first to the second phase? What are the respective responsibilities of the two operational instruments? etc.), but would also increase the risk of contradictions and confusion within the mission. In practice, this means **doing away with the current distinction between commitments and spending “for defence” and “for security”** and rethinking European military instruments in terms of greater civilian/military integration. This contrasts with the current situation in which the Commission, which does not have competence in defence matters, adopts political, industrial, and research and development programmes in the area of security on the condition that these remain totally separate from defence programmes. This distinction leads to useless and costly duplication and is clearly in contradiction with real needs. Needed **technological renewal** of military instruments should be addressed on a European scale. Even putting aside Italy’s specific deficiencies, no European country has sufficient national resources to develop and autonomously acquire the needed technologies. The European Defence Agency should play a coordinating role, but it is unlikely that it can do so without acceptance of greater European interdependence and without stabilisation of the Union’s institutional framework. A corollary that cannot be ignored is the **transatlantic relationship**. NATO has recently established the High Command for the transformation of alliance military instruments; the need for greater coordination between the Agency and the Command is evident. It will be important, however, to keep this transformation from leading to acritical implementation in Europe of American organisational, operational and technological models, both to safeguard autonomous European industrial and technological capacities and because the American model does not appear to be particularly effective. In the critical field of civilian/military

integration and the relationship between defence and security, the European approach pursued to date, though fragmented, appears to be more effective. Proceeding along the lines described here means insisting on the need for a comprehensive reassessment and an advanced European debate in view of drawing up **a new model** that can no longer be just “for defence”, but must be “for defence, security and peace-building”.

3. INSTITUTIONAL REFORM

3.1 European agenda

The French and Dutch “nos” to the Constitutional Treaty have created a situation of great uncertainty about the future of institutional reform in the EU. This uncertainty has in turn had a negative impact on deliberations on economic and social policies, the EU’s international role, and issues related to internal and external security. It also risks reinforcing the sense of distrust and distance vis-à-vis European institutions that underlay – along with purely internal factors that should not be ignored – the French and Dutch no votes.

The **ratification process** has been halted for the moment. The “pause for reflection” agreed upon at the European Council of June 2005 has not so far given way to any debate among Member States about possible ways out of the impasse. Diplomatic discussions are still where they were six months ago, although they are expected to be revived under the Austrian presidency.

After the two referenda, governments have adopted different approaches to the ratification process in their respective countries: some have completed it while others have chosen to suspend it. To date, the treaty has been ratified by 13 out of 25 countries, which together represent over half of the Union’s population.

Institutional actors have thus far given little impetus to a relaunch. The British presidency carefully avoided the subject. Similarly, the European Commission has chosen to concentrate on other issues deemed to have a more immediate impact on European citizens. The Commission is trying simultaneously to improve the Union’s public image through the so-called Plan D in preparation for renewed national debates on the future of reform. To this end, a European conference on the future of the Union is expected in May. Only the European Parliament has shown some initiative: in the Fall it began to debate strategies for ending the impasse on the basis of an articulated resolution project.

At the same time, **occasional initiatives** demonstrate that the problem of the inadequacy of the Union’s institutional instruments has not vanished nor is being ignored. Albeit in a rather disorderly fashion, attempts are being made to address the problem in the absence of the Constitutional Treaty. Four trends are worth noting.

In the first place, **informal application of some of the Treaty's provisions** has continued. In the area of foreign and security policy, for example, work continues, albeit cautiously, towards the creation of the *External Action Service* and the *Defence Agency* was established in July 2004. Furthermore, the solidarity clause against terrorism and natural disasters has been approved. The decision to set up a stable presidency for the Euro Group is also significant.

Second, efforts have been intensified to **create *ad hoc* institutional instruments**, beyond those envisioned in the Constitutional Treaty, capable of implementing increasingly important Union policies more effectively. For example, in the area of justice and home affairs a *Counter-Terrorism Coordinator* has been appointed and an *Agency for External Borders* has been created. In the defence field, an institutional apparatus is being progressively developed to give the Union an increased autonomous capacity for planning and command of military operations.

Third, the tendency to **form restricted groups** of countries with a view to promoting greater cooperation in certain sectors has been reinforced. This confirms the need for greater flexibility in integration projects and creates the conditions for these projects to develop without the participation of all Member States. While the mechanism for reinforced cooperation has not yet been utilised – the EU treaty in force imposes rules that are too rigid – there is a growing tendency to promote closer cooperation in certain political sectors, such as management of migratory flows and defence, among countries that periodically decide on how to proceed. This phenomenon should be seen as both a reaction to the vacuum created by the failure to ratify the Constitutional Treaty and a sign that the dynamism of European cooperation continues to seek a way forward.

Lastly, the problem of how to **reconcile enlargement and the Union's institutions has been given growing emphasis**. Indeed, the need to adapt the Union's political and institutional instruments in order to be able to continue the process of enlargement is increasingly being recognised. For example, it is likely that “absorption capacity” will become increasingly important as a criterion for proceeding with new enlargements. Already clearly enunciated in Copenhagen in 1993, the “absorption capacity” criterion was given particular emphasis during approval of the mandate to engage in accession negotiations with Turkey and Croatia. It is a fact that the new accessions the Union is pursuing pose a series of problems that have a direct impact on institutions and decision-making mechanisms.

Institutional reform in the Union therefore remains a very topical matter. The critical question is how to address it effectively.

A period of inactivity after the shock of the French and Dutch “no” votes was inevitable and it would be short-sighted to interpret this as indicative of what will happen in the medium term. The issue of institutional reform remains on the table because these reforms are vital to the performance of the Union, and the vast majority of countries (including Italy) are in favour of them. Furthermore, the “Eurosceptic” front has proven itself incapable of exploiting its success in the six months since the French and Dutch “nos”. In France, it has not been able to position itself as a political force capable of reorienting the country's European policy as de Gaulle did after his return to power. Blair missed his opportunity to take on genuine European leadership. And it should be noted that among the first acts of the Merkel government was to request that the ratification process continue; Merkel's personal success at the European Council in pursuing a highly Europeanist line already distinguishes her chancellorship from Schroeder's.

Thus it would be a grave mistake to adopt the position that “the Treaty is dead” or acquiesce in the proposal that the ratification process should be stopped. Cessation would be a downright violation of a ‘perfect’ international commitment. It

should be recalled that while the signature of the Constitutional Treaty by 25 governments is not sufficient to bring it into force, it does impose a clear obligation on governments to see the treaty ratified in their respective countries. The final count can only be taken once the process has been concluded, and only then can the will of those who ratified the Treaty (arguable the majority of countries) be measured against the will of those who did not.

At the same time, it is natural and opportune to explore whether and how it might be possible to improve the Union's performance substantively and make its policies more effective even using methods beyond treaty modification. Ways are not lacking (informal application of the Constitutional Treaty, formation of so-called "vanguard groups" and so on) and appear to be more easily implemented because they do not require consent from parliaments or electorates, and do not involve all Member States. On the other hand, it is obvious that these expedient measures do not allow for critically important needs to be addressed, such as reviewing decision-making procedures and strengthening the institutions' democratic legitimacy. In addition, they also risk being disorganised and incoherent. Without a unified design, they could give rise to contradictions and institutional imbalances that might be difficult to correct even with a subsequent organic reform.

3.2 Alternatives and positions within the Union

An assortment of diverse opinions exist in Europe today on the future of institutional reform. To a certain extent, they reflect alternative conceptions of the Union that have been in conflict for decades, sometimes reconciled through compromises and sometimes resulting in periods of stalemate. And while European policy in no country has been exempt from oscillations and mutations, the different conceptions and opinions that have been in conflict in the past and are in conflict today can be traced back largely to the lasting, if not permanent, nature of the strategies of different countries with respect to European unification.

Four principal positions can be schematically identified.

a) Inter-governmental retreat. Taking their cue from the results of the referenda, some European *leaders* propose renouncing all efforts at constitutional reform and focusing on inter-governmental cooperation. This would imply, among other things, giving up on increasing the powers of the European Parliament and reducing the role of the European Commission with respect to that of the Council.

Some European *leaders* have also expressed a position that is contrary in principal to the deepening of the integration process as such, calling into open question the objective of an "ever closer union" set out in the current Treaty. Their thesis is that integration has already gone too far and that is why it has progressively lost support, as the results of the French and Dutch referenda demonstrate. Insistence on an overall reform, which has already been rejected, could not but provoke even greater opposition from European citizens.

Positions such as those described enjoy considerable support in some older Member States such as Great Britain and Denmark, but have also been expressed recently by the new Polish government and some *leaders* of Slovakia and the Czech Republic.

b) Pragmatic progress. A second position, which can be defined as “pragmatic Europe”, believes that given the difficulties in ratifying the treaty, it makes sense to concentrate on sectorial policies that have a more immediate impact on citizens, such as economic and social policies. If in doing so tangible results can be obtained, for example in terms of economic growth, this would re-establish a climate of trust in European institutions. Putting treaty reform back on the agenda could, on the other hand, generate new tensions. The position is that it makes sense to keep reforms frozen while leaving the door open to the possibility of addressing them in the future in a climate that is more favourable to the creation of consensus, for example if the European economy were to begin to grow at a more sustained rate. In the meantime, some minor reforms could be implemented through informal application of some of the Treaty provisions.

This pragmatic approach, authoritatively supported by the president of the Commission, is shared by the governments of Great Britain and other Nordic countries which, though they do not go so far as to declare the Constitutional Treaty dead, want the emphasis to turn to issues such as the common agricultural policy, the budget, liberalisation of services, etc.

c) Vanguard Groups. The difficulties in relaunching the treaty reform project have led some to argue that the best road to take is to implement greater flexibility through the creation of “vanguard groups” among Member States that want more advanced forms of cooperation or integration in this or that sector.

“Vanguard groups” are presented as the only plausible alternative to reform of institutions and, in particular, of decision-making procedures, and as the only way to prevent the *willing and able* from being constantly subjected to the veto of countries focused on defending national prerogatives. The supporters of this position underline how some integration projects have already successfully developed from vanguard groups, for example, the Euro and Schengen. These groups also demonstrated a notable evolutionary capacity, progressively opening up to countries that were not initially members (no less significant is the fact that the Schengen accord, born outside of the treaties, was successively integrated into them). Furthermore, the current treaties provide for an institutional way to create vanguard groups: the reinforced cooperation mechanism.

An important variant of this position is advocated by those who want to see the formation of a cohesive nucleus of countries intent on closer integration in a systematic way. This would avoid the risk of excessive “variable geometries” through the formation of different vanguard groups for different policies and would provide a more organic central motor for integration. With respect to the composition of this nucleus, one looks above all to Euro countries, with the idea that they might eventually create their own institutional structures alongside those of the Union.

French President Jacques Chirac has recently said he was in favour of creating mechanisms that allow for greater political coordination within the Euro-zone. The Belgian premier Guy Verhofstadt went further, calling for the creation of a “federal Europe” beginning with the twelve Euro countries. Other founding nations, such as Luxembourg and Germany, appear interested in exploring the idea of a progressive political and institutional strengthening of the Euro-zone.

d) Treaty Ratification. Formal and substantive reasons lead others to maintain the need for completing the cycle of ratifications.

On the formal side, there is the commitment that all Member States undertook in signing the treaty and setting a deadline of two years from signature for review of the results of national ratifications. Giving each country the chance to express itself on the treaty in the manner provided in its Constitution is not only a duty but also indispensable for taking pondered collective decisions. On the substantive side, supporters argue that the innovations envisioned in the Constitutional Treaty are essential to avoid decisional paralysis – especially after the recent enlargement and in light of possible future ones – and to give the Union an institutional structure that is more efficient and democratic.

Putting some of the provisions of the treaty into practice in an informal manner, while useful, is considered insufficient to reach these objectives because they concern only limited aspects of the Union's performance and because they do not remove the constraints of the existing juridical framework. Some supporters of this position are also highly sceptical of the contribution the “vanguard groups” could make to integration in the absence of a new institutional arrangement for the Union, that is they fear that these groups could break the Union's political and institutional equilibrium.

The new German government has declared its support for renewing the reform process and has committed itself to promoting it during its presidency of the Union in the first half of 2007. Other European countries that have ratified the treaty, such as Luxembourg and Spain (both did so through popular referendum) also back this approach.

Each of the four approaches illustrated here has different nuances and it cannot be said that they are incompatible. In fact it is likely that some of them are complementary. For example, the pragmatic approach does not exclude *per se* the relaunch of the treaty reform process. Analogously, many supporters of the vanguard groups argue that once consolidated, these groups – in particular the Euro area group – could provide a decisive impetus to the overall strengthening of the Union's institutions.

3.3 Italian constraints and interests

Since the 1950s, Italy has considered **support for the institutional strengthening of the Union** a primary interest. Governments with significantly different positions on other political issues have maintained this approach, giving it continuity and coherence for two fundamental reasons. First, a well-functioning Community is considered a favourable framework for Italy's international profile, its economic development and the strengthening of its own political and institutional system. Second, a robust European institutional system is considered indispensable for protecting Italian interests within the European Community (now Union) and for ensuring its *good operation*. Broad agreement on this approach was underscored recently by the positions adopted by the Italian members of the European Convention and the overwhelming *bi-partisan* vote in the House in favour of ratification of the Constitutional Treaty.

Stronger institutions and decision-making procedures permit effective development of Union policies and their efficient implementation in sectors of vital

interest to Italy, such as immigration, internal security, foreign affairs and the economy. It would be difficult to develop these policies without stronger institutional instruments and additional resources. Institutional strengthening is also needed to avoid decision-making paralysis, which has become more likely with the progressive enlargement of the Union. Finally, it also makes the formation of preferential axes or directories from which Italy, as has occurred even recently, tends to be excluded, more difficult – or less necessary.

One of Italy's major strengths in its European and international role is its particularly strong public support for more efficient European policies and institutional strengthening. During the next legislature, this support will once again put whoever governs Italy in a position to play a leading role in diplomatic discussions over the future of institutional reform.

Decades of experience have taught us that a divided, contentious, slow Europe that is unable to take quick decisions or act efficiently cannot but aggravate the crisis of consensus from which it suffers. Overcoming the limitations on the Union's capacity for action imposed by the current institutional arrangements and procedures thus becomes crucial to defending what has been built so far. And overcoming those limitations calls for the modification of the treaties.

It is clear that renewing the debate about treaty reform will cause tension. But no progress has ever been achieved without it, and Italy has many times in the past made the difference between immobility and progress. Furthermore, one cannot underestimate the increasing difficulties the Union will face in the coming years if it is unable to undertake incisive reform of its institutions. Any initiative that opens up contentiousness is a risk. But leaving the matter pending involves even greater risks.

Striking a good balance between enlargement and deepening is also in Italy's interest. To be credible, a policy in support of enlargement, as has been taking root in Italy, must be accompanied by a corollary commitment to reform within the Union. It seems contradictory to support, as do certain countries such as Great Britain, a broad and quick enlargement while at the same time insisting that institutional reform be put aside or suspended *sine die*.

One immediate need is to **recover the Union's dynamism**. Today, it suffers from a negative climate created by the French and Dutch no votes, the enduring economic sluggishness, and the divisions that emerged over critical issues in foreign policy such as the intervention in Iraq and transatlantic relations.

The entire history of European unification shows that its dynamic has been based on a positive interaction between the exercise of political leadership, the creation of vanguard groups, and the construction of an institutional architecture open to those who accept its rules and principles. Guided by its commitment to support them in so far as they furthered the building of Europe, Italy has over time consistently supported all three of these elements. It often provided a decisive contribution. The government of the next legislature should maintain a positive attitude towards them.

Italy should therefore remain in favour of forming and consolidating *vanguard groups* – both within and outside the EU framework – that help to further cooperation and integration, and should seek to participate in them. The countries in the Euro area could constitute a more cohesive vanguard group with the potential to exert a

locomotive effect on the others, and Italy, as a member of that group, has an interest in working towards its strengthening.

However, to be effective, this potential core group will have to find an adequate institutional basis. The future government should therefore support any initiative designed to strengthen *institutions* and institutional actors by giving them greater democratic legitimacy and greater power of initiative. This is what is envisioned in the Constitutional Treaty through, for example, the creation of a stable presidency of the European Council and a Union Minister of Foreign Affairs, the adoption of a new system for nominating the president of the Commission, and granting the European Parliament greater powers.

Third, *leadership* exercised by national governments, either individually or through groups or alliances, should not be opposed when it is undertaken with a view to developing common policies and contributing to a stronger European construct.

Italy should strive for a relaunching of the reform process, with the goal of bringing the Constitutional Treaty into force. The *sine die* extension of the “pause for reflection” on the future of the Constitutional Treaty looks like a trap that should be avoided. Those who have wanted to block European unification have always begun by suggesting a pause.

Finally, Italy has increasingly felt the need to **strengthen the European democracy**. The arguments against the Constitutional Treaty in France and The Netherlands largely referred to the democratic deficit and the lack of transparency and democratic control in a Union with much greater scope and power of intervention than before. It is worrisome that certain national governments tend to deal with this problem with initiatives such as national referenda – the French and Austrian governments’ promise to organize popular consultations on the accession of Turkey is emblematic – that reinforce the national veto on projects for internal transformation and Union enlargement. An exclusively or predominantly national response to the problem of democratic deficit is inappropriate and even counter-productive. What is needed instead are common policies that encourage the creation of a real European public space in which people can identify themselves and participants as European citizens. Certain reforms move in this direction, in particular those promoting the introduction of new election or nomination procedures for institutional organs (e.g. the president of the Commission), the reinforcement of the European Parliament’s powers, the creation of new institutional figures in the inter-governmental domain that are subject to democratic control, as well as mechanisms for popular initiatives at the European level, and the strengthening of the role of European parties.

The last set of considerations concerns what could be called the politics of **internal alliances in the Union**.

Though with some pauses and exceptions, Italy has traditionally avoided stable alliances, not sought the creation of preferential axes and not opposed the *leadership* often exercised in tandem by France and Germany by trying to form an alternative bloc, such as an Anglo-Italian alliance. At the same time, however, it has always objected strongly to any notion of a ‘directory’, even when it would have been included, as in a directory of the larger nations or the founding countries.

Instead, the Italian approach has always been to support those who endeavoured with greater force to strengthen the European construct: common policies, a strong institutional framework, and a clear democratic base. In following this approach, Italy has on different occasions worked in close collaboration with Germany (one thinks of the Genscher-Colombo Act), France and the Benelux countries; Italy's role was decisive in enlargement to Greece, Spain and Portugal. In some cases – as in the creation of the monetary union – it operated in a decisive way within the Franco-German relationship.

Today it is likely that a new phase will begin in which collaboration between Italy and Germany, which has proven advantageous on institutional matters in the past, could form the basis of a relaunching of the Union. The result of the referendum and the imminent presidential elections place France on hold. But the Union needs to recover its dynamism in the short term. Italy and Germany continue to be more interested than others in institutional strengthening and have both ratified the Treaty with large parliamentary majorities. The new German government, which will hold the Union presidency in the first half of 2007, included an explicit commitment to promoting the reform process in its programme.

Given the arguments presented above, the Italian strategy on institutional reform should be based on the following points:

- ***Promote ratification of the Constitutional Treaty.*** This is the essential prerequisite for the governments of the member countries to present defined positions that have already been confirmed by parliament or the electorate. It is important to create a link between, and possibly coordinate actions among, the ratifying countries that today represent more than half of the Union's population. By acting in concert in 2006, countries that have already ratified the treaty could effectively stimulate the two countries where the no vote prevailed and that have not yet developed a strategy for recovering consensus, as well as countries that have not yet voted or where the government has chosen to wait.
- ***Strengthen European democracy.*** Only the European Parliament can provide the impetus required for relaunching institutional reform from outside the inter-governmental arena. In the first place, the parliament is the strongest expression of European democracy. Furthermore, the Commission has given up playing a driving role and there are no links between national parliaments, even those with a large majority in favour of reform. It will be important for countries favourable to and interested in reforms, such as Italy, to work to ensure that any initiatives coming from the European Parliament are met with support and heard at the inter-governmental level. The new treaty could be submitted to the scrutiny of the electorate in a European referendum involving all Member States during the next European Parliament elections (2009).
- ***Encourage pragmatic progress.*** The informal application of some of the provisions of the treaty should be encouraged, while constant attention should be paid to the impact of the changes, above all those that involve the institutional sphere, on the Union's overall constitutional arrangement.
- ***Support and become a part of the vanguard.*** The creation and consolidation of "vanguard groups" both inside and outside the EU can provide important impetus not only for the integration process but also for the reform process

itself. A core group of Euro countries could play this role in a particularly effective way.

- ***Ally with those who want to see Europe go forward.*** It is in Italy's interest to avoid stable alliances, counter any idea of a 'directory' and support those who work with the greater energy to strengthen the European construct: common policies, a strong institutional framework, and a clear democratic basis. In following this line, Italy can continue to achieve important successes in European negotiations. Today it is likely that a coalition between Italy and Germany, which has proven advantageous in institutional matters many times in the past, could constitute the basis for a relaunching of the Union.