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Europe's Place in Economic Globalisation

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Summary

[1]The data show that the EU, which still has a significant weight and influence in the world economy, looks "condemned" to lose them gradually due to the rise of emerging powers and the greater dynamism of the US. The only solution is to strengthen the EU and have it speak with one voice to the rest of the world. We analyse the cases of trade policy and the geopolitics of the euro to illustrate this argument. Finally, we maintain that Europe's experience with economic integration is a good model for establishing the increasingly necessary rules of play for global economic governance.

Introduction

The 50th anniversary of the EU provides a good opportunity to celebrate its successes. An institutional hybrid that is difficult to classify, the EU has done away with military conflict between France and Germany once and for all and helped generate unprecedented levels of economic prosperity. Although the European social model and the process of integration itself are in the midst of a crisis, within the borders of the bloc (which are constantly expanding) people are enjoying living standards and levels of social cohesion that are the envy of the rest of the world. Furthermore, as the Spanish case shows, practically all of the countries that have joined the EU have experienced a rapid and sustained process of real convergence, in both economic and social terms.

In their overseas projection, the countries of the EU have been the major driving forces of economic globalisation, along with the US. By supporting the processes of trade and financial liberalisation – either directly or through multilateral organisations, in which they are still the most influential powers– they have contributed in a decisive way to the expansion of the market economy, both in developing countries and in the nations of the former Soviet bloc. But paradoxically, the very same process of growing world economic interdependence, which the EU has defended and encouraged, is posing new and difficult challenges for the process of European construction.

Although the EU is one of the key players in the global economy, the very dynamics of globalisation are testing the pact that underlies the European social model, which is based on cooperation between the State and the various social partners. The entry of new, emerging powers in the world economy is causing profound changes in the balance of power within the international system and these changes are slowly undermining the economic weight and political influence of Europe in the world. In particular, the rise of the emerging Asian powers is shifting the epicentre of the world economy from the Atlantic towards the Pacific, leaving the EU in a secondary position in many respects. At the same time, growing trade competition from 'Chindia' and the other emerging markets is increasing the sensation of economic insecurity in the EU and testing people's support for globalisation.

More and more people say the European social model and its generous welfare state are unsustainable and that the rigidities of the economies of continental Europe, in which there will be increasingly aging populations, are incompatible with globalisation over the long term. But at the

1 This paper was prepared for a lecture given at a course organised by EUROBASK and the University of the Basque Country. It was entitled 'The 50th anniversary of the European Union: successes and challenges', and was part of the Summer Courses at the University of the Basque Country (San Sebastian, 2-4 July 2007).

same time, the rejection by French and Dutch voters of the proposed EU constitution in 2005, which plunged the EU into a major crisis that has taken two years to resolve, reflects in part its citizens' deep longing to maintain a socially-oriented Europe and regain the comfortable, privileged position that the bloc enjoyed in the world economy for decades. In fact, underlying the 'no' expressed by many voters is more a rejection of certain aspects of globalisation than of the European integration process itself.

In short, the EU has been a victim of its own success. It has managed to generate peace, stability, equitable economic growth and prosperity, but today it has more and more difficulty both in arousing enthusiasm among its citizens (mainly the youngest ones) and finding its place in economic globalisation. As was the case on other occasions, the solution is more integration, more Europe. Throughout this article we will show how only a Europe that is united and able to speak with one voice on the international economic stage will be able to preserve its influence and fashion the process of economic globalisation by making its values the principles of increasingly necessary (and still absent) global economic governance.

Therefore, in these pages we will argue that if the countries of Europe act separately, they are doomed to exert less and less weight in the world economy. But we will also show how in the economic areas in which they have been able to forge a common position, their weight on the international scene not only has not diminished but in fact has grown. To illustrate this argument we will refer in particular to trade policy and the geopolitics of the euro. Finally, we will defend the idea that Europe's experience with economic integration is a good model to follow for establishing the rules of play in international economic integration.[2]

II. The Inevitable Economic 'Decline' of the Countries of the EU: A Question of Numbers

The citizens of the EU enjoy a very high quality of life. Their societies are peaceful and democratic, their prosperity enviable and their currency strong, and they boast excellent systems of social protection, education and health. They are also at the forefront of defending human rights and the environment.

Although per capita income in the EU-15 is still only 70% of the figure for the US (almost €28,000/year on average, but much higher in some member states), the countries of the EU lead the ranking of the Human Development Index that the United Nations Development Program (UNPD) publishes annually.[3] In fact, in the ranking for 2006, of the top 20 countries only three were not European –Canada, the US and Japan–. It is true that the European economy shows less dynamism and is less innovative than that of the US. However, Europeans work fewer hours –and therefore enjoy more leisure time–, feel more protected and secure and live in societies that are relatively more cohesive and supportive (it should be noted that the distribution of income is much more even in the countries of the EU than in the US).

At the same time, the EU-27 has unquestionable weight in the global economy. Its GDP exceeded €11.5 trillion in 2007 (a figure slightly higher than that of the US) and accounts for more than 20% of global GDP. It is also the world's top trading power (it stands out particularly in exports of services), the largest development-aid provider (more than €37 billion in 2006), one of the main senders and recipients of direct foreign investment and four of its members belong to the G8 (Germany, the UK, France and Italy). At the World Trade Organisation (WTO), the EU is without a doubt one of the four main players along with the US, Brazil and India (for the time being China is keeping a low profile at this organisation, just as Japan has done historically). Finally, at the

[2] As the title of this article indicates, we will refer mainly to economic issues, so we will not address questions of a strictly political nature or ones related to security and defence policies.
[3] This index measures human development on the basis of per capita income, life expectancy and educational level. See *www.pnud.org.*

International Monetary Fund (IMF) and the World Bank, the combined votes of the countries of the EU amount to 23% of the total, six points more than the US. With an internal market of 500 million consumers with a lot of purchasing power, the EU is an economic giant.[4]

But we must not be fooled by these impressive figures. The structural change associated with the process of economic globalisation, which is characterised by the rise of new, emerging powers, will lead inexorably to a reduction in the relative weight of each of the EU members in the world and possibly that of the EU as a bloc. Although living standards in the countries of the EU will remain high (in fact it is unlikely that any emerging power will match the EU in per capita income in the next few decades) the size of Europe's economies as a percentage of world production will decline, and with it part of the influence of EU countries in international relations. This structural change could not be averted even if they managed to carry out the ambitious structural reforms proposed in the so-called Lisbon Strategy to increase growth and productivity.

In order to illustrate this trend, all we need to do is consider a few indicators, beginning with population. In 1960, the EU-6 accounted for 12% of the world's population and the rest of Europe for 22%. In 2005, the EU's share of the world population had declined to 7.1% (460 million out of a total of nearly 6.5 billion). According to United Nations projections, in 2050 the EU-25 countries will have less than 6% of the world population, some 600 million out of a total of 9.076 billion (United Nations, 2005; and the European Commission, 2006).

While population is an important element, it does not explain in and of itself relative economic decline over the long term. But most economic forecasts point in the same direction as well. For instance, the report that gave a name to the concept of BRICs, or emerging powers (Brazil, Russia, India and China), published by the American investment bank Goldman Sachs in 2003, compares the expected evolution of the six largest economies in the world (the US, Germany, the UK, France and Italy, also known as the G6) with that of the four BRIC countries from 2000 to 2050. Using realistic and conservative assumptions on rates of growth, demographic evolution and variations in currency exchange rates, the report concludes that the GDP of the BRICs will surpass that of the G6 in 2039 in dollars.[5] But what is more important from the standpoint of the countries of Europe is that starting in 2036 all the BRIC countries will have surpassed in GDP size all of the European nations. In other words, none of them (not even Germany) will be among the world's six largest economies (the US will be first, followed by China, India, Japan, Brazil and Russia). Even in terms of per capita income measured in dollars from the year 2003, Italy and Germany will be poorer than Russia and only 20% wealthier than China.

This relative economic decline will have important implications for the influence that the countries of Europe wield in the global economy. The reduction of the weight of European production and population as part of the world total will be accompanied by a drop in their market share in international trade. This could gradually weaken the EU's current position of leadership in this area, both at the multilateral level (WTO) and in bilateral and regional accords. At the same time, the foreseeable changes that will take place in its shares and votes at the IMF and the World Bank in coming decades will mean a loss of European power, as already seen in the first phase of the reform of the IMF that began in 2006 in Singapore (Fernández de Lis, 2006).

If to all this we add nearly all the European countries' heavy dependence on gas and oil and the predictable increase in price volatility and energy nationalism by exporting countries (mainly Russia), dark clouds hang over the economic horizon of the EU countries in the long term.

[4] All of these figures come from Eurostat, *http://epp.eurostat.ec.europa.eu*.
[5] If purchasing power parity were used instead of market exchange rates, the change would take place much more quickly because the economies of China and India, for instance, are already bigger than those of Germany, France or the UK in terms of purchasing power parity but smaller if measured in terms of market exchange rates.

In short, Europe will gradually lose weight and influence in the world economy. In the words of the former Spanish Prime Minister Felipe González, Europe will experience a 'sweet decadence' because its member states will be less and less relevant on the international stage but their citizens will maintain high income levels and many accumulated rights (which they will not want to lose). In fact, as suggested by the provocative book by Alesina and Giavanzzi (2006), *The Future of Europe: Reform or Decline*, this 'sweet decline' will turn into a free fall unless the EU embarks on an ambitious programme of reforms that allow it to increase the potential growth of its economy, its capacity for innovation and its productivity. But even if the political obstacles to carrying out these reforms were to be overcome, this would only make the loss of EU weight in the global economy more gradual. It would not reverse it.

With this kind of scenario, one can ask what the most effective strategy for reinforcing the role of the EU in economic globalisation is. As we will show in the next section, the best alternative is to strengthen the EU, leave aside nationalist and mercantilist positions and move ahead in common policies. In the economic areas in which the countries of the EU have managed to forge a common position and speak with one voice, their weight and influence in the global economy have risen. In fact, both in commercial aspects and those related to the role of the euro as an international currency reserve, the weight of the EU is much greater than that of the sum of its members. However, in the areas in which it has not yet been possible to articulate a common policy, such as energy, immigration or foreign and common security policy, the influence of European countries in the world is declining quickly. We will now examine these two realities in greater detail.

III. Two Examples of the Power of a United Europe: Trade and the Euro

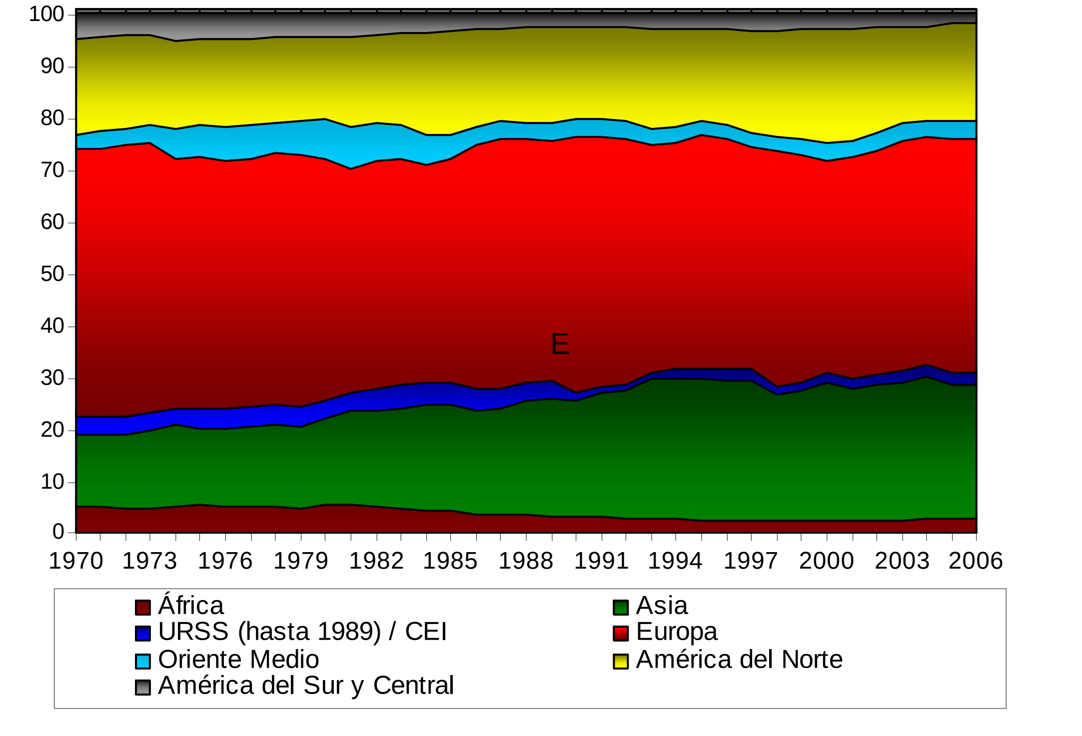
A Giant in Trade Policy

It is a well-known fact that the EU is the world's leading trade bloc. In 2006 its members exported goods worth more than US$4.5 trillion, giving them a share exceeding 40% of the world total. In the service sector its weight is even more important as its exports totalled more than US$1.2 trillion, more than 45% of the world total (WTO, 2007). As Graph 1 shows, the European share of world trade in goods has remained stable over time and has only fallen slightly since the 1970s despite the entry of emerging powers (mainly Asians) in global trade.[6]

Although more than 60% of EU trade takes place among its member states, the Union as a bloc plays a crucial role in determining the rules of global trade, which are increasingly the seeds of global economic governance. This is due not only to its weight in world trade (which is superior to that of the US, the second-largest power in this category), but above all to the fact that in trade policy the EU speaks with a single voice, which enhances its negotiating power tremendously.

[6] Trade among member states of the EU is tallied, but not among states of the US, so the commercial weight of the US is undervalued with respect to that of the EU. Europe's share of world exports –excluding trade among EU member states– exceeds 20%, so the EU as a bloc is also the world's leading exporter.

Graph 1. International trade in goods by regions (imports plus exports) 1970-2006 (%)



Source: World Economic Outlook (IMF), online data base.

Since the signing of the Treaty of Rome in 1957, the trade policy of the member states has fallen under the direct jurisdiction of the European Commission, which sets the common external tariff for the entire bloc and can also negotiate preferential agreements with certain groups of countries, such as those of the Mediterranean basin or Africa, the Caribbean and the Pacific (ACP).[7] This means that it is the European Commissioner for External Trade, Britain's Peter Mandelson (until 2005 it was Pascal Lamy of France, who is now the Director General of the WTO), who represents all the member states in international trade negotiations.[8]

As the EU has taken on new members, the Union's specific weight and negotiating power have increased, first in GATT (the General Agreement on Tariffs and Trade) and then in the WTO since it was created in 1995. In fact, the development of the internal market and the EU's deepening and enlargement have advanced in parallel to world trade integration within GATT, although the former has achieved much more ambitious goals than the latter.[9] And the EU has always advocated multilateral rules for trade governance, something the US has defended with less enthusiasm since the 1980s when it started negotiating bilateral and regional trade agreements.

Forging a common trade policy has not been easy because not all European countries have the same trade interests. For instance, while France has interests to defend in agriculture, Britain has virtually no farming sector. So London does not want the protectionist Common Agricultural Policy to be an obstacle to other countries opening up their markets to exports of services with a high added-

[7] It is often said that the EU has a 'pyramid of trade preferences' because within the WTO it applies a common level of protectionism to all countries but also grants different levels of additional preferences to different groups of countries for economic, geo-strategic or development aid reasons. See Tsoukalis (1997, p. 241-48).

[8] In fact, the treaties establish that it is the Commission which has jurisdiction over trade in manufactured goods, so in trade in services some member states have sometimes adopted positions different from those advocated by the Commission.

[9] See Wilkinson (2006) for a detailed analysis of the evolution of GATT and the role of the EU in the negotiations.

value,[10] the sector in which Britain has a competitive advantage.[11] Germany, meanwhile, mainly exports sophisticated manufactured goods and equipment, while Spain, Italy and Portugal are bent on protecting their textile and automobile sectors against competition from the emerging Asian markets, especially China.[12]

But all the countries have understood that adopting a common position with regard to the rest of the world is the only way to continue to be a powerful global player in international trade and being able to project their interests and values in the governance of world trade. Indeed, cooperation among the member states in trade is the best (and perhaps one of the few) examples of effective performance of the European integration model in dealing with other countries. It is the fruit of a consolidated institutional machinery, shared values and a shared experience according to which Europeans have realised the advantages of putting Brussels in charge of certain policies with an eye to regaining at the supranational level part of the influence that the member states had lost due to economic integration and the advance of globalisation. Tsoukalis sums it up this way:

> 'the advantages of a common voice in multilateral trade negotiations were evident from the outset for the members of the European Community and the rise of the European regional bloc served to change the balance of power in GATT' (Tsoukalis, 1997, p. 233).

This does not mean that the EU does not sometimes behave in a mercantilist and protectionist way in multilateral and regional trade negotiations. Like any other player, it defends its commercial interests, which occasionally leads it to adopt procedures criticised by other states, even if it always does so without violating WTO rules. Thus, European trade policy involves a high degree of agricultural protectionism, excessive use of anti-dumping procedures against trade practices deemed unfair, various kinds of non-tariff barriers, a large number of discriminatory preferential agreements and attempts (not welcomed by emerging powers) to 'export' its policies on competition, investment and public purchases to other countries.

But despite these positions, the EU has always been a staunch defender of the rules devised by the WTO. In particular, it has advocated the existence of a resolution mechanism in trade disputes with capacity for imposing sanctions, similar to the European Court of Justice, and enlargement of WTO regulations to more and more issues (policies on defending competition, the environment, intellectual property rights, protecting investments, etc). Both of the factors show the EU's preference for supranational rules and institutions over the use of unilateral power and coercion as a way to deal with and fashion economic globalisation.

The EU's common trade policy is the best and clearest example of how there is strength in numbers. The bloc's negotiating power in trade issues is significantly greater than that of the sum of its member states, and it has no equal among other EU foreign policy areas.

The Geopolitics of the Euro

Economic and Monetary Union (EMU), the culmination of which was the creation of the euro in 1999, was an internal European project aimed at going further in economic integration and with the single market, increasing economic efficiency by cutting transaction costs, promoting exchange rate stability and trade among member states and driving political union. Therefore, turning the euro

[10] These services, in which in general most European countries have a comparative advantage, are insurance, banking, telecommunications, consulting, legal services, basic and universal services and, in general, the various manifestations of direct foreign investment.

[11] It should be recalled that in general, international trade negotiations follow a mercantilist logic in which the different states trade concessions under the principle of reciprocity.

[12] A more extensive and detailed analysis of the main countries' trade interests can be found in Steinberg (2007).

into an international reserve currency that would compete with the dollar and could be used as a tool of foreign policy was never among the main goals of EMU.[13]

However, less than a decade after it was created, the euro has become a powerful asset for the union to exercise foreign policy. Furthermore, current macroeconomic and global trends, which are characterised by the US's high current account deficit and accumulation of foreign debt and by a weak Japanese economy, suggest that the weight of the euro will only keep rising in the next few years.

Slovenia adopted the euro in January 2007, bringing to 13 the number of EU member states that use the single currency (if Malta and Cyprus join up in January 2008 the number will be 15). Except for the UK, which will probably end up embracing the euro in the future, all the other major powers in the bloc have joined EMU. This has created a strong competitor with the US dollar for the first time since World War I. Although the dollar will continue to be the world's dominant currency, it will gradually lose market share. This will reduce part of the political influence and monetary privileges that the US enjoyed for most of the 20th century.

As seen in Table 1, international money serves various functions, both for private and public purposes. It is a store of value in which individuals and businesses invest, and it allows central banks to accumulate reserves. It is also a unit of account, which serves to denominate international trade or let countries (mainly developing ones) peg their exchange rate to that of an anchor currency. Finally, an international currency serves as a means of payment, both in private commercial transactions and for intervening in currency markets, a task carried out by a central bank.

Table 1. Functions of international money

	Private use	**Official use**
Store of value	Investment/financing currency	Reserve currency
Unit of account	Denomination/quotation currency	Anchor currency
Means of payment	Invoice/ vehicle currency	Intervention currency

In the international monetary system there is a natural tendency for just a few currencies to serve as international money. This oligopolistic structure is due to the existence of network externalities and economies of scale, under which the more players using a given currency, the higher the likelihood that others will use the same currency because it is more convenient, efficient and cheaper for them (Cohen, 2003; Eichengreen, 1996, chapter 1). Historically, there have been a dominant world currency and a few secondary ones –usually regional leaders– that allowed a degree of diversification in the asset portfolios of individuals and central banks, so a pyramid structure of 'international monies' would tend to form. In the 19th century, the dominant currency was the British pound sterling, and since World War I it has been the US dollar. Changes in the role of a dominant currency have always been slow because of the significant inertia that made it hard for an emerging currency to displace the leading one. For example, the dollar did not overtake the pound sterling until World War II, even though Britain's economic decline with respect to the US began at the start of the 20th century.

A currency's consolidation as international money depends on several conditions. First, it must be backed up by a strong, dynamic and large economy which also has a significant share of world trade and good economic governance. Secondly, it must be issued by a central bank that controls inflation (to keep assets from losing their value). Third, it must have large, established and liquid financial markets that offer a wide range of instruments that allow investors to diversify risk.

[13] Although it was to be foreseen that creating the euro would have geopolitical implications favouring the EU, practically none of the Commission's publications that analysed the expected benefits of EMU cited the role of the euro as an international currency.

Finally (and even though it is a short-term and secondary factor), it should not be structurally prone to depreciation, which means the state issuing the currency must not have an unsustainable accumulation of debt. In other words, it should not run up structural current account deficits for an extended period.

To all of these conditions one must add government preferences and geo-strategic considerations, which can give rise to political decisions to adopt a currency even if there is no clear economic justification. Consider, for instance, Iran, which sells its oil for euros, or Cuba, which taxes the use of dollars.

Table 2 allows us to carry out a first comparison of some of these elements among the euro zone, the US and Japan. It is clear that the euro meets the necessary (but not sufficient) conditions to become an international reserve currency. The euro zone together is the world's second-largest economy measured in GDP and its share of world exports exceeds that of the US. It also boasts an independent central bank that has proved itself to be an adamant defender of price stability, even more so than the US Federal Reserve.[14]

Table 2. International comparison of key indicators (2006)

	Euro zone	US	Japan
Population (millions)	315	300	128
GDP as % of world GDP	16	21	8
GDP per capita (€ thousand, PPP)	25.5	35.6	25.9
Exports (% of world total)	20	15	9
Current account balance (% of GDP)	-0.2	-7.0	3.9

Source: the author, with data from Eurostat, BIS and DB Research.

But due to the geopolitical and military weight of the US, its economy's higher potential for growth and, above all, powerful inertia that makes it hard for a currency to overtake the supremely dominant one, the euro is still far from reaching the dollar's 'market share', especially in terms of central bank reserves.

Still, it is important to note that data suggest the euro has a major potential for growth (unlike the Japanese yen, which has been losing 'market share' since the 1990s). Ever since its creation, the euro has managed to have a greater weight than the sum of the national currencies that preceded it in the euro zone, including the ECU. It has gone from accounting for less than 18% of the reserves of the world's central banks in 1999 to more than 25% in 2003. The dollar's share is about 65%, although it has been declining since 2001 and the pound sterling has grabbed third place from the yen with 4.4%.[15] Furthermore, the IMF says that more than 60 countries –most of them close to the euro zone geographically and commercially– have in some way pegged their exchange rate to the euro. This obliges them to have reserves in euros and enhances the political influence of the EU.[16]

Finally, there are two elements that favour the euro over the long term. First is the huge, growing and unsustainable current account deficit in the US (fuelled in part by a high public deficit and not very responsible macroeconomic management). This could trigger a loss of confidence in the dollar, which would in turn boost the weight of the euro in investors' portfolios and central banks.[17]

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[14] Furthermore, in December 2006 the number of euro bills in circulation exceeded that of dollars for the first time, reaching €628.2 billion. However, there were still many more dollars outside the US than euros outside the euro zone (Becker, 2007, p. 3).

[15] As the make-up of central bank reserves is not public information, it is not possible to know exactly the percentage of each currency. Several estimates are used. The data we use are taken from Becker (2007) and the Bank for International Settlements (BIS) in Basel.

[16] We are referring especially to the weight of the euro in central bank reserves because of its geo-strategic importance. However, in 2006 46% of the bonds issued around the world were in euros (39% in dollars) while in other respects, such as international trade or buying and selling of hard currencies in international markets, the dollar is still dominant.

[17] See Crespo & Steinberg (2005) for an analysis of how this loss of confidence could trigger a crisis with the dollar and lead investors and central banks to seek refuge mainly in the euro.

In second place there is the massive accumulation of reserves by central banks in emerging economies (mainly Asian and oil exporters). It surpassed US$5 billion in 2006 and could lead to a greater diversification of portfolios and a quest for investments that are more profitable than US treasury bonds, possibly making the euro more attractive.

These data allow some analysts to espouse the hypothesis that around 2010 more than 30% of the reserves in central banks around the world could be denominated in euros (Becker, 2007; Posen, 2005; ECB, 2005). With this kind of figure the euro would be in a position to start to compete seriously with the dollar, especially if the UK ultimately decides to adopt the European single currency.[18]

Therefore, although it is not likely that the euro will replace the dollar in the next few decades, it is in fact possible that we are approaching a dual monetary hegemony. In order to strengthen even further the role of the euro as an international currency, it is essential to go further with EU structural economic reforms that will allow higher potential European growth, improve the system of economic governance of the euro zone and integrate and deepen even more its financial markets.

This will let the euro zone exercise more flexibility in designing its macroeconomic policy, increase its seigniorage revenue, obtain external financing at a lower cost and, above all, wield greater political influence on the international scene, including a capacity to pressure other states.[19] Furthermore, if there were an agreement for the countries of the euro zone to speak with one voice in international financial organisations, the headquarters of the IMF and the World Bank would have to move to the euro zone because the sum of the votes of its countries is greater than that of the US.

In short, even if it does so in a less clear way than in trade, the geopolitics of the euro also shows how the deepening of the process of European integration allows its member states to exert greater influence in international monetary relations. In the early 1970s, before the breakdown of the Bretton Woods system of fixed exchange rates pegged to the dollar, then US Treasury Secretary John Connally said: ‘The dollar is our currency but your problem’. This statement is in contrast with one by Joseph Christi, a member of the board of governors of the Bank of Austria, who recently said ‘the euro is our currency and everyone’s asset’.

IV. Conclusion: Moving Towards Global Economic Governance: The EU’s Role

The examples cited above show how the weight and influence of the EU in the world increase when its member states group together and defend a common position. There is an enormous contrast between trade issues and foreign policy areas in which there is no common policy, such as energy and immigration. In the former, the EU is a solid, influential and respectable power; in the latter its internal conflicts weaken its international position and negotiating power, something which other states take advantage of.

But the most constructive and long-term contribution that the EU can make to economic globalisation is to use its model of integration and supranational economic governance to inspire increasingly necessary global economic governance. Besides exporting goods and services, the EU aims to export values and ways of resolving conflicts peacefully and through negotiation based on its own successful experience. Khanna (2004) has gone so far as to suggest that the EU is the first *metrosexual* power, using its soft power, economic influence, values and persuasion (and not

[18] Other authors are less optimistic. See Cohen (2003) and some of the articles compiled in Posen (2005).
[19] For an analysis of how political power and coercion can be exercised through the strategic use of an international reserve currency, see Cohen (2006) and Kirshner (1995 and 2003).

military might) to 'sell' its model abroad. It is here that the EU can make a major contribution to globalisation.

The fundamental problem with economic globalisation is that it lacks global rules. It does not yet have a set of solid norms and institutions agreed in a legitimate, multilateral way to govern an economy which in many aspects is already global but which is still run by economic policies that are national and sometimes clash, either directly or within international economic institutions.

In a world which is more and more integrated and interdependent economically, the political autonomy of states is reduced and that of markets is increased. It is even possible that democracy is undermined when integration in the world economy restricts governments' options in economic policy. This tends to happen mainly in developing countries, but also in developed ones. The only way to keep this decline in national sovereignty from turning into growing discontent with globalisation is to establish legitimate and democratic supranational institutions to keep order in the process of integration and reduce its adverse effects (Rodrik, 2000; Steinberg, 2007). Global problems such as persistent poverty and underdevelopment, rising inequality (both between countries and within countries), deterioration of the environment, an increase in volatility and a greater tendency towards financial crises as a result of market integration or trade rules lacking legitimacy require global responses.

But this is in fact what the EU has been doing gradually. After five decades of work, the EU has managed to create the world's most integrated economic area, with a complex political and legal regime for decision-making and the division of power that establishes a system of checks and balances among the member states. The consolidation of this 'European dream' (Rifkin, 2004) has taken shape through successive treaties which grant more and more supranational power to EU institutions and oblige national legislation to adapt to the principles established by the bloc, turning to the European Court of Justice when conflicts arise.[20]

This pioneering organisational structure has reduced the scope for manoeuvre of each of the member states and created a formal body of EU law, but it has not eliminated the democracy or sovereignty that the bloc's citizens enjoy. Rather, it has transferred the top level of political decision-making to Brussels; in other words, to the supranational realm. Furthermore, in an effort to avoid North-South conflicts between relatively rich and relatively poor countries, the EU has established a fledgling mechanism for transferring wealth through so-called structural and cohesion funds. As Keohane says (2003, p. 128):

> 'The EU is *sui generis* because it is a more powerful and complex institution than traditional international organisations. Its Member States have ceded sovereignty, giving up both veto power over many decisions and determining if EU legislation does or does not become national legislation. […] In its current configuration it is half-way between an international organisation and a state'.

Although the EU's supranational model has been a success, it does have problems with the way it functions. On one hand there is a sort of deficit of democracy because even though there are direct elections to the European Parliament, democratic control over the European Commission is limited. In almost all member countries, there is resistance to deeper political integration.

The difficulties that have manifested themselves in the European experience show that establishing a similar model of global federalism will not be easy, for at least two reasons. First, because there would be many more countries involved, and this would hamper decision-making and render it harder to resolve the problem of the deficit of democracy. Secondly, because the differences in development level, income, institutional capacity and diversity of political preferences that there

[20] See Tsoukalis (2005) for a detailed analysis of the process and its future challenges. Moravcsik (1998) offers a thorough analysis of the process of intergovernmental negotiation through which the EU has become what it is.

would be among these countries would be greater than in the European case. So it would be difficult to agree on just what best serves the public good.

But despite these obstacles, the European experience shows that it is possible to gradually move ahead in building supranational economic governance that utilises the enormous advantages that globalisation offers and reduces its most adverse effects. A strong and united EU is the body that can best lead this process, which would allow the benefits and costs of globalisation to be shared more fairly and equally. This would make the process more legitimate and thus more sustainable.

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