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THE SPROUT

Vol III Issue 05 February 2005

INVESTIGATION, SATIRE & FREE SPEECH DIRECT FROM BRUSSELS



Stockholm Network Report £5

Reform in Europe is like sex. It's not spoken of in polite company, but people assume that everybody else is doing it. In this sense, 2004 was a relatively abstemious year for Europeans, even if it was a momentous year for the continent. The historic rapprochement that began with the fall of the Berlin Wall fifteen years ago saw eight former Communist countries (plus Malta and Cyprus) become members of the European Union - the world's largest capitalist club. Several joined the North Atlantic Treaty Organisation to boot. War on the European Continent has never been such a remote possibility.

Yet accession has brought with it significant challenges for both the new members and the EU-15. For the former, greater access to European markets is mitigated by constant calls for tax harmonisation, and their comparative workforce advantage is ever more encumbered by regulation and prohibitive 'minimum standards'. These are sources of great friction between the competing member states, as the previously sheltered economies of 'Old Europe' struggle to compete with efficient foreign competitors.

The rapid ageing of Europe's population over the next few decades is likely to exacerbate these tensions. Current budget deficits and levels of national debt will appear insignificant as the cost of maintaining the continent's bountiful welfare system become increasingly apparent. Economic growth and productivity will level off and begin to decline as an ageing workforce is unable to replace itself. Commensurately, government programmes that rely on current revenue streams will fail to meet the ever increasing demand for healthcare and social security.



As conditions worsen, socialism and protectionism will seem all the more appealing to the public, and government's populist instinct to centralise power will only strengthen.

Fortunately, there is a growing consensus on the necessity of reform.

The Stockholm Network recently completed *The State of the Union*, a report which examines the progress of market-oriented reform in the EU in 2004. Authors from all the member states contributed essays looking back over the previous year in their individual countries, and the collection makes compelling reading. It seems natural that the governments of the Scandinavian welfare states are making the least progress in reforming their entrenched civil bureaucracies. However, they are quietly pursuing the most far-reaching reforms. For example, Finland and Sweden both have commissions examining the role of the entire public service system which, given sufficient political cover, are likely to propose far-reaching reform. Conversely, with a general election looming in Britain, both major political parties are attempting to burnish their reformist credentials. Such is the weight of Margaret Thatcher's legacy.

As the report elaborates, significant progress was made in some areas in 2004, for example on the Danish and Lithuanian pensions systems, and in Germany on welfare provision. But while EU member states face many of the same economic and demographic challenges, the obstacles to, and progress of, reform vary greatly between regions. *The State of the Union* dwells equally on the idiosyncrasies of the EU's constituent parts in an effort to understand the sporadic nature of reform in Europe. For example, the Mediterranean nations of Spain and Italy have long endured a powerful central state. Their culturally diverse regions retain few powers of governance, and all major political decisions are taken in Madrid and Rome with the inevitable economic inefficiencies. Conversely, Eastern and Central European nations, having recently emerged from the yoke of Soviet oppression, are often torn between maximising their new found economic freedom and a desire to retreat into the familiar embrace of the state.

At the EU level, the appointment of José Manuel Barroso, the reform minded former Prime Minister of Portugal, gives much cause for optimism in 2005. He has vowed to make the Lisbon Agenda his first priority, but as both he and many of the authors in *The State of the Union* recognise, national governments alone that have the political legitimacy to enact the tough reforms that will ensure Europe's prosperity continues well into the 21st century.

Sacha Kumaria