

## 64<sup>th</sup> Königswinter - Conference Summary

Cambridge, 27<sup>th</sup>-29<sup>th</sup> March 2014

### Europe's place in the changing world: Global Hub or Museum?

The leaden skies of last year's conference in Neuhardenberg made way for Cambridge in the spring sunshine for this year's Königswinter Conference, held in the glorious setting of King's College. The outlook for Anglo-German relations was also on the up in this 300<sup>th</sup> anniversary year of the coronation of King George I. Only four weeks earlier, Angela Merkel had visited London and had been bestowed with the rare honour of addressing both Houses of Parliament. She had also taken tea with another popular and long-serving woman, Queen Elizabeth II. It was now over a year since the British government had laid out their plans for a more flexible Europe and announced their intention to hold an in/out referendum. A fortnight earlier, David Cameron had provided his thinking on EU reform and put forward his seven targets for a new EU. This was the context for the 64<sup>th</sup> Königswinter: Europe's place in the changing world: Global Hub or Museum?

The Conference Chairmen Sir Michael Arthur and Jürgen Großmann opened the conference and set out the areas of divergence and convergence between the two countries. With Germany the largest eurozone member and the UK the largest non-eurozone member, it was clear that this would result in differing visions for the EU. However, there was also convergence on how to reform the EU, boost trade and improve competitiveness in an outward looking EU. The pressing issue of Ukraine was also a recurring theme of this year's conference. How to handle Putin would test the resolve of these two nations. As one participant put it, "the bear is growling." Königswinter's role would be to facilitate frank and open discussion and find areas for common action.

### Opening Panel

After the three group topics were introduced, the highlight of the opening evening was a panel discussion with George Osborne, Chancellor of the Exchequer and Wolfgang Schäuble, the German Finance Minister. Their comments were off the record, however, in an interesting demonstration of the convergent thinking between London and Berlin, the two Ministers published a joint op-ed in the Financial Times the following day, which covered aspects of the debate.

The overall message of the jointly penned piece was that further reform was needed to integrate the eurozone whilst protecting the interests of those member states outside of the eurozone. Although the UK and Germany were performing well economically with record levels of employment, reforms were still necessary and would support recovery. Some of these reforms would be at the national level but others would have to take place at the European level such as completion of "the EU's single market, especially in services". A stable euro was in the interests of both countries and much had been achieved to strengthen the functioning of the single currency such as the formation of the permanent bailout fund (the ESM) and the new banking union. But the crisis had shown that the eurozone needed a common fiscal and economic policy. However, this had to be achieved in a way that did not put member states outside the euro at a disadvantage. The UK fully supported the case for necessary further eurozone integration but "future EU reform and treaty change must include reform of the governance framework to put euro area integration on a sound legal basis, and

guarantee fairness for those EU countries inside the single market but outside the single currency". This was an important procedural step to enable fair play for all in a Brussels that respected "the principles of subsidiarity and proportionality". Echoing the theme of this year's conference "Global Hub or Museum" the two Finance Ministers finished on an upbeat message that reform was possible and would support recovery. "No one should assume that European decline is inevitable. It is in our hands to build our future success. And the UK and Germany are committed to making that happen".

### **Is Europe a 21<sup>st</sup> Century power and player?**

In the following day's discussions, Group 1 had been set the topic, "is Europe a 21<sup>st</sup> Century power and player?" This had provoked a critical look at the EU as a foreign policy actor. The EU had been inward-looking in recent years as a phase of enlargement had come to an end. But now the EU needed to reposition quickly to deal with the threat posed by Russia. One German participant quoted Winston Churchill, "nothing focuses the mind more than being shot at." A British participant referred the group to Mike Tyson's famous adage, "everyone has a plan until they get punched in the face".

The EU was swiftly likened to an integration "tank" that was in the process of a redesign to add wings to make it fly. What was the best way to do this? One German participant noted that with enough thrust anything would fly. But the fuel needed to provide the thrust in terms of popular support was sorely lacking.

Picking up on the earlier theme of converging and diverging views between the UK and Germany, there was a consensus in the group that with the possible exception of Asia, there was more convergence in foreign policy than in previous years. In Germany, there was a lot of support for Angela Merkel's stance on Russia. But as leader of a grand coalition, the differences around her would soon bubble up to the surface if the crisis escalated. German participants debated whether the Ukraine crisis would provide the catalyst for an energy security debate in Germany, or whether the Energiewende would complicate any move to reduce dependency on Russian gas. As one participant put it, "Ukraine is not a big enough crisis for Germany yet. The lights have to go out in Hamburg, not just Sofia". The spectre of Cyber war was also raised. Russia's latest diplomatic weapon was to leak transatlantic diplomatic discussions but the real threat was Russia deploying its offensive cyber capability against the EU. "The tank that just learned to fly needs to upgrade its software too".

The divergence between the foreign policy and defence establishment and society at large was becoming increasingly pronounced, with public opinion increasingly shaped by social media and less deferential journalism. Policymaking had to take these views into account but then critically leadership was required to bring the public along, step by step. Some British participants identified this as increasingly difficult in the UK where populist parties exploited the aversion to wars of choice and mistrust of intelligence post the Iraq war. Public opinion in the two countries was converging and the British public were becoming more German and more anti-interventionist. UKIP in particular was tapping an isolationist seam in claiming that "cosmopolitan elites involve us in foreign adventures".

The group concluded with a discussion about Europe's strength and weaknesses. The clear strength was in soft power, winning the "battle of lifestyles". But the power and attractiveness of the "European model" and the shared values could only work if the EU

had a unity of purpose and common intent. One British participant remarked, “we might be a museum but people still aspire to a western model – not the Chinese or Russian models”. Although others cautioned about just how favourable the model was seen from afar. “Europe is from Venus, but the rest of the world is from Mars.” The weaknesses remained in hard power, with EU defence spending at half of US levels but producing only 10% of the military capacity there. The next NATO summit would importantly discuss Article 5 but the question was whether the EU would have the military capacity to match the new political will.

### **Modernising Europe faced with shifting sands in public opinion**

Group 2 considered the economic challenges ahead with a critical look at both countries. There was broad consensus that although the headline numbers were encouraging on growth and employment, looking at both the composition of growth and the longer term headwinds, a very different picture emerged. The UK in particular was vulnerable to this with the fastest growth rate in the G7. The growth however was consumer-led with business investment well below that of Germany and France. Dis-saving by the consumer could be seen in the growing current account deficit and with the fabled rebalancing was yet to materialise. The positive employment numbers too, had to be viewed in the context of abysmal labour productivity statistics for which no clear answer could be found.

The German economy had proved to be resilient with GDP well above its pre-crisis peak. Here several German participants argued that was that there was a risk of complacency setting in, together with back tracking and unwinding of previous labour market reforms. The big topic for Germany was energy. As one British participant put it, “how much irrationality can you afford?” Demographics and education were identified as two other levers to ensure “that we don’t end up in a museum”. Some British participants questioned Germany’s approach to public investment. The focus on debt reduction and the absence of a golden rule to enable public borrowing for investment purposes would have pernicious longer term consequences. Present borrowing conditions with real interest rates close to zero were not being utilised to bolster woeful levels of public investment and upgrade education.

Both British and German participants maintained that the single market was vital for the EU long term economic performance. There was also agreement from both sides that services liberalisation should be the top priority for the incoming Commission, although some participants warned about growing fatigue on the subject.

### **Visions of the European Union**

Group 3 debated “visions of the European Union”. This kicked off with the question: was there a common European model? “Yes, it costs a lot” came the immediate reply but further unpacking of the statement led to wide agreement that there was more to it than just membership of a trading club. Instead, it was rooted in shared values including personal freedom, rule of law and democracy. It quickly became clear that there were two visions for Europe driven by the “two beating hearts” at the core of Europe: the single market and the eurozone. British participants were concerned about the effect future eurozone integration would have on European decision making. From 2016 onwards, the eurozone would have a qualified majority, would meet prior to a vote of all EU member states and could caucus along those lines. There was a risk of spill-over from eurozone discussions to financial decisions. Such concerns were not just theoretical and

the recent demand from the ECB that euro clearing houses should be located in the eurozone had rattled the cage somewhat.

Whether the two competing visions could be maintained over time was then examined. As the “pre-ins” joined the euro, the number of “outs” dwindled, and as some non-eurozone countries participated in eurozone institutions such as banking union, could the interests of the few continue to be balanced against the interests of the many? One British participant pointed out that it would be a long time before the UK would be the only non-eurozone member state. 80-90% of Swedes were against joining the euro and Poland required constitutional change in order to join. Maintaining balance and fairness between the groups was clearly not just a British problem.

The vision for the eurozone also hinged on whether full fiscal union was needed or not. Here, the British participants were divided, with some challenging the approved wisdom. After all, the US Federal Government did not bail out bankrupt states such as Detroit. Bankruptcy led to losses for US creditors, as would be the case in Europe under the newly adopted bail-in regime. But Angela Merkel in her speech in London a month ago, had clearly spoken about the need for more “binding coordination of economic policy... this requires that we adapt the treaty basis for economic and monetary union quickly in a limited and targeted way in order to ensure lasting stability for monetary union.” Full fiscal union was therefore some way off and Germany needed oversight before it could commit.

Rising euroscepticism and its effects were a hotly contested subject with both sides split on how much emphasis to place on it. It was likely that in the upcoming European Parliament elections the “protest vote” plus those who did not vote would form a considerable proportion of the electorate. The effect would then be compounded post-election by an inward looking Brussels fixated by an “irrelevant debate about the next Commission President”. Others thought that the threat was overplayed. The radicals were a fractured group of political parties. The National Front in France had nothing to do with Golden Dawn in Greece or UKIP in England. It was former Ambassador Thomas Matussek of the Alfred Herrhausen Foundation who identified the root cause of this in his closing address. There was a fundamental “lack of trust” between the electorate and their leaders and the system. The implication was that this was not the time for bold strides towards integration but to instead regain trust through leadership.

## **Conclusion**

Last year the conference was dominated by the new British policy of “repatriation followed by referendum.” This year, in the words of one British participant, “normal service has been resumed”. Words matter and the discussion had moved from a polarising topic of repatriation to areas of convergence in EU reform and subsidiarity. Some British participants identified the referendum as the “elephant in the room” and cautioned against underestimating its potential to disrupt events down the line. What was needed was a vigorous debate about the counterfactuals. What were the real alternatives to a reformed EU? What did the eurosceptics truly mean by “out”? Their ambiguity would surely count against them in the voting booth.

As Ambassador Wolfgang Ischinger put it in his dinner speech on the second night of the conference, “Putin has brought about leadership and purpose in the EU”. Another senior German participant suggested that Putin should be awarded the “Prix Charlemagne” for

the shot in the arm he had provided. Even the polls in the UK showed people were now more favourable to the EU since the Ukraine crisis.

For all the talk of leaving the EU, when it came to external threats like Russia, it was Britain who could be found in the front of the pack alongside Germany. Some German participants queried whether the UK was just “talking tough” but Simon Macdonald, the British Ambassador, countered these suggestions in his reply to Ambassador Ischinger’s dinner speech. Britain was ready to fight economically and he underlined that such a fight would have to be sustained for a long time. Both sides agreed that European unity had failed over foreign policy before in the Balkans and spectacularly over Iraq. Could European unity crack again? Or would this be the point when Germany showed leadership in foreign policy?

On the conference question, “Global Hub or Museum”, David Lidington, Minister for Europe, volunteered an answer on the opening evening. The participants had enjoyed pre-prandial drinks in the magnificent Gothic setting of Kings College Chapel and were seated in the neo-Gothic Hall when he used the example of Cambridge University to illustrate his point. The attendees of the 64<sup>th</sup> Königswinter had just experienced Cambridge in all of its architectural splendour, worthy of any museum. But Cambridge was also a hub: 90 Nobel Prizes had been awarded as a result of research conducted at the University. Cambridge then, offered a lesson for Europe in combining heritage with new ideas in an increasingly connected world. He went on to say that it was this shared heritage and the common values among the transatlantic community that must be defended. He reminded the participants of two significant anniversaries this year, a century since the outbreak of the Great War and a quarter century since the toppling of the Berlin wall. Much in the way of freedom, prosperity and security had been achieved in the last 25 years and we would have to work hard to protect this. Michael Roth, Minister of State for European Affairs at the Federal Foreign Office, provided the reply to David Lidington. He paid tribute to the close, pragmatic cooperation of the UK and Germany on issues such as Ukraine. Indeed that very morning he had been in London as part of a regular bilateral meeting of EU state secretaries. He underlined that the EU was not just about value for money but about values and quipped that he looked forward to “ever closer union” between the UK and Germany. The participants departed Kings College Cambridge eagerly awaiting next year’s conference, which, lest we forget, will take place in an election year in the UK.