

Washington wants economic reform in Europe

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As the new European Commission takes office today, there will be no better way for José Manuel Barroso, its president, to assert his authority than by pressing ahead with the Lisbon Strategy, the European Union's economic reform commitments.

Mr Barroso needs to convince the European Union member states to adopt these reforms to boost long-term economic growth. Without such measures, Europe's generous social welfare policies will be unsustainable. More important, with fewer economic resources at its command, Europe's diminished ability to engage internationally will confirm what many in the new Washington administration suspect: that the US should no longer attempt to accomplish its principal foreign policy goals through the transatlantic relationship.

The transatlantic economic relationship has remained largely insulated from the political tensions arising from the Iraq war and other issues. The US and Europe continue to trade and invest in each other's economies at a robust rate, and the US and the EU still exert joint leadership in the World Trade Organisation, the World Bank, the International Monetary Fund and other international institutions. So all is right with the world? Far from it.

The US and the EU confront economic challenges and ageing populations that will place health insurance, unemployment and pension schemes under strain. The US boosted competitiveness (in the 1980s) and tackled fiscal policy challenges (in the 1990s). The present added homeland security costs are likely to be manageable.

On the other hand, although the EU has shown it is capable of economic renewal, such as the 1992 single market plan and the introduction of the euro, the reform track record of Europe's big economies since the launch of the Lisbon Strategy is discouraging.

As suggested in a new study by the Atlantic Council of the US, if the EU is not able to achieve economic reforms, the already fraying transatlantic political partnership could begin to break apart. Europe is on probation in the eyes of George W. Bush's administration. True, the US maintains strong relationships with the UK, Italy and a few other long-standing EU members, while among the new, former-communist member states there are strong ties with the US based on memories of cold war solidarity. But many of these links are under strain.

Once-solid partners have clearly distanced themselves from US foreign policy (Spain), have decided to pull their troops from Iraq (Hungary), or appear to be disappointed with the terms of their ties to Washington (Poland). Add long-term

economic decline to contrariness, and this US administration - which knows it cannot go it alone - is likely to look elsewhere for allies in global policy.

There will increasingly be alternative partners with the requisite political and economic capital to help the US achieve its goals. With a faltering Europe, the US could turn towards China and India for political and security policy allies, as their global influence is likely to continue to strengthen. These emerging powers may not fully share the political and cultural traditions that have helped cement transatlantic co-operation but that will be less important if a more or less unilateralist US opts for ad hoc arrangements with these countries rather than binding alliances.

To ensure that a rules-based global trade and financial system continues, the US may decide to reach out to the Group of 20 developing countries, which includes emerging regional powers such as Brazil and South Africa, so that they have a meaningful stake in an orderly and just functioning of the international economy.

Can anything be done to preserve the transatlantic partnership up to 2020? While the US needs to bring its fiscal deficit under control to sustain its international leadership role, the key will be for Europe to make good on the reforms set out in the Lisbon Strategy.

Stimulating faster economic growth, which will require higher labour participation rates, is crucial if the EU is to acquire the wherewithal to maintain its position of joint global stewardship with the US. Without such a revived Europe, the unpalatable alternative is a US that has lost its balance, an inward-looking Europe and a rudderless international system.

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