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A Ship of Fools—Failing Harmonization and the Disregard of Principles of Finance

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The development of the EU according to the strategy Europe 2020 has encountered significant difficulties. It was caused in great part by the underestimation and in some cases total ignorance towards the principles of financial science. The paper discusses the absence of financial-law based point of view regarding the future development scenarios until 2020. Then the five goals set out by the strategy are examined. The critical state of finance in the EU shows the fruitlessness of all the harmonization efforts lately. The authors of fake statistics and fake misleading prognoses have not been brought to justice. The causes of the crisis have been wrongly identified. We are losing our wealth, which generations had labored to accumulate. We are actively giving up our civil rights and the security of our citizens to create a more pleasant environment for Saudi Arabia. During this effort we have contributed to the destruction of millions of lives in the Middle East. We are the only ones in the world still lending our trust to rating agencies that deliberately derailed the global economy in the pursuit of extra profit.

Keywords: Europe 2020 strategy, evaluation, harmonization, financial law, growth scenarios, headline targets, crisis management, synergies

Introduction

> Our world of today feels like a ship of fools en route to sinking, while the crew members keep convincing each other to accept the current order that is leading them to catastrophe. Much the same as in Plato's allegory of the Ship of fools as a sick state, the captain may be the tallest and strongest among the crew, but he is weak of sight and hearing and not particularly skilled at navigation. And the crew fight one another for control of the rudder, even though none of them is a learned helmsman. (Pauer, 2003, pp. 544-550)

The Ship of fools is an allegory used in occidental culture since ancient times. Plato used it in his reasoning against democracy. The centerpiece of the allegory is a ship without a captain, forcefully seized by insane and oblivious passengers. This mob, drunk on power, is capable of destroying anyone who would threaten its supposed interests. A navigator with knowledge of the stars and actual direction of a ship is conspicuously absent, but no one seems to be troubled by this situation (Steinbauer, 2014).

Is the situation really that dire? May the EU correctly be compared with Plato's sick state? Yes, we have great cause for concern, and yes, the pathos of the sick state allegory is entirely justified. We are currently wasting much of the wealth that previous generations had labored to accumulate. We are losing our civil rights and liberties that the generations past suffered and died to gain. We have relinquished the security of our citizens in order to create a more pleasant environment for Saudi Arabia; thus we have contributed to the

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destruction of millions of lives in the Middle East. We are the only ones in the world still lending our trust to rating agencies that deliberately derailed the global economy in the pursuit of extra profit.

The dictionary definition of harmonization states that it is the addition of chords to a melody according to the principles of harmony.[1] As per official government definition, harmonization aims at "a set of international legal provisions directed towards Member States, the purpose of which is to ensure that Member States accommodate their national legal systems to the requirements of the common provisions on harmonization".[2] The Europe 2020 strategy is, however, impossible to implement following the principles of harmony; indeed, it seems an absurd and infeasible plan. The history and present of the strategy, as well as the European semester, may be described as a bad idea undergoing an even worse implementation. Considering the limitations on the size of this contribution, this paper only focuses on particular important points, in order to offer a positive impulse for future stages of implementation.

On the Ship of Fools

We must begin the evaluation of the initiatives in question by an analysis of the narrative used by then-president of the Commission J. M. Barroso to introduce the Europe 2020 strategy. Europe is left with clear yet challenging choices. Either we face up collectively to the immediate challenge of the recovery and to long-term challenges—globalisation, pressure on resources, ageing,—so as to make up for the recent losses, regain competitiveness, boost productivity and put the EU on an upward path of prosperity ("sustainable recovery"). Or we continue at a slow and largely uncoordinated pace of reforms, and we risk ending up with a permanent loss in wealth, a sluggish growth rate ("sluggish recovery")[3] possibly leading to high levels of unemployment and social distress, and a relative decline on the world scene ("lost decade").[4]

A cursory glance at Figure 1 depicting the abovementioned scenarios will suffice to cast doubt on its authors' mental faculties. It is entirely unclear what values the axes of the graphs are meant to represent. The horizontal axis (X) indicates the passage of time, "years", and the vertical (Y) measures the scalar "output level". How is output level to be measured, and output of what? The dotted line represents economic growth before the crisis. The deceptive pre-crisis numbers were, however, influenced by the swelling of the infamous "mortgage bubble"—i.e., the overvaluation of mortgage investments' yields. How this trend could continue after said bubble had burst and the inaccuracy of economic growth prognoses had been exposed is not explained. Furthermore, the worst-case scenario is deceptively entitled "lost decade": In Slovakia, it is far from an overstatement to speak of a lost quarter-century. While it is true that nominal wages have risen to multiples of their original values, the real incomes of Slovak citizens have increased much less dynamically. Adjusting for inflation, only in 2007 were our wages higher than in the year 1989 for the first time, after almost two decades of transformation spanning the lives of an entire generation. According to Juraj Marušiak, analyst for

1 Retrieved from http://slovnik.azet.sk/pravopis/slovnik-sj/?q=harmoniz%C3%A1cia.

2 Retrieved from https://www.employment.gov.sk/sk/ministerstvo/medzinarodna-spolupraca/koordinaciasystemov-sz/koordinacia-harmonizacia.html.

3 Communication from the Commission *EUROPE 2020: A strategy for smart, sustainable and inclusive growth.* Consolidated version from 03/03/2010, quoted as of 27/12/2013. Available online: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52010DC2020&from=EN

4 Communication from the Commission *EUROPE 2020: A strategy for smart, sustainable and inclusive growth.* Consolidated version from 03/03/2010, quoted as of 27/12/2013. Available online: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52010DC2020&from=EN

the Institute of Political Sciences (Slovak Academy of the Sciences), the reasons for celebration lasted but briefly: In 2008 the global financial crisis hit and a period of sinking real wages ensued, effectively lasting until the end of 2011. Only in 2012 was the trend reversed, bringing economic growth. Marušiak continues: "Subjective welfare depends not only on material factors, but also on subjective feelings of injustice. Thus, it may happen that political upheaval and a potential rise of authoritarian regimes will not be caused by poverty alone, but to the same extent by influences such as corruption, the perception of impunity of the powerful, or fear for one's safety" (Marušiak, 2016).

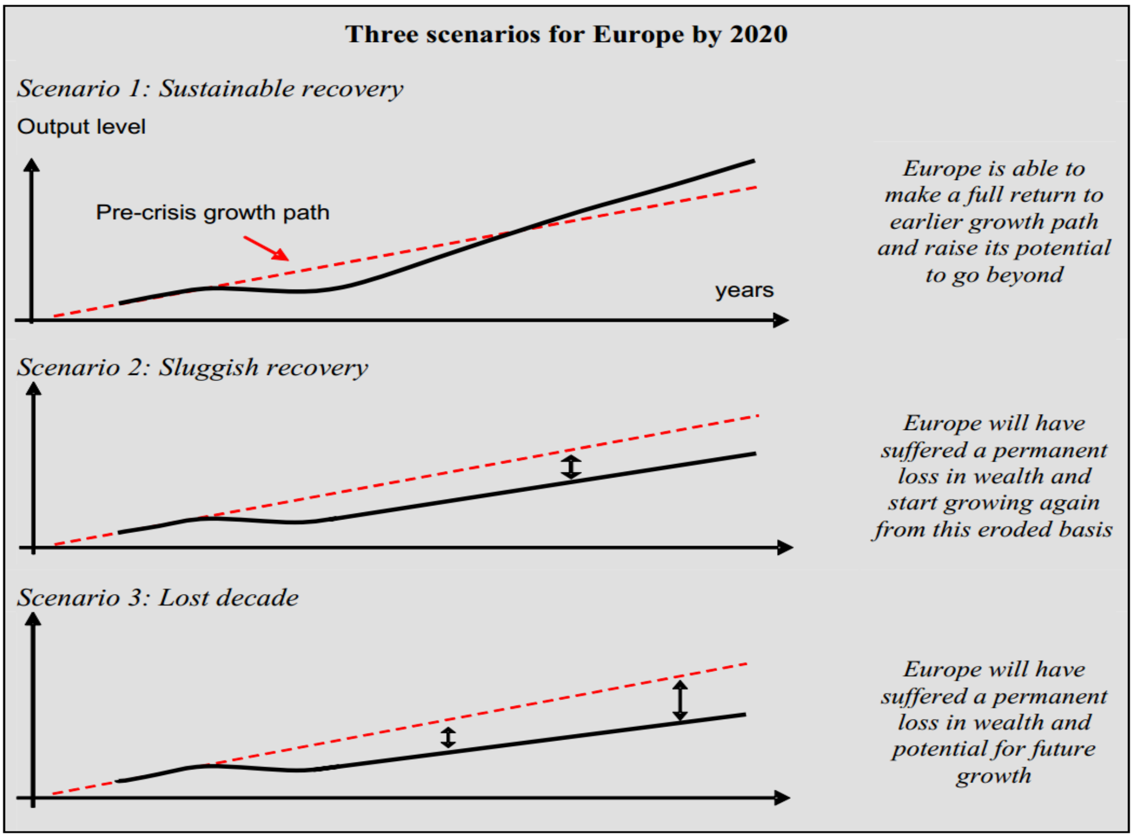

Figure 1. Three scenarios according to Strategy Europe 2020.[5]

We Know What We're Doing!

"I am not a fool"—almost any fool will say of himself. As the report of "Five presidents" entitled "Completing Europe's Economic and Monetary Union" states in its introduction:

> The euro is a successful and stable currency. It is shared by 19 EU Member States and more than 330 million citizens. It has provided its members with price stability and shielded them against external instability. Despite the recent crisis, it remains the second most important currency in the world, with a share of almost a quarter of global foreign exchange reserves, and with almost sixty countries and territories around the world either directly or indirectly pegging their currency to it. Europe is emerging from the worst fnancial and economic crisis in seven decades. The challenges of recent years forced national governments and EU institutions to take quick and extraordinary steps. They needed to stabilise their

[5] Communication from the Commission *EUROPE 2020: A strategy for smart, sustainable and inclusive growth.* Consolidated version from 03/03/2010, quoted as of 27/12/2013. Retrieved from http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52010DC2020&from=EN.

> economies and to protect all that has been achieved through the gradual and at times painstaking process of European integration. As a result, the integrity of the euro area as a whole has been preserved and the internal market remains strong.[6]

No one seems to notice that recent developments are regarded very differently from outside the EU. According to Kumar (2015) "The crisis of the Eurozone is an economic crisis caused by the collapse of financial institutions, extensive sovereign debt and the growing disparity between the volatility and return-on-investment value of state bonds, faced by multiple European countries. The European sovereign debt crisis started in 2008 with the collapse of Iceland's banking system. After that, during the year 2009, the crisis spread to ireland, Greece and Portugal. The crisis has shaken markets' trust in European economies". According to many authors outside Europe, the crisis of the Euro began in 2008 and goes on to this day, with no end in sight for the forseeable future.

The epicenter of the current global financial crisis can be traced to the USA. Accodring to official explanations published by the US Government and the Federal Reserve, policies had been incorrectly implemented due to human error. Leading employees acted without due regard for economic reality. Eight years after the fact, however, the steps taken by relevant actors may be interpreted in retrospective: The alleged misconduct by Fannie Mae and Freddie Mac executives have proven extremely advantageous in the medium term. Thanks to these decisions the United States effectively exported its own toxic assets to the entire globe, while minimizing the domestic ramifications of the mortgage bubble's collapse. This reality is further attested to by the fact that the persons responsible for the direction of Fannie Mae and Freddie Mac received outrageously high severance benefits and have since been cleared of all charges. Fannie Mae is not a private corporation in the strict sense, however; it serves a function analogous to a state housing development institute (fund). Additionally, Fannie Mae never went bankrupt and has been reporting record profits recently. Together with Freddie Mac it controls 90% of the US mortgage market.[7]

In addition to mortgage troubles, a problem with credit card debt has emerged, incorporating consumer debts usually ensuing from automobile and other purchases, student loans etc. After the mortgage market's failure households preferred to tend to housing problems and defer repayments of such consumer debt. Despite the enormous amount of credit cards issued, the total amount in default on credit card debt is lower than mortgage defaults in total, while still weighing in at approx. one trillion USD. The two abovementioned quasi-government institutions Fannie Mae and Freddie Mac has an important role to play, in buying up receivables on loans from primary lenders (alongside mortgages, car leases, student loans, credit card consumer loans and others were subject to such resale). The fact that lending was thus backed by the state has proven critical: Primary, immediate lenders had shed the common fears for their clients' solvency—the government would reimburse them for their unpaid receivables regardless.

Key to bloating the bubble was a legal system supporting the transfers of assets between banks and relevant special-purpose vehicles (SPVs)—Fannie Mae, Freddie Mac etc. Thus banks were able to bundle

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[6] *Completing Europe's Economic and Monetary Union,* available online: https://ec.europa.eu/priorities/sites/beta-political/files/5-presidents-report_en.pdf.

[7] Integral to the New Deal program was the creation of the Federal National Mortgage Association, shortened to Fannie mae for practical reasons, the purpose of which was to support American housing in the long term. Fannie mae as a federal agency bought up mortgages backed by the Federal Housing Administration and later also the Veteran administration, from US lending institutions. In 1968 Fannie Mae was privatized, in 1970 Congress enabled it by law to purchase common mortgages (SÍLEŠ, 2010).

subprime mortgages of dubious quality. Such bundles were further bundled into even larger collections, later transferred onto an SPV founded for this very purpose. The SPV issued collateralized debt obligations (CDOs) as financial instruments based on the original dubious assets, thus removing them from the relevant banks' balance sheets. After being assigned a rating by rating agencies, the CDOs were sold to investors by way of intermediaries working on commission to ensure the marketing and sale of such instruments (Okálová, 2010).

CDOs belong to a line of product innovation by US securities markets, being initially highly regarded and lauded by the Federal Reserve. They are so-called asset-backed securities, offering creditors the option to repossess debtors' property (usually real estate) in case of default. However, the underlying principle was the accumulation of various low-quality bonds and receivables (low-quality mortgage bonds, receivables on credit card debt in default etc.) into apparently sophisticated bundles giving the impression of promising investments. Additionally, these instruments were awarded AAA ratings by rating agencies. As foreign banks and investors were tempted to purchase CDOs en masse, the US real-estate market spilled over to the supranational, global economy. Based on the generous ratings, CDOs were bought up by skilled and informed investors, and those with no knowledge of their content alike (Švihlíkova, 2008).

According to documentation accompanying the Europe 2020 strategy[8] the EU has taken the lessons of the 2008 crisis to heart: "The 27 EU economies are highly interdependent: the crisis underscored the close links and spill-overs between our national economies, particularly in the euro area. Reforms, or the lack of them, in one country affect the performance of all others, as recent events have shown; moreover, the crisis and severe constraints in public spending have made it more difficult for some Member States to provide sufficient funding for the basic infrastructure they need in areas such as transport and energy not only to develop their own economies but also to help them participate fully in the internal market. Coordination within the EU works: the response to the crisis showed that if we act together, we are significantly more effective. We proved this by taking common action to stabilise the banking system and through the adoption of a European Economic Recovery Plan. In a global world, no single country can effectively address the challenges by acting alone; The EU adds value on the global scene. The EU will influence global policy decisions only if it acts jointly. Stronger external representation will need to go hand in hand with stronger internal co-ordination".

It must be stated that we have accepted the wrong conclusions about the crisis. Further tight regulation and enormous financial aid given to the cartel of private banks have proven fundamentally ineffective. The USA, unlike Europe, moved in the opposite direction, allowing certain banks to fail, increasing the sovereign debt ceiling and effectively nationalizing Fannie mae and Freddie Mac. The US has since escaped the crisis, while the EU hopelessly wallows in it from 2010 to this very day.

Worst Practice

Let us analyze, then, what we are doing wrong, by taking a closer look at the Europe 2020 startegy's headline targets: The Commission hopes to strengthen key policies such as the internal market, budget creation and the external economic policies of the EU in order to meet the stated main goals of the strategy. An integral part of the strategy consists of operational plans meant to ensure that the key policies are fully harnessed to head towards the strategy's fulfilment. There are five headline targets set by the Europe 2020 strategy:

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[8] Communication from the Commission *EUROPE 2020: A strategy for smart, sustainable and inclusive growth.* Consolidated version from 03/03/2010, quoted as of 27/12/2013. Available online: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52010DC2020&from=EN.

(1) Increase employment levels.

(2) Invest 3% of EU GDP into Research & Development.

(3) React adequately to climate change.

(4) Increase mean education levels of EU citizens.

(5) Reduce poverty and social exclusion.

Ad 1)—*Employment.* The goal is to raise the employment rate of the population aged 20-64 from the current 69% to at least 75%, including more women, senior employees and migrants to the workforce.

It is to be noted that the first headline target definition already contains inherent contradictions: The Europe 2020 strategy operates with the term *employment rate* as opposed to the common *unemployment rate*. The reality is that the percentage of employed citizens has decreased dramatically since 2010. Raising the employment rates of the current populaton and increasing incorporation of migrants into the workforce are contradictory agendas: the more migrants included, the less potential room for the inclusion of current populations remains. Let us analyze, then, the unemployment rate during the period of declared striving towards higher employment rates. Figure 2 depicts the development of unemployment rates in the EU 18,[9] the EU 28,[10] Japan and the USA. It is painfully obvious that unemployment has been on the rise since 2010, *not accounting for the influx of new migrants*.

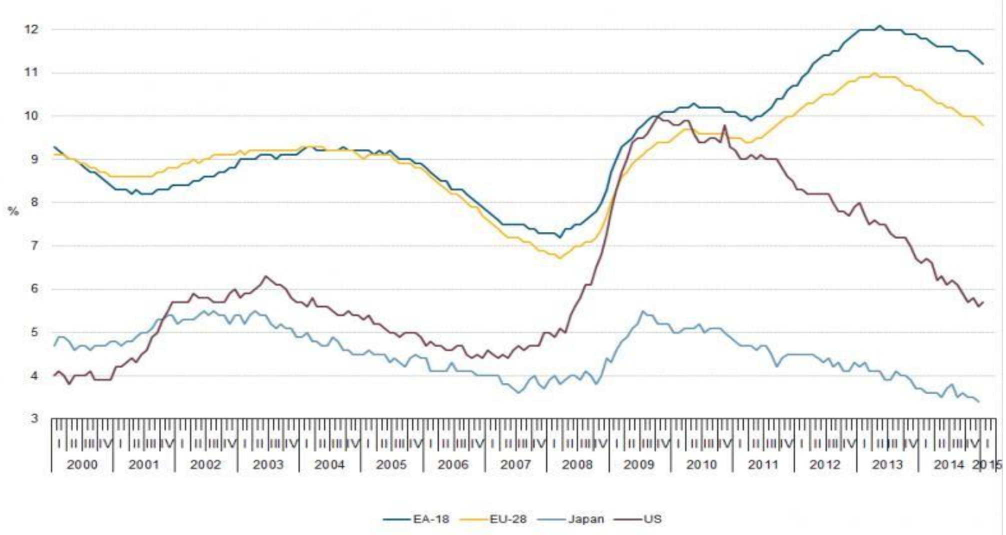

Figure 2. Employment comparison.[11]

Ad 2)—*Research & Development*. It remains unclear what scientific and/or technological fields are to be researched and developed with the aid of investment equal to 3% of the EU's GDP. For any research and development initiatives to remain beneficial to the economy, industrial implementation of the technology created must continuously be achieved. Much of the results of European research efforts remains exclusively

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[9] Belgium, Germany, Estonia, Ireland, Greece, Spain, France, Italy, Cyprus, Latvia, Luxembourg, Malta, the Netherlands, Austria, Portugal, Slovenia, Slovakia and Finland.

[10] E18 Member states and Bulgaria, the Czech Republic, Denmark, Lithuania, Hungary, Poland, Romania, Sweden and the United Kingdom.

[11] Source: Eurostat. Retrieved from http://ec.europa.eu/eurostat/statisticsexplained/index.php?title=File:Unemployment_rates_EU-28_EA-18_US_and_Japan_seasonally_adjusted_January_2000_January_2015.png&oldid=223344

implemented offshore, benefiting foreign and global players while having a negligible positive effect on EU economies. As for the percentage of domestic product and incomes invested back into research, some increase has been achieved, but the target levels still remain to be met. In Slovakia, the situation is that much worse, as illustrated by Figure 3.

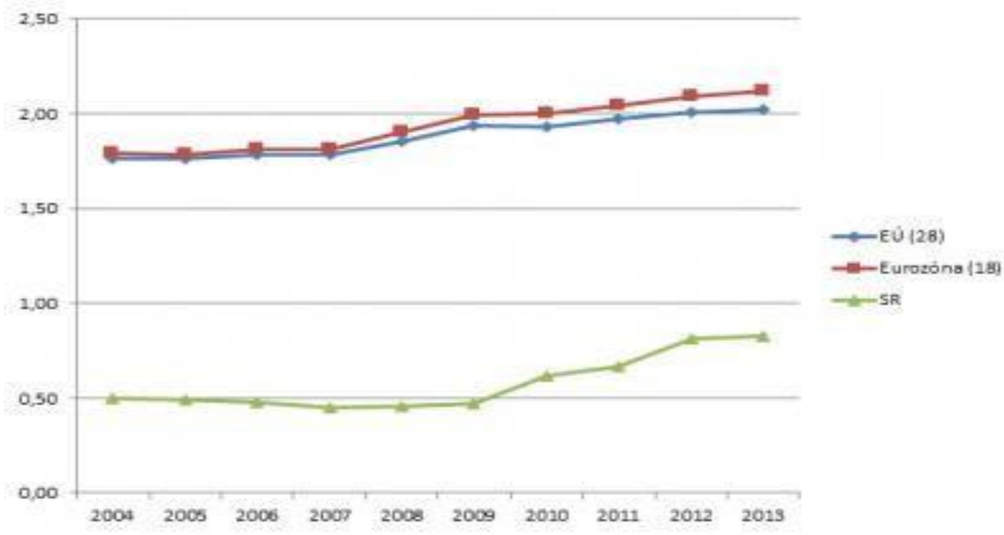

Figure 3. R & D comparison.[12]

Ad 3)—*Climate change and energy sustainability*, the requirement to meet the 20/20/20 goals with regard to climate and energy economics: To reduce greenhouse gas emissions by a minimum of 20% compared to 1990 levels, increase the ratio of energy produced from sustainable sources to total energy consumption by 20%, and to increase energy efficiency by 20%. Of all the stated headline targets this one is to be viewed as the least well-considered and most inherently contradictory. The reduction of emissions does in no way contribute to our industry while the competition refuses to abide by current global conventions regarding emissions. Additionally, such ambitions usually results in attempts by manufacturers to circumvent the relevant legislation and/or to obfuscate test results, as has been demonstrated in the Volkswagen case. Furthermore: sustainable energy sources tend to be less efficient than unsustainable ones, therefore the only way to increase their representation in total consumption and simultaneously increase efficiency is a cutback on industrial production. To illustrate said points, statistics of greenhouse gas emissions may be contrasted with statistics of industrial output of relevant economies. Figure 4 represents the development of industrial production, while emissions trends are shown by Figure 5.

[12] Source: Eurostat. Retrieved from http://ec.europa.eu/eurostat/statisticsexplained/images/6/62/Europe_2020_Headline_indicator_R%26D.png.

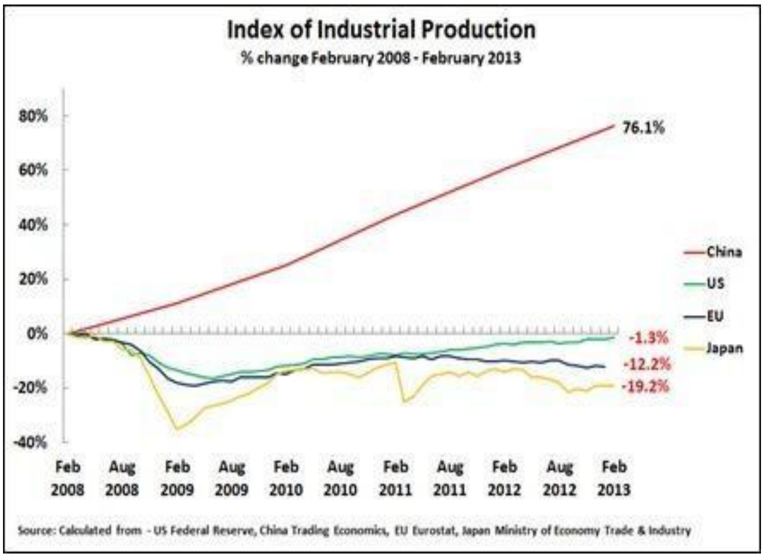

Figure 4. Industrial production comparison.[13]

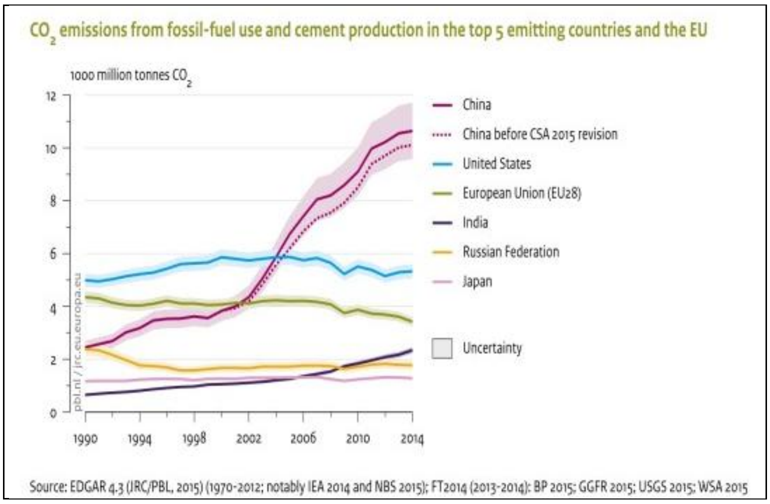

Figure 5. Emissions comparison.[14]

[13] Source: Calculated based on US Federal Reserve, China trading economics, Eurostat, Japan Ministry of Economy, Trade and Industry data.

[14] Source: EDGAR emissions database, available online: http://edgar.jrc.ec.europa.eu/.

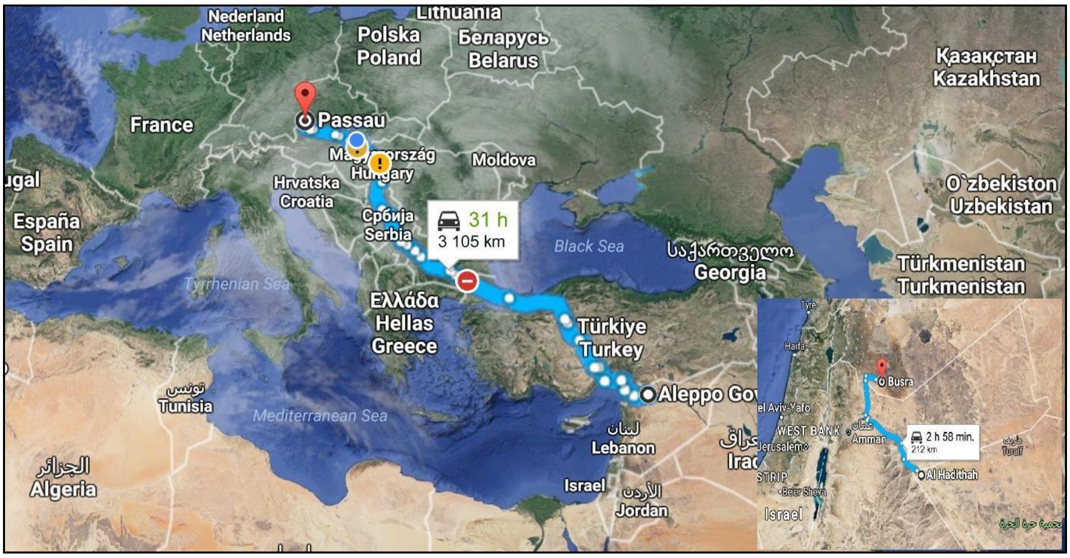

Figure 6. Travel route comparison.[15]

Supposing that global warming/climate change is indeed caused mainly by anthropogenic CO_2 emissions, it is obvious that the EU does not belong to the largest emitters. Since it is certain that reductions of emissions go hand-in-hand with reductions of industrial output, we would be tilting at windmills in hoping to achieve all of the relevant goals and remain competitive, as long as our influence over emissions of Asian countries is negligible. Europe’s contribution to climate change also remains unknown, as no scientific studies have dared to calculate whether – and to what extent – reducing emissions within the EU would potentially impact climate.

Ad 4)—*Raise the education levels of EU citizens.* The percentage of the population prematurely leaving elementary education is to drop under 10%, and the percentage of citizens aged 30-34 with tertiary (university) education should increase from 31% to 40%. I believe this point requires little further commentary: as has been demonstrated, the major centers of research and innovation have moved outside the EU. As the number and intensity of industrially implemented R&D activities in Europe declines, the need for highly educated workers will also decline. Generally speaking, it is beyond frustrating to complete 15+ years of education, only to work a job that requires no more than a few days’ worth of practice.

Ad 5)—*Stop social exclusion and reduce poverty*. To rescue at least 20 million of EU inhabitants from the risk of poverty and social exclusion, a process of separation of individuals from society at large. The causes of individuals’ personal situations leading to social exclusion include demographic changes, financial burdens on households, income inequality (including its regional aspect) and unemployment. Social inclusion as the polar opposite represents the process of integration of formerly excluded communities into the larger society, including their active integration in the day-to-day social, economic, political and cultural life.[16]

EU foreign policy and military interventions by NATO must be regarded as additional causes of social exclusion. The “Arab Spring” began in 2011; the whole Western world celebrated the imminent fall of stable authoritarian regimes in the Middle East, so rebels were given political, material and even military support. Several years later, the European migrant crisis has emerged as a result, producing unprecedented numbers of

[15] Source: created using google maps: https://www.google.sk/maps/.
[16] Communication from the Commission *EUROPE 2020: A strategy for smart, sustainable and inclusive growth.* Available online: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX: 52010DC2020&from=EN.

socially excluded inhabitants.

Let us examine what Middle Eastern migrants go through on the way to their exclusion from society in the EU: Figure 6 illustrates the road from Syria to the German border, totaling 3,105 km, and the distance of mere 212 km from the Saudi border. Saudi Arabia has the capacity to accommodate enormous numbers due to the annual mass pilgrimage to Mecca (hajj). If the safety and well-being of Syrian migrants is so paramount, why do we not rent accommodation capacities, e.g., millions of tents from the Saudis? Instead, migrants are currently forced to travel thousands of kilometers through dangerous territories with the help of smugglers; would it not be more efficient for the EU to receive payments from refugees directly, instead of the money being spent on the services of migrant smugglers? If we have a substantial portion of NATO naval capacities in the Mediterranean, why do we not organize transport by sea directly from the Syrian or neighboring ports? Why do we not even perform basic protection of the Schengen border by checking the identities of new arrivals? The reaction of the EU is inexplicable. If we are to be viewed as reasonable partners by the community of nations, our borders must exist in fact, not only in theory. Arguments based on migrant interests are preposterous in this regard—on the contrary, border protection is an eminent interest of the migrants themselves, not to be accompanied by persons who forced them to flee their homes in the first place, so that they may infiltrate the EU. US media commonly cites inadequate border protection as the cause of the terrorist diaspora within the EU.[17]

Social exclusion is the process of separation of individuals from majority society. According to Aristotle: “He who is unable to live in society, or who has no need because he is sufficient for himself, must be either a beast or a god”. The normal human being as an individual is unable to really separate themselves from society, such a prediction is preposterous; instead, a part of society is excluded as a whole and will start functioning as a parallel society.

Conclusion

We may conclude that Europe has been heading in the wrong direction since the adoption of the Europe 2020 strategy, in all the fields targeted by its main initiatives, such as increasing employment, investing 3% of EU GDP into R&D, combating climate change, raising education of EU citizens and stopping poverty and social exclusion. It is becoming increasingly obvious that basic premises of financial law and science had been severely underestimated, if not ignored in outlining the scenarios of the EU’s development up to 2020. Due to the limited extent of this paper, only a few critical issues are explored with the intent to bring about a deeper analysis from the financial standpoint. The varying progress in fulfilling goals for the main target fields shows that harmonization will bring about synergy and will be successful, as long as Member states as well as the EU itself implements the principles of financial law with respect to mutual interests. Changes so conceived will create the potential to restart and continue growth in the Member states, and the union.

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