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The Differentiation Paradox of European Integration: Why Going it Alone Produces Suboptimal Results¹

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Abstract

Differentiation is not only a design feature of European integration, it is also a Member State strategy to overcome preference divergence. However, putting together an optimal group is difficult: Either the resulting club lacks the capacity to produce the club good efficiently; or differentiation attempts lead to an equally suboptimal outcome of a club too large and too heterogeneous to be effective. This paper develops an explanation of this *differentiation paradox*. When an avant-garde group proposes differentiation, the presence or absence of its go-it-alone power determines the outcome. The former leads to suboptimally large clubs due to the bandwagoning dynamic that produces a cascade. By contrast, the absence of go-it-alone power triggers a blockade and results in suboptimally small clubs. This actor-centred approach to differentiated integration is tested by analysing the establishment of Permanent Structured Co-operation in security and defence, which declined from an ambitious idea into a diluted reality.

Keywords: European Union; differentiated integration; go-it-alone power; club theory; permanent structured co-operation

Introduction

Differentiation in its various designs, such as the creation of a ‘multi-speed Europe’, a ‘Europe à la carte’, or a ‘variable geometry approach’ (Stubb, 1996), has become the *modus vivendi* for EU Member States, which seek to accommodate differences in willingness and capabilities as well as to prevent blockades when negotiating the EU’s design and scope (Kelemen *et al.*, 2014; Leruth *et al.*, 2019b; Leuffen *et al.*, 2013). Scholarship has taken an ambiguous stance on differentiation, which is a ‘double-edged sword’ for some (Chopin and Lequesne, 2016).

One group of researchers emphasizes the potential of horizontal differentiation for both the avant-garde and integration laggards – that is, of the creation of ‘clubs within the club’ (Ahrens *et al.*, 2005), to overcome preference heterogeneity regarding future integration (Jensen and Slapin, 2012; Kölliker, 2001; Lord, 2015; Neve, 2007; Schimmelfennig and Winzen, 2020). Another camp of scholars is more sceptical. Driven by the Brexit, an instance of differentiated *disintegration* (Leruth *et al.*, 2019b), they point to a major risk inherent to differentiation – the driving apart of the EU (Leruth *et al.*, 2019a). Especially when it reaches the area of the rule of law, differentiation endangers the normative basis of the European project (Kelemen, 2019) and could encourage further disintegration (Kelemen, 2021).

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However, even differentiation sceptics seem to acknowledge the existence of a relatively promising type of differentiation. The method of creating a multi-speed Europe, for example the establishment of an enhanced co-operation, builds on the idea that ‘common objectives are pursued by a group of EU countries both capable and willing to advance, it being implied that the others will follow later’.² Put differently, this type of horizontal differentiation is supposedly non-permanent and conducive to future convergence while being a valuable tool for the avant-garde to overcoming present preference divergence (Kroll and Leuffen, 2014; Leruth *et al.*, 2019a, p. 1392). To set this convergence mechanism in motion, the avant-garde needs to create a club of the capable and willing, which is attractive enough for the outsiders to invest in convergence and attempt to join the club at a later stage. Yet, why do we rarely observe this mechanism in practice?

This paper argues that an avant-garde’s horizontal differentiation strategy is unlikely to result in clubs of the willing and capable. For the avant-garde, an *optimal club* is small and homogeneous enough to agree on a common, ambitious agenda while at the same time large and capable enough to produce club goods efficiently. To create such an optimal club, the avant-garde needs to convince these integration-sceptical laggards, whose capabilities are needed to achieve the desired goals, while excluding those who lack capabilities and willingness. However, horizontal differentiation tends to result in *suboptimal clubs* that are either too small and lacking capabilities or too large and heterogeneous in ambition to provide the club goods efficiently. Either most of the laggards join right away, which creates a suboptimally large club lacking ambition, or none of them does, which leaves the avant-garde with a suboptimally small club lacking capabilities.

This *differentiation paradox* is rooted in go-it-alone power (Gruber, 2000). If an integrationist avant-garde possesses this power, their differentiation attempt generates negative externalities for the laggards. When the first laggards decide to join the initiative, this increases the costs of staying outside. Consequently, even the integration-sceptic laggards with high adaptation costs join the club one after the other – a cascade that results in a suboptimally broad membership. By contrast, if the avant-garde lacks go-it-alone power, differentiation produces no negative externalities for the laggards, and they will not join the initiative. The avant-garde is left on its own, and a resulting club would be suboptimally small.

I engage in a theory-testing process-tracing (Beach and Pedersen, 2013) of the recent activation of Permanent Structured Co-operation (PESCO) to test the paper’s argument. PESCO is a most likely case for the convergence mechanism envisaged by concept of a multi-speed Europe. As a form of enhanced co-operation customized for the area of defence, PESCO was designed to allow a group of willing and capable states to move ahead in centralising their defence and military planning activities (TEU, Art. 42(6)). This case provides temporal within-case variation, which cannot be explained by existing approaches focusing on differences across issue areas (Kölliker, 2001; Schimmelfennig and Winzen, 2020).

In the first phase (2007–16), an avant-gardist group of EU Member States repeatedly tried to activate PESCO. However, as the avant-garde lacked go-it-alone power, the laggards, including the United Kingdom (UK), blocked each attempt. As a result, European

²This definition could be found in the EUR-lex glossary until April 2021. It is still available at https://web.archive.org/web/20090214194351/http://europa.eu/scadplus/glossary/multispeed_europe_en.htm, accessed on 28 October 2021.

defence co-operation fragmented into various minilateral frameworks outside the EU treaties. In the second phase (2016–17), activating PESCO was successful. Twenty-five out of 27 Member States formally joined the avant-garde's initiative in a veritable cascade, among them PESCO's most pronounced critics. Given the UK's decision to leave the EU and the election of NATO-sceptic US President Donald Trump, the avant-gardists' newly acquired go-it-alone power altered the outcome – but the avant-garde ended up with a diluted and inclusive PESCO.

This paper adds to EU integration literature by introducing an actor-centred perspective to the analysis of differentiation. It treats differentiation as a Member State *strategy* (Jensen and Slapin, 2012) and examines the impact of go-it-alone power on its – suboptimal – outcomes. The avant-garde's possession of go-it-alone power determines whether a club generates negative externalities and induces the outsiders to join. However, independently of whether an avant-garde possesses go-it-alone power, threatening with exclusion is unlikely to result in clubs with willing and capable members. Such suboptimal clubs will not provide incentives for outsiders to invest in convergence, as implied by the multi-speed Europe concept. Instead, from the perspective of the avant-garde, going it alone results in suboptimal clubs characterized by diluted ambition or a lack of capabilities.

The following section theorizes the differentiation paradox and develops the causal mechanism with its two pathways to suboptimal clubs. The two pathways are then tested in the third and fourth sections by analysing the genesis of PESCO. The conclusion discusses the implications of the differentiation paradox for European Integration.

I. Explaining Suboptimal Clubs

Member State preferences on further integration in a given policy area often diverge. Interdependence can be asymmetric and functional pressure unevenly distributed, making integration unattractive for some Member States (Schimmelfennig, 2016), politicization processes (Hooghe and Marks, 2009) and the emergence of increasingly autocratic governments (Kelemen, 2019) can drive Member States to resist European integration. Such preference divergence accounts for outcomes of horizontal differentiation – be it in the form of opt-outs, opt-ins, or multi-speed approaches (Kelemen *et al.*, 2014; Leruth *et al.*, 2019b; Leuffen *et al.*, 2013). Especially the latter variant, positive horizontal differentiation, for example in the form of enhanced co-operation among a group of willing and capable Member States, is seen to be an effective way to overcome preference heterogeneity, offering 'the option for some Member States to move forward without affecting the current pace of integration' (Leruth *et al.*, 2019a, p. 1392, Kroll and Leuffen, 2014).

However, positive horizontal differentiation in the sense of engaging in deeper co-operation among a group of willing and capable Member States is not always supplied when there is a demand for differentiation (Kroll and Leuffen, 2014; Schimmelfennig and Winzen, 2020). Only in three of the nine cases Kroll and Leuffen (2014) have analysed, the attempt to create an enhanced co-operation was successful, while uniform integration or an unchanged status quo was the result in the other instances. Current scholarship draws on Kölliker (2001) to explain such variation through the properties of the respective good to be produced. Enhanced co-operation tends to be successful when it has

neither positive nor negative externalities on the outsiders. Only when externalities are neutral a multi-speed approach tends to be stable.

I build on these works to further scrutinise the mechanisms that determine whether a multi-speed approach can be a way for a group of Member States to produce the desired club good efficiently and stimulate future convergence. While the type and external effects of the good explain variation across issues, I propose an actor-centred and power-based approach to explain the dynamics that emerge when a group of Member States pursues the strategy of moving ahead alone *in a given issue area*. Holding the issue area and thus the type of good constant requires the inclusion of actors and their power into previous explanations based on club theory (Ahrens *et al.*, 2005; Kroll and Leuffen, 2014; Schimmelfennig and Winzen, 2020).

In general, the efficient production of *club goods*, which are ‘excludable and subject to some rivalry in the form of congestion’ (Sandler and Tschirhart, 1997, p. 336; Kölliker, 2001), depends on the membership constellation. Every additional member of a club reduces the cost of the jointly produced good while simultaneously consuming parts of it (Buchanan, 1965). Therefore, for any given sub-club within the EU, the integrationist avant-garde needs to find the optimum membership, in which the marginal benefit of including an additional member equals the marginal cost. At the same time, however, each laggard calculates the benefits of participation and the costs of joining the club (Jensen and Slapin, 2012).

Thus, pursuing a strategy of positive horizontal differentiation implies optimizing the *size of the club* – that is, the club composition along two dimensions. The first comprises the members’ capabilities to produce the club efficiently. The second is their willingness to do so. The interdependent avant-garde seeks to include the optimal number of capable members – those possessing the capabilities and willing to help produce the good. However, integration-sceptic laggards are only willing to join when the benefits of participation exceed the costs. If the resulting club is either too small or too large, it cannot efficiently fulfil its founding purpose. A club too large is a group that is too heterogeneous to be ambitious and thus unable to agree on how to produce the club good. A club too small is a group of states that lacks the capabilities to efficiently exploit economies of scale, which endangers the production of the club good (Snidal, 1994).

The Adverse Effects of Go-it-Alone Power

The avant-garde needs to incentivize the capable while keeping out those who would cause congestion and the dilution of standards and ambition to optimize the trade-off between the cost and benefits of inclusion (Thompson and Verdier, 2014). However, in light of asymmetric interdependence or politicization, the members of the avant-garde often need to convince the capable laggards to join their club to reap economies of scale. How do you convince states to join in a co-operative effort that is detrimental to their utility?

For the avant-garde, the answer lies in moving ahead among themselves and demonstrating their *go-it-alone power* (Gruber, 2000) – their ability to cause negative externalities to the outsiders. What convinces the laggards to integrate is not ‘the prospect of mutual gain’ but the losses of being excluded from co-operation altogether (Gruber, 2000, p. 47). Consider the example of market integration through standard-setting. Going it alone, an avant-garde agrees to integrate its markets and introduce a common standard, thus

erasing the non-cooperative status quo from the set of feasible alternatives for the laggards (Gruber, 2000, p. 39). Even though the integration-sceptics would prefer the non-existence of standards, they are now confronted with a binary choice. They either adhere to the undesired standard and can export their goods into the avant-gardist states or remain outside the institution and lose market access. When the avant-garde possesses go-it-alone power – that is, when its market is of great importance to the laggards – the latter's costs of exclusion will exceed their adaption costs, and they will join the institution. Thus, integrating their policies with the avant-garde might be detrimental to the laggards' utility compared to the unregulated status quo. However, the status quo is no longer achievable and joining is better than being cut off.

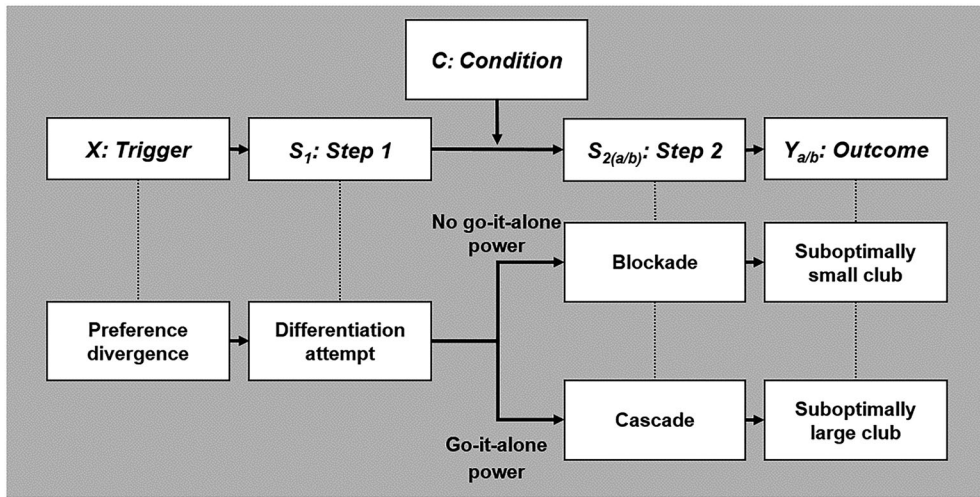
This sounds like good news for the avant-garde. However, there are two significant caveats to going it alone. The first is related to the impact of the proposed club on the laggards. A club needs to cause negative externalities if it is to exert pulling force and induce some laggards to integrate their policies against their original preferences (Kölliker, 2001; Schimmelfennig and Winzen, 2020). These negative externalities, more than anything, depend on the membership constellation of the proposed club. However, when the avant-garde lacks go-it-alone power, the sceptics are unlikely to join the proposed institution. Returning to the standard-setting example, the laggards are not likely to abide by the standards proposed by the avant-garde if there are other, unstandardized markets available. So, without additional members, the avant-garde is unlikely to assert itself and impose its preferred standard on the world market, which is likely to retaliate. Therefore, a suboptimally small club will result when the avant-garde announces its intention to move ahead without the power to generate negative externalities for any laggards.

The second caveat relates to the 'bandwagoning dynamic' inherent in go-it-alone power (Gruber, 2000, p. 47). The costs of exclusion for an outside state increase with the size of the membership of an institution. The more states join the avant-gardist project, the higher the negative externalities for those staying outside. Consider, for the last time, standard-setting. The more states share a minimum standard for a particular good, the fewer export possibilities remain for a state that does not comply with this standard: its outside options are often substantially reduced. In addition, heterogeneous Member States are likely to diverge in their susceptibility to exclusion and adaptation requirements. Taken together, whenever the integration-sceptic state with the lowest adaptation cost to cost of exclusion ratio decides to join the avant-gardist project, this generates additional costs of exclusion for the remaining outsiders and induces the next in the ranking to participate (Gruber, 2000, p. 46, see, Jensen and Slapin, 2012, for the opposite case of an opt-out cascade). This bandwagoning dynamic of laggards joining the avant-garde results in a suboptimally large club.

The Differentiation Paradox – A Causal Mechanism

When EU Member States try to achieve an optimal membership structure by moving ahead alone, they are fall victim to the differentiation paradox: Whether the avant-garde possesses go-it-alone power or not, the outcome is a suboptimal club. Figure 1 depicts the causal mechanism, which splits into two pathways. This section describes the causal logic and the *observable manifestations* of each step.

Figure 1: The Differentiation Paradox



The *trigger* (X) of the differentiation paradox is preference divergence concerning further integration. Two groups form, those willing to integrate (avant-gardists) and those reluctant to do so (laggards). Positional characteristics (such as geographic exposure) and domestic factors (such as competitiveness and politicization) are the sources of the preferences in question (Moravcsik, 1998, p. 26; Biermann *et al.*, 2019; Hooghe and Marks, 2009). We should observe Member State representatives voicing conflicting preferences.

As a *first step* (S_1), the group of avant-gardists select horizontal differentiation as the strategy to overcome resistance to further integration. In so doing, they face a problem when seeking to achieve the optimal size for their club. Accordingly, the avant-garde is theorized to make a differentiation attempt, announcing its willingness to create a club to the laggards. We should observe the avant-gardist group of Member States actively pushing for differentiation and voicing their willingness to move ahead while inviting the laggards to join them.

Conditioned (C) by the avant-gardists' possession or otherwise of go-it-alone power, the mechanism breaks down into two pathways. We can determine the avant-garde's go-it-alone power in a specific issue area, considering their collective autarky and non-reliance on co-operation with the laggards. At the same time, however, their go-it-alone power depends on the laggards' inability to reach their governance goals when cut off from collaboration.

If the avant-garde lacks go-it-alone power, the proposed club does not pose a risk of negative externalities to the laggards, and the *second step* will consist of a blockade (S_{2a}). Two observable implications are conceivable. First, responding to avant-gardist pressure, the laggards try to improve their position by creating outside options. Second, the avant-garde cannot formally integrate within the EU treaties and looks for informal solutions to mitigate interdependence. The *outcome* (Y_a) will be a suboptimally small club that lacks the capabilities to produce the club good efficiently.

If, on the contrary, the avant-garde possesses go-it-alone power and the differentiation attempt causes negative externalities, a cascade (S_{2b}) will follow. The integration-sceptic state with the lowest cost ratio will join the avant-garde. This leads the next state in the ranking to reconsider its resistance until even the most sceptical states can no longer refuse participation. This cascade and the effect of go-it-alone power can be observed when laggards voice their discontent with the avant-garde's initiative but eventually decide to join one after another despite this expressed preference. This cascade's *outcome* (Y_b) is a suboptimally large club, which prevents the avant-garde from reaching its envisaged level of attainment.

Method and Data

The following two sections present a theory-testing process-tracing (Beach and Pedersen, 2013) of a typical attempt to create a club within the club. The analysis shows that every part of the hypothesized causal mechanism was present in the PESCO case. While 'no claims can be made [...] about whether the mechanism was the only cause of the outcome', successful process-tracing allows for a high degree of internal validity of the theoretical argument, which then stands for falsification in other cases (Beach and Pedersen, 2013, pp. 3, 15). Holding the policy area constant, I analyse temporal within-case variation in PESCO's genesis in two phases, which lends itself to a quasi-experimental design: (1) PESCO's persistent blockade between 2007 and 2016 and (2) the cascade leading to its almost uniform establishment between 2016 and 2017.

The analysis draws on legal documents from European institutions for the relevant period from 2007 to 2017, complemented by the 54 working documents of European Convention Working Group VIII on 'Defence', issued between 2002 and 2004, to verify the assumed Member State preferences on PESCO. Moreover, I traced the positions of the EU's most powerful Member States, Germany, France, Italy and the United Kingdom, by analysing all publicly available government documents and speeches, parliamentary debates, and interpellations mentioning PESCO (2007–17). In addition, I examined a text body of over 90 newspaper articles to account for each Member State's timing of and reasoning for joining PESCO in 2017.³ Finally, 12 confidential background interviews with EU, NATO, and EU Member State officials were conducted to confirm empirical findings from other sources and better understand the process leading up to PESCO's activation.

II. Blockade: Regional Fragmentation of European Defence Co-operation

In 2007, when signing the Lisbon Treaty, the EU Member States formally agreed to include PESCO in the Treaty on European Union (TEU, Art. 42(6)) as a tool designed to allow flexibility – that is, horizontal differentiation – in European defence co-operation (Fiott *et al.*, 2017). Treaty Protocol No. 10 specifies the club goods produced by PESCO: by participating in PESCO, EU Member States should achieve a higher level of defence investment expenditure, convergence concerning their defence apparatus, improved interoperability and deployability of forces, and appropriate participation in major European

³Using the keyword combination Member State (for example Malta) + PESCO in the Nexis® and Factiva® newspaper databases and in the Google news search for the year 2017.

equipment programmes. However, all attempts to use PESCO's potential to advance differentiated integration in defence were blocked over the next decade.

X: Diverging Preferences on Defence Co-operation

Variation in two dimensions – strategic orientations and security concerns on the one hand and defence industrial considerations on the other – shape the EU Member States' preference constellation on security and defence integration. The first dimension divides the Member States into Atlanticists, Europeanists, and neutrals (Menon and Lipkin, 2003; Wivel, 2005). For the Atlanticists, European security primarily depends upon a good relationship with the US. This group upholds NATO's primacy over any deeper European co-operation. The Europeanists, by contrast, desire a more substantial or even autonomous role for the Common Security and Defence Policy (CSDP). Finally, most neutral states prefer to maintain good relationships with both the EU and NATO and thus can neither be seen as a driver nor a brake to further EU integration in defence (Devine, 2011).⁴

The second dimension has to do with uneven economic pressures to co-operate and divides EU members into downstream and upstream states – that is, states characterized by niche industries at the end of the supply chain and those with significant defence industrial capacities (Trybus, 2014, pp. 23–4). When national procurement budgets were shrinking, development costs exploded after the Cold War, and economic patriotism became unsustainable for upstream states, they developed a preference for liberalizing the European Defence Equipment Market (Fiott, 2017; Hoeffler, 2012; Weiss and Biermann, 2021). Losses from system duplication, a lack of interoperability, and protectionist production practices were estimated to total 100 billion euros per annum (European Commission, 2016). These numbers, however, left the downstream states unimpressed: relying on intergovernmental off-the-shelf procurement, they were less dependent on European defence co-operation (Bátora, 2009).

Combining these two dimensions, the avant-garde of Europeanist upstream states comprised four EU members, France, Germany, Italy and Spain, which possessed large defence industries and military apparatus and accounted for just over 50 per cent of EU-27 defence expenditures⁵ in 2016. All other EU members were sceptical about further European defence integration and made up the group of the laggards – either because they were downstream states or, like the UK, had an Atlanticist orientation.

S₁: Proposing a 'Defence Euro-Zone'

Because of diverging Member State preferences, the group of avant-gardists proposed to include PESCO, a 'defence Euro-zone' (de Villepin and Fischer, 2002; Spini, 2002), in the Treaty establishing a Constitution for Europe. This differentiation offer was to be 'open to all Member States wishing to carry out the most demanding tasks and fulfilling the requirements for such a commitment to be credible' (European Convention, 2002, para. 54).

⁴ Austria, Finland, Ireland and Sweden have interpreted their military neutrality as being compatible with active membership of the CSDP (Devine, 2011). Cyprus, due to its conflict with NATO-member Turkey can be seen to be part of the Europeanist camp while Malta 'is but a drop in the ocean' in defence terms and consequently assuming a free-rider role (Fiott, 2015, p. 96).

⁵ SIPRI Milex data 1949–2016, available at: <https://www.sipri.org/databases/milex>.

Initially, the avant-gardist strategy seemed to work. In reaction to their proposals, some of the laggards voiced concerns about being excluded from defence co-operation (Piks and Rihards, 2002, p. 2). They demanded that ‘willingness to participate’ should be the primary criterion for admission (Gaber and Slavko, 2002, p. 3). However, it soon became evident that the avant-garde’s differentiation proposal was not credible. The downstream states were backed by the most potent laggard, the UK, which developed into the downstream states’ protection power. Fearing the establishment of independent military structures, the UK was ‘against proposals ... which would imply competition, rather than complementarity, with NATO’ (United Kingdom, 2003, p. 207).

PESCO only found its way into the 2003 Draft Constitutional Treaty (European Union, 2005, Art. III-312) because the laggards did not have to worry about its formal activation. PESCO was to be activated by a qualified majority and could thus be prevented relatively easily in light of the sizeable coalition of laggards (nine members, including the UK, would suffice, see Consilium, 2018). Keeping PESCO as a potential route to future co-operation while retaining the means to prevent any undesired developments that could undermine NATO became the best strategy for the avant-garde.

S_{2a}: Blocking PESCO

The avant-garde’s subsequent efforts to activate PESCO failed. Lacking go-it-alone power, their initiatives did not create negative externalities. Without the UK, which accounted for over 23 per cent of EU-27 defence expenditures,⁶ forming a defence union was not feasible, and the avant-garde had to give up each of their attempts.

In 2008, France made the activation of PESCO one of its top political priorities in preparing for its Council presidency (Taylor, 2008). However, the informally circulated proposal foundered as the UK fundamentally opposed it. Geoffrey Van Orden, a Conservative MEP, warned, ‘[t]his will end in tears’ (The Guardian, 2008). The other laggards shared the UK’s scepticism, and in the end, the French government did not include the activation of PESCO in the official programme for its Council presidency (France, 2008).

Two years later, when the financial crisis turned into the Euro crisis, this put potential savings from European defence integration back on the agenda. In 2010, only 23.4 per cent of European defence procurement and 12.7 per cent of Research and Technology spending was co-operative (EDA, 2011, pp. 14–16). Avant-gardist Spain consequently organised an exploratory seminar in 2010, which was followed by two further workshops organised by the Belgian presidency (Biscop and Coelmont, 2012, p. 77). Yet, the avant-gardist strategy to convince some of the laggards to join the PESCO-framework in an informal setting shattered against ‘an unbreachable wall’ of Member States’ concerns (Biscop, 2017, p. 3). The UK put an end to the discussions when Liam Fox, then prospective UK defence minister, not only made clear that Britain was not ready to advance with PESCO but even threatened to pull back from the European Defence Agency (Fox, 2010, p. 2). Consequently, at an informal meeting in Bruges later that year, EU defence ministers decided not to proceed with PESCO’s activation (EPRS, 2016, p. 4).

⁶SIPRI Milex data 1949–2016.

Y_a: Minilateralism and Avant-gardist Divisions

As a result of the Euro crisis, however, interdependence also increased among the laggards. Even so, the laggards did not desire PESCO and thus closer co-operation with the avant-garde. Nor was it an option in light of continued UK opposition. PESCO would have pushed the downstream states, characterized by niche defence industries and comparatively small military capacities, into even greater specialization and less autonomy concerning the use of their capabilities (Wivel, 2005, p. 402). The laggards resorted to a regional bottom-up approach to mitigate the economic pressures resulting from the Euro crisis and maintain modern defensive capabilities. The Nordic countries formalised pre-existing collaboration efforts and created the Nordic Defence Co-operation (NORDEF) at the end of 2009 to 'explore common synergies' (Denmark, Finland, Iceland, Norway, and Sweden, 2009, Art. 1).

Similarly, the Central European Defence Co-operation was created in 2010 (Bundesministerium Landesverteidigung Österreich, 2010). Moreover, the Visegrád Group (V4) and the Baltic states reinvigorated their respective regional defence co-operation and called for closer ties between their frameworks (Baltic Defence Cooperation, 2010; V4, 2014). Despite the window of opportunity provided by the Euro crisis, the avant-garde could not convince additional Member States to activate PESCO and further integrate defence co-operation.

The avant-garde, confronted with the laggards' minilateralism, had to look for institutional alternatives to cope with interdependence. It is no coincidence that the Franco-British Lancaster House Treaties and the German-Swedish Ghent Initiative came into being in the last quarter of 2010. These undertakings confirmed the already ongoing fragmentation of European defence co-operation. The Ghent Initiative was directed at creating a coherent frame around the regional initiatives. However, to reach consensus in the Council, the initiative did not include any binding commitments, did not refer to PESCO and thus represented no more than a 'buzzword' (Coelmont, 2017) and amounted to damage control (Interview #3, 2017).

Given Franco-British bilateralism, which represented a further turning away from the Europeanization of security and defence, damage control was necessary. With the Lancaster House Treaties, France undermined the avant-gardist coalition and irritated its partners. Robert Hochbaum, a member of the German parliament, found it 'unfortunate the British and the French are doing it without us' as 'it's always harder to get involved when two states go on ahead than when joint talks are held from the outset' (cited in Brunnstrom, 2010).

The avant-garde's attempts to establish differentiated integration resulted in the fragmentation of European defence co-operation into small, minilateral clubs. PESCO was out of reach, and observers were convinced that no changes to this situation were in sight (Centre for European Policy Studies, 2015). Yet, surprisingly, in 2016, the process that led in the end to the unexpected, almost uniform agreement to PESCO began to gain momentum.

III. Cascade: Integration to Prevent a European Defence Core

On 11 December 2017, the Council formally activated PESCO (Council of the European Union, 2017, Art. 2), and 25 EU Member States joined the initiative (all, that is, except for Denmark, Malta, and the UK). Thus, PESCO did not develop into an exclusive and ambitious club of the willing and capable but represented a suboptimally extensive, heterogeneous framework with moderate ambition (Biscop, 2017, p. 7). Two external shocks, the UK's decision to leave the EU and the loss of credibility of US security guarantees, tipped the balance and turned the avant-gardists' differentiation plans into a threat of exclusion with considerable negative externalities. The risk of being confronted with a European defence core set the laggards' cascade in motion.

X: Persistently Diverging Preferences

Donald Trump's election as US president in 2016 increased the laggards' security dependencies on the EU. Trump's questioning of the absolute character of the NATO solidarity clause (The Guardian, 2016) undermined the laggards' preferred alternative to EU integration. However, even when Trump was elected, the Atlanticists did not focus on the EU. They still worked towards ensuring 'credible deterrence by continuing persistent presence of the US' forces' (Reuters, 2016) in light of the perceived incalculable Russian threat. Moreover, the divide between liberalization-friendly upstream states and protectionist downstream ones persisted. The laggards were able to cushion economic pressures through minilateral co-operation, and the US continued to be eager to sell defence products to Europe (Reuters, 2018). Thus, preferences concerning moving ahead with PESCO consistently diverged.

S_I: Threatening a Defence Core

The avant-gardist coalition was well aware of the window of opportunity for PESCO presented by Brexit and the election of the NATO-sceptic Trump. Only three days after the US election, Germany's then Defence Minister Ursula von der Leyen stated, 'the Brexit decision and the election in the US have set a new course' (EUobserver, 2016) for European defence integration. Another three days later, on 14 November 2016, the avant-garde put PESCO back on the agenda during the Foreign Affairs Council. Member States agreed to 'explore the potential of an inclusive Permanent Structured Co-operation ... subject to the willingness of Member States to undertake concrete commitments' (Council of the European Union, 2016, para. 17). Yet, given the laggards' continued resistance to this undertaking (The Guardian, 2017; V4, 2017), the Council could not agree on a clear deadline to operationalize the proposal.

Consequently, the avant-garde needed to deliberate on incentivizing some laggards to vote for and join PESCO to achieve a membership structure that would allow them to undertake joint projects efficiently and increase the sales market for collaborative undertakings. On 6 March, the day of the next Council meeting, the avant-garde's heads of state and government met in Versailles for a mini-summit. At this venue, then French President François Hollande emphasized that 'unity is not uniformity' (Deutsche Welle, 2017). German Chancellor Angela Merkel was even more explicit: 'A multispeed Europe is necessary; otherwise we are blocked We must have the courage to accept that some

countries can move forward a little more quickly than others' (Deutsche Welle, 2017). Put differently, the avant-garde underlined that they intended to go it alone.

Since they lacked the backing of the UK this time, the differentiation attempt posed a significant risk of negative externalities to the laggards. After the Brexit vote, 11 Atlanticists would need to stand firmly together to block PESCO's establishment (Consilium, 2018). More importantly, Brexit implied the loss of the UK as the power offering protection to the laggards in decision-making on European defence. The UK's relative importance as the third-largest net contributor to the EU's budget had shielded the laggards from budgetary repercussions (European Commission, 2017). In this situation, it is understandable that the Council agreed to continue work on PESCO (General Secretariat of the Council, 2017, para. 6).

The laggards accepted this step against their preferences. Two statements are exemplary: 'The Versailles summit does not look so good if you come from one of the small Member States', a Hungarian Member of the European Parliament stated (Euractiv, 2017). Moreover, Bulgaria's then Deputy Prime Minister Denitsa Zlateva emphasized, 'we declare ourselves against the creation of the so-called core of Europe and the rest, the periphery' (Balkan Insight, 2017). The fear of being sidelined led the laggards to reconsider their position. The anti-PESCO coalition began to crumble in June 2017 when the Council 'agree[d] on the need to launch an inclusive and ambitious Permanent Structured Co-operation' (European Council, 2017). While not having PESCO at all was the laggards' preferred outcome, this was no longer a viable option. Therefore, the calculus changed for some: being a member of a less ambitious PESCO was better than being excluded from European defence co-operation altogether (Interview #1, 2018).

S_{2b}: The Cascade Sets In

Estonia, which should hold the Council Presidency in the second half of 2017, became the first laggard to back PESCO publicly. On 3 May 2017, Prime Minister Jüri Ratas made public that 'Estonia today decided that should PESCO materialize, Estonia definitely wishes to be a part of that co-operation' (ERR News, 2017). Meanwhile, the avant-gardists further increased the pressure when reiterating their case for differentiation, in which 'some countries will go faster than others' (Merkel) and 'different levels of integration' (Gentiloni) should be allowed (Politico, 2017a). Shortly after that, in June 2017, Sweden and Greece, both characterized by competitive niche industries and thus not fearing significant negative economic consequences, signalled their interest to join PESCO.

On 13 July 2017, the avant-garde came up with a proposal for the operationalization of the criteria and commitments (Conseil franco-allemand de défense et de sécurité, 2017). One week later, Belgium, the Czech Republic, Finland, and the Netherlands backed this proposal (France, Germany, Spain and Italy, 2017). This self-selection by Member States is in line with theoretical expectations: it comprises those laggards with the next lowest adaptation costs – the Netherlands, Belgium, and the Czech Republic possess relatively competitive niche industries while Finland, as a non-NATO member, was not characterized by a traditional Atlanticist orientation.

This altered the calculus for the remaining laggards as the activation of PESCO became more and more realistic, and the negative externalities increased with every Member

State willing to join (Interview #2, 2017). A few days after the communication of the proposed criteria, Bulgaria, Hungary and Latvia were ready to jump on the bandwagon, Luxembourg published its intention to join in July. It was only a matter of weeks before, on 7 September 2017, Slovakia and neutral Austria declared their plans to accede. Lithuania followed suit one day later. Romania and Croatia declared their interest on 17 October 2017; Cyprus and Slovenia on 8 and 10 November 2017, respectively, while Portugal's communist-backed minority government needed to resolve internal quarrels (Politico, 2017b) and only decided on 7 December 2017.

This cascade is decisive evidence for the laggards' rationale for joining PESCO primarily to prevent exclusion. The cases of Poland and Ireland are smoking guns in this regard. When Poland decided to join the framework, the Polish foreign and defence ministers formally attached a letter to their accession notification. The letter raised three concerns; the unclear relationship between PESCO and NATO, the fear that capability specialization would mean a loss of independence for some Member States, and the risk of neglecting the eastern flank (Waszczykowski and Macierewicz, 2017). However, the need to avoid a 'defence core', which would likely leave 'countries such as Poland on the margins of defence industry co-operation in Europe' (Terlikowski, 2016), was stronger. Because of its deeply anchored neutrality, the Irish government had to deal with considerable domestic resistance to the PESCO plans (The Irish Times, 2018). Despite these hurdles, it decided to subscribe to PESCO. Irish Minister of State for Defence Paul Kehoe countered opposition concerns by reminding them that 'Sweden and Austria, which have neutrality policies similar to ours, have already signed up to Pesco' (TheJournal.ie, 2017). Thus, confronted with the risk of negative externalities, the respective governments were willing to accept considerable costs.

Y_b: Inclusive PESCO without Ambition

When the Council decided on the formal activation of PESCO, 25 Member States participated. The exceptions were Denmark, for whom, due to its defence opt-out, PESCO never came into consideration, the UK, which was set on leaving the EU, and Malta, which was still undecided and took a 'wait-and-see' approach considering whether to join at a later stage (Malta Today, 2017). This strikingly inclusive group was not what the avant-garde had hoped for⁷ and appears unsuitable to efficiently produce the club good of joint military planning and procurement.

First, while PESCO subsumed an impressive 47 projects in 2020, only a few of these were initiated within the new framework; the vast majority pre-existed it and 'had been launched or planned before PESCO' (Terlikowski, 2020). What is more, 30 projects have remained at the 'ideation phase, including some which were already established in ... 2018' (Council of the European Union, 2020, p. 4). Second, the almost uniform integration disfigured the 'binding commitments' beyond recognition. As PESCO members decide by unanimity, commitments correspond to minimal consensus in line with the preferences of the least ambitious Member States. There were no provisions, for instance, specifying a date by which the 2 per cent defence-spending goal was to be reached (France, Germany,

⁷ Interviews with two German Member State representatives (Interview #2, 2017; Interview #4, 2017) revealed that while Germany preferred PESCO to be more inclusive than France, it nonetheless would have desired PESCO to be more exclusive and ambitious than it finally turned out.

Spain and Italy, 2017, Art. III (1, 4)). The avant-gardist attempt to achieve an ambitious step towards vertical integration in defence through horizontal differentiation had failed again.

Conclusion

Prior research has demonstrated that the outcomes of using horizontal differentiation as a strategy to overcome preference divergence are only stable when the externalities generated by a club are neutral for the outsiders (Kroll and Leuffen, 2014; Schimmelfennig and Winzen, 2020). This paper has shown that moving ahead alone results in suboptimal clubs whenever an avant-garde is dependent on the support of some of the laggards to produce the club good efficiently. When EU member states intend to circumvent resistance to vertical integration by proposing positive horizontal differentiation, they risk falling victim to the differentiation paradox. Attempts at a multi-speed Europe are unlikely to deliver the desired outcome of producing the club good efficiently. Moving ahead alone produces adverse effects. If underpinned by go-it-alone power, differentiation attempts lead to a domino effect and can result in suboptimally large and heterogeneous clubs. If the avant-garde lacks go-it-alone power, differentiation attempts risk being blocked by the laggards.

As this paper presented a theory-testing process-tracing of a single case over time, comparative cross-case analyses are mandated to complement internal with external validity. Potential cases include instances in which horizontal differentiation did not take place despite attempts to create a club within the club, resulting in either in uniform integration, such as in the case of the European company statute, or in co-operation formats outside the treaties, as in the cases of the Prüm Convention, or the creation of the Joint Armaments Organisation (OCCAR). Research on such outside co-operation appears especially rewarding, as they offer the avant-garde a way out of the differentiation paradox:

Considering qualified majority voting on PESCO's establishment, it becomes apparent that the avant-garde could either not convince the laggards to join at all or could not stop the cascade of Member States joining the framework. The same holds for attempts at enhanced co-operation in other policy areas, which is established unanimously in the Council. Thus, for an avant-garde to optimize their club membership, it appears beneficial not to create clubs *within* the club (Ahrens *et al.*, 2005) but outside the treaties. Only when the founders of a club have the sole discretion over the membership criteria they can strike a balance between incentivizing the capable while excluding those Member States that dilute ambition. France, most dissatisfied with PESCO's inclusive character, appears to have understood that. The French government proposed the European Intervention Initiative, an exclusive military framework established alongside PESCO in 2018.

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