

Eurozone Reform: Between Hope and 'Mission Impossible'

21. February 2018 by [Viriato Soromenho-Marques](#) and [Ricardo Cabral](#)

If we ponder, calmly and dispassionately, the current state of the European Union (EU), stripping away some excessively enthusiastic interpretations derived from the favourable but transient current point of the economic cycle, we will be compelled to admit that the Union is still far away from the safe lane. While the problems faced by the EU are many and varied, the key task is to identify which is the critical issue to be tackled with absolute priority in order to assure its survival. For us, the right answer would undoubtedly have to be the reforming of the flawed machinery of the Economic and Monetary Union (EMU). If the survival and the fostering of democracy and prosperity throughout the whole EU is a true political goal, the time for procrastination regarding the deficient functioning of its core – the eurozone – should come to an end.

In this post, we will restrict ourselves to two issues: a) the foreseeable impact on the eurozone reform debate of the current political trends and circumstances; b) the form by which the appointment of the president and other executive board members of the Governing Council of the ECB may deeply affect the wider discussion on the future of EMU's working rules.

2018: Are we reaching a turning point?

Ever since the European Coal and Steel Community, according to the blueprint designed by Jean Monnet and Robert Schuman, was announced in 1950, the French-German *entente* has been the key driving force behind the long-lasting and somewhat tortuous process of European integration. The EMU, within the boundaries established by the Treaty of Maastricht, was no exception. In the last decades, however, the role played by France lost considerable relevance and transformative power, giving greater latitude to a kind of '[German unipolar moment](#)' that occurred when the consequences of the flawed EMU architecture became visible with the advent of the euro crisis. Nevertheless, for the first time in many years, it seems now possible to envision a more balanced and strategically-driven partnership between Paris and Berlin. With President Macron, France is putting a disputable but clear EMU reform agenda on the table (see his [26 September 2017 Declaration](#)) in stark contrast to the pale and secondary role played both by Sarkozy and Hollande. On the other hand, the perspective of a German 'Jamaica' government coalition, which would have almost certainly frozen the debate on the EMU reform (given the strong opposition stance of the FDP), was overcome by the hope of a renewed Great Coalition between the CDU, the CSU and the SPD. It's a rather positive sign to read that the need of 'A new departure for Europe' is the first chapter [agreed in Berlin on 7 February](#). But times are (relatively) turbulent in Germany. The prospective agreement (contract) between SPD and CDU/CSU is still waiting for the electoral approval of the SPD militants. The vote will take place in an emotional atmosphere marked by a virulent personal clash of egos and ambitions.

Yet, a candid evaluation of the framework conditions in which the future German-French dialogue will evolve recommends caution against excessive optimism regarding its possible outcomes. There are at least three different reasons to be prudent. The first one is of political nature. Since the last elections for the European Parliament in 2014, the reins of political initiative were clearly taken by parties and movements that act as centrifugal and fragmentary forces regarding the integrity of the EU as a shared and cherished political common house. Beyond the four Visegrád countries, where democratic liberal values are already under severe stress, we now have the weird

Austrian neoliberal right-wing government prone to increase the angry chorus, alongside

with populists and nationalists of diverse political families and geographical regions, against any European benign reform (see [Andreas Rahmatian](#)). Besides that, the impetus for fragmentation or rebellion without a reasonable cause that was depicted in the case of Brexit by James Bartolomeusz under the label of a '[horror story](#)', is latent or already extending its shadows to other European regions. In Spain, for instance, the apparent legitimate aspiration of Catalonia for more self-government gave birth to a perilous internal split that not only divided the Catalan society as also seems to be driving Madrid away from an intense participation in the core issues of the European future debate, and confronts the EU policy makers with uncomfortable questions about democracy and the right to self-determination. The same can happen in Italy, sooner or later, after the coming March elections, where the political landscape looks far from being able to welcome a serious and strategically oriented discussion on European reforms.

The second reason for keeping the expectations low lies in the heart of the so called economic recovery of the eurozone. The return to growth, yet, wasn't able neither to diminish the growing economic divergence between countries, increased sharply after 2009, nor to correct the huge and expanding gap of inequality within even the richer country of the eurozone. That's why trade unions are fighting for better wages and work conditions in Germany (see [Peter Scherrer](#)). Or taking a more European-wide perspective, we can conclude like [Agnieszka Piasna](#) that 'pre-crisis real wage growth considerable slowed down after 2010, while in-work poverty amplified between 2010 and 2015 at EU level.'

Finally, the third reason to be moderate in expectations about the future mirrors a blend of psychological and sociological features. A [recent yearly study](#) on the level of societal trust developed in 28 countries from different continents offers a dark view of the prevailing European state of mind in eight of the nine countries participating in the inquiry. The latter ranged for years clearly in the distrustful zone (between 0 and 49 points), the political institutions being one of the main reasons for that negative citizens' mood.

A truly successful turning point in the eurozone's institutional structure would require both a firm reformist resolve and a strong leadership from Paris and Berlin, coupled with a welcoming attitude from the overwhelming majority of countries and social actors in the EU. Therefore, taking into consideration the combination of the three diverse sets of reason above mentioned, the current hostile circumstances prevailing in the EU, which in many respects is still adrift and aimless, make the tasks of a possible Franco-German front much more demanding in the urgent endeavour of reforming the eurozone.

Policy shift instead of 'business as usual'

Some topics of the French-German agenda for the renewal of the EMU are already known, and we will tackle them critically in our following posts. A truly integrated fiscal policy will require a specific and reasonable large eurozone budget under a clear legislative scrutiny. In January 2017, at the Humboldt University, [Emmanuel Macron](#), then still presidential candidate, alerted to the fact that the common currency, in its current and fragile status, worked basically as a kind of 'weak Deutsche Mark', useful only within the boundaries of a narrow perception of the German national interest. Reform is vital, therefore, if the eurozone is to survive the coming decades. On 18

January 2018, a [policy paper](#) was published, signed by 14 French and German experts, with what may probably be considered as the first agreed (and rather incomplete, as we'll explain in our coming posts...) agenda for discussion. For sure, the road ahead will be

long, difficult and tiresome, but it is also a worthwhile challenge for a fairer common future.

Amidst the uncertainties pervading the discussion about the right path to follow in the eurozone reform, there is however something that's completely sure: the timetable for shifting some of the higher official positions in the eurozone administration. The first stage of a process that will last almost two years started in late January with the replacement of Jeroen Dijsselbloem by Mário Centeno at the Presidency of the Eurogroup. However, the key posts are located in the European Central Bank (ECB). In May 2018, Vice-President Vítor Constâncio will step out, and in October 2019 the time will come to replace Mario Draghi at the helm of the ECB. That's not a routine event, but a rather delicate and meaningful one. It is now almost indisputable that the EMU was rescued from an almost unavoidable collapse by the new flexibility and dynamism introduced in the action of the ECB under Draghi's leadership. Particularly, the key step was accomplished in July 2012, in a period of high speculative pressure, with the announcement by Mario Draghi, in London, that the ECB would do 'whatever it takes' to save the euro. In the following month, the ECB announced a new programme called the [OMT](#) (Outright Monetary Transactions) that implied that the ECB would eventually purchase eurozone member countries sovereign debt in secondary markets, i.e. a form of quantitative easing. The announcement of the OMT was instrumental to give back a semblance of normality to the European sovereign debt markets.* The OMT was a symbol of the ECB's resolve and commitment to assure the euro's survival, mitigating and reverting the panic and the speculative attacks against the sovereign debt of several euro area member countries. The ECB had to act decisively in order to compensate for the unspeakable lack of common fiscal policy, resulting from the dismal software flaws still affecting the performance capacity of the EMU.

The quantitative easing programme of the ECB remains in place at the time of the writing of this text, presumably until September 2018. It has contributed to dramatically reducing the interest rates and spreads of the eurozone's member countries' sovereign debt. All eurozone member countries finally experience economic growth, with the eurozone growing for 18 consecutive quarters.

It is in this context that the choice of the next President of the ECB assumes particular importance.

In the growingly visible race to this absolutely key EMU post, there is one candidate that seems to be in a strong pole position: Jens Weidmann, the President of the other central bank located in Frankfurt, the Bundesbank (see [Werner Mussler](#)). The problem, nevertheless, shouldn't be dealt with in terms of the nationality of possible candidates,

* The OMT was subject to a legal challenge appreciated by the German Constitutional Court, which referred the case to the Court of Justice of the European Union. It was found that under certain conditions the OMT was within the [ECB mandate](#), since it was necessary to ensure the 'singleness' of the monetary policy and price stability. The OMT was never implemented by the ECB. Instead, the ECB formulated a wider Asset Purchase Programme (APP), which from March 2015 included a Public Sector Purchase Programme (PSPP), i.e., quantitative easing. In contrast to the OMT the APP and the PSPP foresaw the acquisition of debt instruments according to the adjusted capital key of each country participating in the ECB.

but in the expression and practical meaning and consequences of their political principles, beliefs and strategies. Mr Weidmann is a long-standing stern opponent of all the main decisions taken by the ECB under Draghi, particularly of the quantitative easing (OMT and PSPP) programme. In a speech, delivered in Essen on 27 November 2017,

where the programmatic tone of a candidate to presidency of the ECB was more than evident, [Weidmann](#) argued for the need to correct the current 'accommodative monetary policy', appealing to the 'toughening of the fiscal rules' and to a kind of return to the 'Maastricht framework'. In the plausible scenario of a continuity in the lack of a common eurozone budget, and even in the absence of a more modest coordination in national fiscal policies, the abrupt reversal of the ECB accommodative monetary policy, or merely expectations of such reversal of monetary policy, could have irreversible repercussions on some member states, with negative side-effects over the balance of the entire eurozone fabric.

Thus, the immediate challenge to the EMU is not further reform. It is simply to ensure that the next decisions, namely on the reform process of the eurozone and on the appointment of the next ECB president, do not revert what little has been accomplished in terms of economic growth since 2012. This modest appraisal says plenty about the current weak expectations regarding our common ability to reform the EMU successfully.

Therefore, we thoroughly agree with the message of the [open letter](#) of prominent academics, including Ulrike Guérot and Thomas Piketty, which argues for the urgency of bringing the discussion about the future of the ECB Presidency well beyond the strict diplomatic and political closets, that is, away from the narrow paradigm of business as usual. The discussion of the future of the ECB, focused on fundamental policies and not in personalities, throughout the public realm, involving the media, but also the civil society movements, the Universities, the European and national parliaments, would be a remarkable contribution to boost the momentum needed to fuel a strong and lasting debate about our common European future in a united, fair and democratic polity.