The EU will choke off Europe’s recovery

*Italian journalist **Thomas Fazi** writes that European states are being offered a pittance in Covid recovery funding in exchange for giving up even more power to the EU. The 750 billion euro ‘Next Generation’ Covid fund is all about increasing Brussels’ control over the budgetary policies of member states and strengthening the EU’s regime of technocratic and authoritarian control.*

The Covid-19 pandemic has forced governments and international institutions throughout the world to resort to ‘radical’ economic measures that would have been considered taboo just a year ago. The European Union and Euro area are no exception.

In early 2020, the EU suspended its infamously tight fiscal rules to accommodate pandemic bailouts. At the same time, the European Central Bank (ECB) launched a €1 trillion bond-purchasing programme to help governments finance (and in some cases fully cover) their ballooning fiscal deficits. And last summer, the EU agreed on a much-vaunted, €750 billion Europe-wide ‘recovery plan’ known as Next Generation EU (NGEU). The money will be raised on financial markets directly by the European Commission.

Many commentators believe that these extraordinary measures represent a long-term revolution in the institutional design of the Eurozone – a ‘Hamiltonian moment’ comparable to the 1790 agreement between Alexander Hamilton and Thomas Jefferson on public borrowing, which helped to turn the United States into a political federation. In this view, the EU is finally moving in the direction of greater fiscal federalism, while at the same time governments have been liberated from the budgetary constraints of the past. Some have even claimed that these changes in the Eurozone ‘have upgraded Eurozone member states to currency issuers for the moment’, because member states, it is argued, can now spend as much as they want.

I strongly disagree. Eurozone members have not regained monetary sovereignty. If your currency is issued and controlled by an institution outside of the perimeter of the state, as is the case for Euro countries, then you, as a nation, are not a currency issuer and are not monetarily sovereign, however the currency issuer – in this case the ECB – behaves.

What defines monetary sovereignty is the hierarchical relationship between government and the central bank. In currency-issuing nations, the central bank is effectively dependent on government or representative institutions – even if the central bank may be formally ‘independent’, as it is in most countries. As Ben Bernanke, former governor of the Federal Reserve, once said, ‘the Fed will do whatever Congress tells us to do’. Governments in the Euro area, in contrast, are dependent on their central bank. As the late, great British economist Wynne Godley presciently wrote in 1992: ‘The power to issue [one’s] own money, to make drafts on [one’s] own central bank, is the main thing which defines national independence. If a country gives up or loses this power, it acquires the status of a local authority or colony.’

The experience of the Euro has proven such fears to be well founded. I have documented the numerous instances in which the ECB has engaged in an arbitrary and illegitimate use of its monopoly currency-issuing powers, with the aim of coercing governments to comply with the political and economic agenda of the EU and its dominant actors. These include: the ECB’s delayed response to the European ‘sovereign debt crisis’, from 2009 to 2012; the signing of Ireland’s bailout programme with the Troika in 2010; the ousting of Italian prime minister Silvio Berlusconi and his replacement by the ‘technocrat’

Mario Monti in 2011; the shutdown of the Greek banking system in 2015; and the bond-market turbulence that accompanied the formation of the Five Star Movement / League government in Italy, from 2018 to 2019.

Ultimately, the events of the past decade have exposed the ECB for what it really is: a full-fledged political body with the power to bring member states to their knees. European nations have already paid a very high price for giving up their monetary sovereignty, to the extent that it is legitimate to ask if Euro countries can even be considered democracies at all. Are we really to believe that all these problems have magically vanished, purely because European institutions have decided to temporarily relax their spending constraints of governments? Of course not.

The temporary suspension of the Stability and Growth Pact's fiscal rules and the ECB's extensive and unconditional support might give the impression that Eurozone governments are free to spend as much as they want, even if just 'for the moment'. But the reality is that the architecture of the Euro, by its very nature, continues to constrain the spending capacity of governments. That is because national governments understand full well that at some point, central-bank support will be curtailed and fiscal rules will be restored. And once that happens, they don't want to be left hanging out to dry with an excessive overhang of de facto foreign-currency debt (a consequence of the fact that they don't control their own currency, and thus they can neither set interest rates nor roll over the debt with newly issued money).

This helps explain why the fiscal response of Eurozone countries to the crisis has been much more lukewarm than that of other advanced countries, which have retained monetary sovereignty. The US, UK, Canada, Australia, Japan and New Zealand – and even most emerging economies – have all put in place fiscal responses in the range of 10 to 20 per cent of GDP. But the discretionary fiscal stimulus of Eurozone governments – which include some of the countries hit hardest by the pandemic, such as Italy and Spain – has so far amounted to five per cent or less of GDP. Germany is the only real outlier, with a fiscal response worth around 10 per cent of GDP.

Moreover, even though the pandemic in Europe is far from contained and the economy is not yet on a firm recovery path, all Eurozone countries (including Germany) have already announced their intention to *reduce* their budget deficits next year. Governments clearly aren’t convinced that the EU and ECB’s change of heart on monetary and fiscal policy is anything other than temporary. And with good reason.

This is not solely a case of ideological stubbornness. The reality is much more disquieting. The European elites are aware that the entire logic of discipline and punishment, on which the Eurozone is built, is at stake. Because if governments are allowed to ‘self-fund’ their deficits on a permanent basis, without the constant threat of rising interest rates or excessive deficit procedures (EDPs), citizens might become aware of the fact that money is created out of thin air by central banks and that governments can never really run out of money.

Indeed, Reuters recently reported that sources within the ECB were concerned that the central bank’s de facto monetary financing of government deficits ran the risk of making the EU’s official credit lines – such as the European Stability Mechanism (EMS) and Next Generation EU – ‘less palatable to governments’. Both of these come with very tight Troika-like conditionalities attached. Former ECB board member Yves Mersch was also concerned that countries would ‘rather rely on national debt-issuance’, which would be implicitly backed by the ECB. And that would ‘circumvent measures that have been put into place at the European level’.

The insistence that countries need to take money from these schemes, with strings attached, is clearly not motivated by 'European solidarity'. Despite all the fanfare surrounding the EU's recovery plan, the Next Generation EU package, and the 'huge amounts of money' that it is purported to mobilise, the truth is that all of this new EU money is 'macroeconomically irrelevant', as Wolfgang Münchau starkly put it.

As much as €750 billion may sound, it amounts to barely five per cent of the EU's GDP. What's more, the funds will be disbursed over the course of six years, resulting in a fiscal expansion of around one per cent of GDP on average between 2021 and 2024 at best, according to the ECB's own estimates. And that's compared to a GDP loss for the EU as a whole of around 15 per cent just in 2020.

Furthermore, the lion's share of the funds will be channelled to member states in the form of loans. Even the so-called grants it makes available will indirectly be repaid by the recipients through contributions to the EU budget. For Italy, that amounts to a pitiful total net transfer of less than €4 billion a year. This is not even close to the €160 billion Italy lost in GDP last year alone.

In exchange for this pittance, member states will be subject to very strict conditionalities, as mentioned. Indeed, the NGEU funds are conditional on compliance with the European Commission's infamous country-specific recommendations, which in the past have consistently demanded that governments cut public spending – especially on social expenditure (particularly pensions), healthcare and unemployment benefits. This is ultimately what the NGEU is all about: increasing Brussels' control over the budgetary policies of member states and strengthening the EU's regime of technocratic and authoritarian control. So I'd suggest leaving Hamilton to rest.

In light of the above, I think it is safe to assume that the intention of European elites is to return as soon as possible to a situation in which the ECB reverts to being a ‘dealer of last resort’, whereby the central bank’s bond-purchasing support is conditional on governments putting their economic policies under the control of Brussels, by signing up to instruments such as the ESM or NGEU.

And so we can expect, at some point down the road, that the ECB will progressively begin to reduce its purchases of government bonds by appealing to the fact that the emergency phase is over, leaving no choice to those countries still running large deficits and burdened with crushing debts to resort to the EU’s official credit lines as a condition for continuing to receive ECB support.

As Italian author Giuseppe Tomasi di Lampedusa famously wrote in his novel, *The Leopard*, sometimes ‘everything needs to change, so everything can stay the same’. This perfectly encapsulates the political elites’ age-old ability to constantly rearrange the existing social order to keep themselves in power. Nothing testifies to that better than the EU.

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