

# A Bridge Towards the Future

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We are engulfed in a crisis that is systemic, and we need to find a way out of this crisis, towards a long-term governance of the Euro area. This governance should follow some principles, which we might be able to agree on easily in the current situation, but the difficulty is to survive until that time, until we will be able to install this governance.

But there is a way to provide a bridge into this longer term. That solution is something that the council I am a member of, the Council of German Experts, proposed last autumn, a European redemption pact. And I am very grateful to have the chance to describe its elements here in this circle.

## ► **Why can't we just jump into a better future?**

Let me just step back for a minute and describe the problem. Why do we need a bridge towards the future? Alas, the euro area is suffering from a severe crisis, a systemic crisis, a crisis of confidence, and there is no straightforward solution to this crisis, because three areas are entangled with each other to generate this crisis. These are (i) the area of sovereign debt, where there is a debt overhang in many countries in the Euro area; (ii) the area of ailing banks, with insufficient equity to provide a buffer to shocks, so that states which are ailing have to help banks which are ailing themselves, and both are entangled in a vicious circle; and (iii) many countries in our region have developed a low level of competitiveness over time, and overcoming this low level of competitiveness needs time and structural reform. But you cannot engage in structural reform, if you do not have the time to breathe and to refinance your normal operations.

This is a vicious circle of three problem areas, and you need a strategic solution. You need a solution that addresses all three of them at the same time, because if you do it one at a time you might help in one situation and exacerbate the situation in another area. This credible encompassing strategy needs to do at least two things at the same time. First of all, it needs to specify how the sovereign debt levels, the debt-to-GDP ratios, are brought back within a palatable range. The Maastricht Treaty provided a limit, arbitrary of course, but a limit which might be quite a good one to aim at, 60% of the GDP in each country. The strategy, at the same time, needs to specify what kind of structural reform will be undertaken with what timeframe and what efforts.

This strategy needs to be convincing not only for us, for voters, for politicians, for economists, but also for the potential investors that states and governments turn to in order to refinance their activities. It might be the case that European policymakers and leaders have so far understood the systemic nature of the problem; I cannot look inside their heads. However, they do not really act in this way. They have engaged in a sort of piecemeal engineering, with a stepwise widening of the rescue funds, and this of course is testing the devotion of European leaders, and of European voters also, to prevent a breakup of the euro area in each step.

Every time a new council meeting or a new summit agrees on a new step to widen the rescue funds, to take another step towards political integration, banking union or whatever, you test devotion to the European idea. Therefore, there should be a strategy, which is once and for all set and kept to within the next decade, where all the decision-makers stick to their promises.

### ► **Balancing solidarity and competitiveness**

This is something I have to say, and I am happy to be able to say it here. It is easy to understand that the German Government is insisting adamantly on a strategy of *quid pro quo*. I think that without conditionality and without adjustment measures it will be difficult to regain competitiveness. Solidarity and competitiveness have to be balanced, and one way of facilitating that is a bridge, the European redemption pact, which we suggested.

It is a pact with one element, the European redemption fund, which would allow member states, participants in this pact, to take all debt beyond 60% of their own GDP and put it into a fund with joint and separate liability. That is one part of the proposal. However, why is it a pact? There are conditions that come with it, namely the installation of a crisis resolution mechanism at the end of the process, with private sector involvement if

necessary, and in particular a commitment to the installation of national debt brakes.

This fund would be temporary and limited in magnitude, albeit very large, on the order of EUR2.5 trillion. And the 60% in each country which is not transferred to the fund would need to be kept at 60%, and that is only possible by using debt brakes and sticking to the agreement that is set out at the beginning.

There is one major point, at least from the point of view of the German Council of Economic Experts, namely that also the German voters have to be convinced that this is working, and that other players in the game are sticking to their promises. That is why several safety valves are included, for example the pledging of gold reserves or currency reserves.

I cannot explain in detail what these safety valves are, but I think everybody has to understand that this would be a way to provide a bridge, and embracing it means embracing all elements of it, embracing joint and several liability, embracing the low interest rates accompanying this decision, and also embracing the conditions to provide a better structure for future prosperity.

Therefore, in the end, my answer is that neither a European Germany nor a German Europe would be sufficient. It would not be sufficient only if Germany became more European, and it would also not be sufficient, if Europe became more German, whatever that might mean. We need both elements to come true to proceed to a prosperous, peaceful and coherent Europe. We have a bridge, but we have to embrace all of its elements at the same time, or it will not be a success.