The euro is 20 – time to grow up

By Jérôme Creel and Francesco Saraceno [1]

At age twenty, the euro has gone through a difficult adolescence. The success of the euro has not been aided by a series of problems: growing divergences; austerity policies with their real costs; the refusal in the centre to adopt expansionary policies to accompany austerity in the periphery countries, which would have minimized austerity's negative impact, while supporting activity in the euro zone as a whole; and finally, the belated recognition of the need for intervention through a quantitative easing monetary policy that was adopted much later in Europe than in other major countries; and a fiscal stimulus, the Juncker plan, that was too little, too late.

Furthermore, the problems facing the euro zone go beyond managing the crisis. The euro zone has been growing more slowly than the United States since at least 1992, the year the Maastricht Treaty was adopted. This is due in particular to the inertia of economic policy, which has its roots in the euro's institutional framework: a very limited and restrictive mandate for the European Central Bank, along with fiscal rules in the Stability and Growth Pact, and then in the 2012 Fiscal Compact, which leave insufficient room for stimulus policies. In fact, Europe's institutions and the policies adopted before and during the crisis are loaded down with the consensus that emerged in the late 1980s in macroeconomics which, under the assumption of efficient markets, advocated a "by the rules" economic policy that had a necessarily limited role. The management of the crisis, with its fiscal stimulus packages and increased central bank activism, posed a real challenge to this consensus, to such an extent that the economists who were supporting it are now questioning the direction that the discipline should take. Unfortunately, this questioning has only marginally and belatedly affected Europe's decision-makers.

On the contrary, we continue to hear a discourse that is meant to be reassuring, i.e. while it is true that, following the combination of austerity policies and structural reforms, some countries, such as Greece and Italy, have not even regained their pre-2008 level of GDP, this bitter potion was needed to ensure that they emerge from the crisis more competitive. This discourse is not convincing. Recent literature shows that deep recessions have a negative impact on potential income, with the conclusion that austerity in a period of crisis can have long-term negative effects. A glance at the World Economic Forum competitiveness index, as imperfect as it is, nevertheless shows that none of the countries that enacted austerity and reforms during the crisis saw its ranking improve. The conditional austerity imposed on the countries of the periphery was doubly harmful, in both the long and short terms.

In sum, a look at the policies carried out in the euro zone leads to an irrevocable judgment on the euro and on European integration. Has the time come to concede that the Exiters and populists are right? Should we prepare to manage European disintegration so as to minimize the damage?

There are several reasons why we don't accept this. First, we do not have a counterfactual analysis. While it is true that the policies implemented during the crisis have been calamitous, how certain can we be that Greece or Italy would have done better outside the euro zone? And can we say unhesitatingly that these countries would not have pursued free market policies anyway? Are we sure, in short, that Europe's leaders would have all adopted pragmatic economic policies if the euro had not existed? Second, as the result of two years of Brexit negotiations shows, the process of disintegration is anything but a stroll in the park. A country’s departure from the euro zone would not be merely a Brexit, with the attendant uncertainties about commercial, financial and fiscal relations between a 27 member zone and a departing country, but rather a major shock to all the European Union members. It is difficult to imagine the exit of one or two euro zone countries without the complete breakup of the zone; we would then witness an intra-European trade war and a race for a competitive devaluation that would leave every country a loser, to the benefit of the rest of the world. The costs of this kind of economic disorganization and the multiplication of uncoordinated policies would also hamper the development of a socially and environmentally sustainable European policy, as the European Union is the only level commensurate with a credible and ambitious policy in this domain.

To say that abandoning the euro would be complicated and/or costly, is not, however, a solid argument in its favour. There is a stronger argument, one based on the rejection of the equation “euro = neoliberal policies”. Admittedly, the policies pursued so far all fall within a neoliberal doctrinal framework. And the institutions for the European Union’s economic governance are also of course designed to be consistent with this doctrinal framework. But the past does not constrain the present, nor the future. Even within the current institutional framework, different policies are possible, as shown by the (belated) activism of the ECB, as well as the exploitation of the flexibility of the Stability and Growth Pact. Moreover, institutions are not immutable. In 2012, six months sufficed to introduce a new fiscal treaty. It headed in the wrong direction, but its approval is proof that reform is possible. We have worked, and we are not alone, on two possible paths for reform, a dual mandate for the ECB, and a golden rule for public finances. But other possibilities could be mentioned, such as a European unemployment insurance, a European budget for managing the business cycle, or modification of the European fiscal rules. On this last point, the proposals are proliferating, including for a rule on expenditures by fourteen Franco-German economists, or the replacement of the 3% rule by a coordination mechanism between the euro zone members. Reasonable proposals are not lacking. What is lacking is the political will to implement them, as is shown by the slowness and low ambitions (especially about the euro zone budget) of the decisions taken at the euro zone summit on 14 December 2018.

The various reforms that we have just mentioned, and there are others, indicate that a change of course is possible. While some policymakers in Europe have shown stubborn persistence, almost tantamount to bad faith, we remain convinced that neither European integration nor the euro is inevitably linked to the policies pursued so far.

[1] This post is an updated and revised version of the article “Le maintien de l’euro n’est pas synonyme de politiques néolibérales” [Maintaining the euro is not synonymous with neoliberal policy], which appeared in *Le Monde* on 8 April 2017.

Does Price Stability entail Financial Stability?

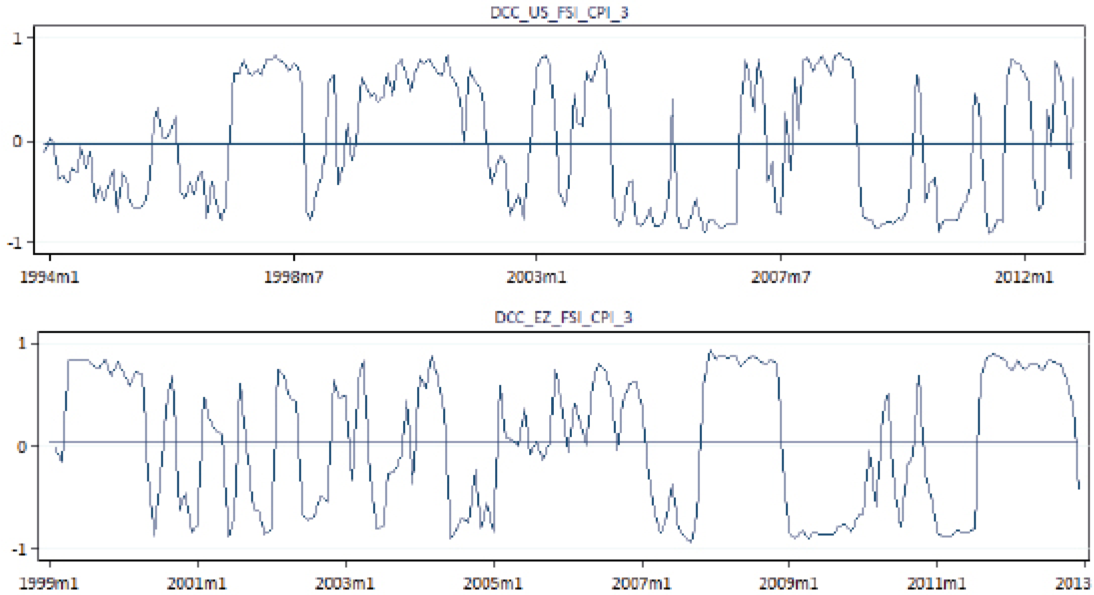
by Paul Hubert and Francesco Saraceno (@fsaraceno)

Paul Krugman raises the very important issue of the impact of monetary policy on financial stability. He starts with the well-known observation that, contrary to the predictions of some, expansionary monetary policy did not lead to inflation during the current crisis. He then continues arguing that tighter monetary policy would not necessarily guarantee financial stability either. If the Fed were to revert to a more standard Taylor rule, financial stability would not follow. As Krugman aptly argues, “*That rule was devised to produce stable inflation; it would be a miracle, a benefaction from the gods, if that rule just happened to also be exactly what we need to avoid bubbles.*“

Krugman in fact takes position against the “conventional wisdom”, which has been widespread in academic and policy circles alike, that a link exists between financial and price stability; therefore the central bank can always keep in check financial instability by setting an appropriate inflation target.

The global financial crisis is a clear example of the fallacy of this conventional wisdom, as financial instability built up in a period of great moderation. A recent analysis by Christophe Blot, Jérôme Creel, Paul Hubert, Fabien Labondance and Francesco Saraceno shows that the crisis is no exception, as over the past few decades, in the US and the Eurozone, the link between price and financial stability has been unclear and moreover unstable over time, as shown on the following figure.

Figure. Coefficient of correlation between consumer price index and financial stability index for the US (top) and the Euro area (bottom)



Source: Authors' computations. For more details on data and methodology, please refer to: https://ideas.repec.org/a/eee/finsta/v16y2015icp71-88.html

We therefore subscribe to Krugman's view that financial stability should be targeted by combining macro- and micro-prudential policies, and that inflation targeting is largely insufficient. In another work, Christophe Blot, Jérôme Creel, Paul Hubert and Fabien Labondance argue that the ECB should be endowed with a triple mandate for financial and macroeconomic stability, along with price stability. They further argue that the ECB should be given the instruments to effectively pursue these three, sometimes conflicting objectives.

What do we know about the end of monetary unions?

By Christophe Blot and Francesco Saraceno

The European elections were marked by low turnouts and increasing support for Eurosceptic parties. These two elements reflect a wave of mistrust vis-à-vis European institutions, which can also be seen in confidence surveys and in the increasingly loud debate about a return to national currencies. The controversy over a country leaving the euro zone or even the breakup of the monetary union itself started with the Greek crisis in 2010. It then grew more strident as the euro zone sank into crisis. The issue of leaving the euro is no longer taboo. If the creation of the euro was unprecedented in monetary history, its collapse would be none the less so. Indeed, an analysis of historical precedents in this field shows that they cannot serve as a point of comparison for the euro zone.

Although there seem to be a number of cases where monetary unions split apart, few are comparable to the European Monetary Union. Between 1865 and 1927, the Latin Monetary Union laid the foundations for closer monetary cooperation among its member states. This monetary arrangement involved a gold standard regime that established a principle of monetary uniformity with a guarantee that the currencies set up by each member state could move freely within the area. Given the absence of a single currency created *ex nihilo* as is the case today with the euro, the dissolution of the Union that occurred in 1927 holds little interest for the current debate. In fact, experts in monetary unions instead characterise this type of experience as “areas of common standards”. A study in 2007 by Andrew Rose (see here) assesses 69 cases of exits from a currency union since the Second World War, which would indicate that there is nothing unique about the break-up of the euro zone. However, this sample of countries that have left a currency union cannot really be used to draw meaningful lessons. A large number of these cases involve countries that gained their political independence in the process of decolonization. These were also small developing economies whose macroeconomic and financial situations are very different from those of France or Greece in 2014. The most recent experience was the break-up of the rouble zone, following the collapse of the USSR, and of Yugoslavia, both of which involved economies that were not very open commercially or financially to the rest of the world. In these circumstances, the impact on a country's competitiveness or financial stability of a return to the national currency and any subsequent exchange rate adjustments are not commensurate with what would happen in the case of a return to the franc, the peseta or the lira. The relatively untroubled separation of the Czech Republic and Slovakia in 1993 also involved economies that were not very open. Finally, the experience most like that of the EMU undoubtedly involves the Austro-Hungarian Union, which lasted from 1867 to 1918. It had a common central bank in charge of monetary control but no fiscal union [1], with each State enjoying full budgetary prerogatives except with regard to expenditure on defence and foreign policy. It should be added that this Union as such could not go into debt, as the common budget had to be balanced. While the Union established trade and financial relations with many other countries, it is important to note that its break-up occurred in the very specific context of the First World War. It was thus on the ruins of the Austro-Hungarian Empire that new nations and new currencies were formed.

It must therefore be concluded that monetary history does not tell us much about what happens at the end of a monetary union. Given this, attempts to evaluate a scenario involving an exit from the euro are subject to a level of uncertainty that we would call "radical". While it might be possible to identify certain positive or negative results of exiting the euro, going beyond this to give specific calculations of the costs and benefits of a break-up comes closer to writing fiction than to robust scientific analysis. As for the positive side, it can always be argued that the effects on competitiveness of a devaluation can be quantified. Eric Heyer and Bruno Ducoudré have performed such an exercise for a possible fall in the euro. But who can say how much the franc would depreciate in the case of an exit from the euro zone? How would other countries react if France left the euro zone? Would Spain leave too? In which case, how much would the peseta fall in value? The number of these variables and their potential interactions lead to such a multiplicity of scenarios that no economist can foresee the result in good faith, let alone calculate it. The exchange rates between the new European currencies would once again be determined by the markets. This could result in a panic comparable to the currency crisis experienced by the countries in the European Monetary System (EMS) in 1992.

And what about the debt of the private and public agents of the country (or countries) pulling out? The legal experts are divided about what share would be converted by force of law into the new currency (or currencies) and what would remain denominated in euros, which would add to agents' debt burden. So it is likely that an exit would be followed by a proliferation of litigation, with unpredictable outcomes. After the Mexican crisis in 1994, and again during the Asian crisis in 1998, both of which were followed by devaluations, there was an increase in agents' debt, including government debt. Devaluation could therefore increase the problems facing the public finances while also creating difficulties for the banking system, as a significant share of the debt of private agents is held abroad (see Anne-Laure Delatte). The risk of numerous private defaults could therefore be added to the risk of default on the public debt. How would one measure the magnitude of such impacts? Or the increase in the default rate? What about the risk that all or part of the banking system might collapse? How would depositors respond to a bank panic? What if they seek to prop up the value of their assets by keeping deposits in euros and opening accounts in countries that they consider safer? A wave of runs on deposits would follow, threatening the very stability of the banking system. It might be argued that, upon regaining autonomy for our monetary policy, the central bank would implement an ultraexpansionary policy, the State would gain some financial leeway, put an end to austerity and protect the banking system and French industry, and capital controls would be re-established in order to avoid a bank run … But once again, predicting how such a complex process would unfold amounts to astrology … And if the example of Argentina [2] in late 2001 is cited to argue that it is possible to recover from a currency crisis, the context in which the end of the "currency board" took place there should not be forgotten[3]: a deep financial, social and political crisis that does not really have a point of comparison, except perhaps Greece.

In these circumstances, we believe that attempting to assess the cost and benefits of leaving the euro leads to a sterile debate. The only question worth asking concerns the political and economic European project. The creation of the euro was a political choice – as would be its end. We must break with a sclerotic vision of a European debate that opposes proponents of leaving the euro to those who endlessly tout the success of European integration. There are many avenues open for reform, as has been demonstrated by some recent initiatives (Manifesto for a euro political union) as well as by the contributions collected in issue 134 of the *Revue de l'OFCE* entitled "Réformer l'Europe". It is urgent that all European institutions (the new European Commission, the European Council, the European Parliament, but also the Eurogroup) take up these questions and rekindle the debate about the European project.

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[1] For a more detailed analysis of comparisons that can be drawn between the European Monetary Union and Austro-Hungary, see Christophe Blot and Fabien Labondance (2013): "Réformer la zone euro: un retour d'expériences", *Revue du Marché Commun et de l'Union européenne*, no. 566.

[2] Note that Argentina was not in a monetary union but rather

under what was called a "currency board". See here for a classification and description of various exchange rate regimes.

[3] See Jérôme Sgard (2002): "L'Argentine un an après: de la crise monétaire à la crise financière", *Lettre du Cepii*, no. 218.

What Reforms for Europe?

by *Christophe Blot [1], Olivier Rozenberg [2], Francesco Saraceno [3] et Imola Streho [4]*

From May 22 to May 25 Europeans will vote to elect the 751 Members of the European Parliament. These elections will take place in a context of strong mistrust for European institutions. While the crisis of confidence is not specifically European, in the Old Continent it is coupled with the hardest crisis since the Great Depression, and with a political crisis that shows the incapacity of European institutions to reach decisions. The issues at stake in the next European elections, therefore, have multiple dimensions that require a multidisciplinary approach. The latest issue of the *Debates and Policies Revue de l'OFCE* series (published in French and in English), gathers European affairs specialists – economists, law scholars, political scientists – who starting from the debate within their own discipline, share their vision on the reforms that are needed to give new life to the European project. Our goal is to feed the public debate through short policy briefs containing specific policy recommendations. Our target are obviously the candidates to the European elections, but also unions, entrepreneurs, civil society at large and, above all, citizens interested by European issues.

In the context of the current crisis, the debate leading to the next European elections seems to be hostage of two opposing views. On one side a sort of self-complacency that borders denial about the crisis that is still choking the Eurozone and Europe at large. According to this view, the survival of the euro should be reason enough to be satisfied with the policies followed so far, and the European institutions evolved in the right direction in order to better face future challenges.

At the opposite, the eurosceptic view puts forward the fundamental flaws of the single currency, arguing that the only way out of the crisis would be a return to national currencies. The different contributions of this volume aim at going beyond these polar views. The crisis highlighted the shortcomings of EU institutions, and the inadequacy of economic policies centered on fiscal discipline alone. True, some reforms have been implemented; but they are not enough, when they do not go in the wrong direction altogether. We refuse nevertheless to conclude that no meaningful reform can be implemented, and that the European project has no future.

The debate on Europe’s future and on a better and more democratic Union needs to be revived. We need to discuss ways to implement more efficient governance, and public policies adapted to the challenges we face. The reader nevertheless will not find, in this volume, a coherent project; rather, we offer eclectic and sometimes even contradictory views on the direction Europe should take. This diversity witnesses the necessity of a public debate that we wish to go beyond academic circles and involves policy makers and citizens. Our ambition is to provide keys to interpret the current stakes of the European debate, and to form an opinion on the direction that our common project should take.

[1] OFCE, Sciences Po

[2] Sciences Po, Centre d'études européennes

[3] OFCE, Sciences Po, (@fsaraceno)

[4] Sciences Po, Ecole de droit et Centre d'études européennes

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And what if Italy's elections turned out to be an opportunity for Europe ?

By Franscesco Saraceno

The whole of Europe is currently fretting about the election results in Italy. The Centre-Left coalition won a narrow majority – because of an electoral law that everyone denounces, but no one seems to have the knowledge or ability to change – which gives it an absolute majority only in the Chamber of Deputies. Due to the way bonuses are attributed for majorities won on a regional basis, no coalition in the Senate has a majority. With its system of "perfect bicameralism", Italy now finds itself in a situation where there is no possibility of forming a government with a political majority. This note explores one possible scenario for the coming few weeks and its economic consequences for Italy and Europe.

Aside from the spectacular political resurrection of Silvio

Berlusconi, whose stated goal from the beginning was to prevent the victory of the Left rather than to secure a majority, the two startling results of this poll are on the one hand the defeat of the incumbent Prime Minister, Mario Monti, and on the other the progress of the Five Star (*Cinque Stelle*) movement of the former comedian Beppe Grillo, who now heads the leading party in the Chamber of Deputies.

The defeat of Mario Monti is a stinging repudiation of austerity policies that Italy's citizens view as imposed by Europe and Germany. In Monday's *New York Times*, Paul Krugman called Monti a "proconsul installed by Germany to enforce fiscal austerity on an already ailing economy". Called in November 2011 to the bedside of a country left prostrate by the Berlusconi government, Monti has failed to offer anything other than austerity policies which, unsurprisingly, did not deliver the growth promised. The support the former European Commissioner initially enjoyed slowly eroded as the memory of the problems marking the end of the Berlusconi era faded, and especially as Italy sank deeper and deeper into economic crisis. Mario Monti undoubtedly expected to play a decisive role in the formation of a majority in the Senate, and thus to be able to negotiate his reappointment as Prime Minister. But his gamble failed, and he is now condemned to numerical insignificance.

Beppe Grillo, in contrast, rode to a remarkable success on a tidal wave that now makes him key to the formation of a new government. Thanks to a masterful campaign conducted in the media as well as the street, his movement is the leading party in the Chamber and in the Senate in several regions. He managed to capture the exasperation of the Italians against the "political caste", and he brought almost nine million voters into a campaign that tapped into right-wing populism (*e.g.* on several occasions he made remarks on immigration and the euro that are not reflected in his programme). He has also played on key concerns of the traditional Left, such as the rejection of austerity, environmental issues, the reduction of working hours, a national minimum income scheme, the regulation of conflicts of interest, limited terms for elected officials with no cumulation of mandates, and the ineligibility of those sentenced by the courts.

What will happen in the coming weeks? All Europe is wondering, and the initial reactions of the markets seem to betray nervousness about future developments. For institutional reasons, a new election in the very near term is not an option. President Giorgio Napolitano, who is at the end of his term, cannot dissolve Parliament; invoking this option would mean waiting until May for his successor (who is chosen by the MPs elected yesterday). Moreover, it is not certain that the Parliament chosen in any new elections would lead to a political majority.

The majority electoral law gives the Democratic Party an absolute majority of the seats in the Chamber of Deputies, which makes it indispensable to the formation of a new government. This means there are only two possible scenarios: firstly, a broad coalition between Left and Right (with or without Mario Monti's party). This seems unlikely, firstly, because of the ideological divide between the two parties, which has been aggravated by the return of Silvio Berlusconi; and secondly, because it would be perceived by the voters as ignoring the outcome of the election, which saw the two major parties lose over 11 million votes since the 2008 election.

The second solution would be a minority government of the Centre-Left, which could seek out votes from Beppe Grillo's MPs on a programme that was limited in scope and duration. In this case it would be worth considering what possibilities might exist for a convergence between the Five Star movement (whose programme can be downloaded here [in Italian]) and the Pierluigi Bersani coalition. There would certainly be a consensus on some very popular measures for dealing with the ongoing political crisis (abolition of the provinces, limits on the terms and multiple mandates of parliamentarians, ineligibility, reducing the cost of the political machinery, etc.), and for fixing some of the most vexing problems from the two decades of Berlusconi (reforms on conflicts of interest and corruption, judicial reform).

The environmentalist wing of the Centre-Left could also find convergences on incentives for energy efficiency and on investment in renewable energy.

In economics, some of Beppe Grillo's key measures could also see a convergence with the Centre-Left, for example on the adoption of a national minimum income scheme or minimum wage, themes which, as has been shown in the French debate, are not necessarily populist or unrealistic.

It would be difficult to agree on any convergence between the Centre-Left and Beppe Grillo within the framework of the current fiscal consolidation, so it's worth repeating that a prerequisite for this would be calling into question the austerity policy repudiated by the voters. This would inevitably pose problems for the Democratic Party which, like the Socialist Party in France, has gone in for austerity. Negotiations with the Five Star movement would imply abandoning the ambiguous position that the Democratic Party has long held on austerity. This would in turn have an impact throughout Europe. In the coming few weeks, Europe's leaders may be faced either with the lack of a government in the third-largest economy in the euro zone or with a government that is likely to turn its back on austerity. Europe could then be forced to rethink its own economic strategies, and some countries that have been tightening up only reluctantly (like France?) could seize the opportunity to call into question the model of growth through austerity.

Does inequality hurt economic performance?

By Francesco Saraceno

Economic theory has long neglected the effects of income distribution on the performance of the economy. Students were taught right from Introduction to Economics 101 that the subject of efficiency had to be separated from considerations of equity. The idea is that the size of the cake had to be expanded to the maximum before it is shared. It was implicit in this dichotomy that economists should address the issue of efficiency and leave the question of distribution (or redistribution) to the politicians. In this framework, the economist's role is simply to ensure that choices about the channels for redistribution through taxation and public spending do not affect growth by interfering with the incentives of economic agents. Echoes of this view can be found both in the debate about the taxation of very large incomes envisaged by the French Government as well as in authors like Raghuram Rajan who justify inequality with references to technical progress and international trade, a view refuted by Paul Krugman.

Since the work of Simon Kuznets in the 1950s, some economists have of course questioned whether excessive inequality might not inhibit economic growth, in particular by blocking the accumulation of human capital. But this has long been a minority view among economists. Indeed, the dramatic increase in inequality documented among others by Atkinson, Piketty and Saez as well as by institutions such as the OECD and the IMF failed to give rise to a deep-going reflection about the relationship between inequality and economic performance.

It was the crisis that revived this concern. Growing inequality [is now suspected]() of being a source of increasing household debt and speculative bubbles, leading to the accumulation of internal and external imbalances that have set off the current crisis. This is the argument developed by authors like Joseph Stiglitz and James Galbraith.

Today the dichotomy between efficiency and distribution is no longer tenable. Inequality is becoming an essential theme in economic analysis, for both the short and long terms. To stimulate discussion on this topic, the OFCE and the SKEMA Business School are holding a workshop on "Inequality and Economic Performance" in Paris on 16 and 17 October 2012.

Plea for a growth pact: the sound and fury hiding a persistent disagreement

By Jean-Luc Gaffard and Francesco Saraceno

The emphasis on the need to complement fiscal restraint by measures to boost growth, which is rising in part due to the electoral debate in France, is good news, not least because it represents a belated recognition that austerity is imposing an excessively high price on the countries of southern Europe.

Nevertheless, there is nothing new about invoking growth, and this may remain without consequence. In 1997, as a result of a French government intervention, the Stability Pact became the Stability and Growth Pact, but this had no significant impact on the nature of strategy, which remained fully oriented towards the implementation of strict monetary and fiscal rules and a constant search for more flexible markets.

Last week, Mario Draghi, along with Manuel Barroso and Mario Monti, were worried not only about the recession taking place in Spain, Portugal, the Netherlands and Great Britain but also about the need to respond formally to a request that may come from a new French government. They too are arguing for a negotiated Growth Pact, while taking care to note that it must consist of a common commitment to carry out structural reforms wherever they have not yet been made. This position echoes the February letter of the eleven Prime Ministers to the European authorities. In other words, nothing is to change in the doctrine that determines the choice of Europe's economic policy: growth can be achieved only through structural reform, in particular of the labour markets.

There are two grounds for criticizing this position. It is far from sure that structural reform is effective, unless, that is, it is wielded in a non-cooperative spirit to improve the competitiveness of the country that undertakes the reform at the expense of its trading partners, as Germany was able to do with the Hartz reforms. Secondly, widespread reform, including where this is justified in terms of long-term growth, would initially have a recessionary impact on demand [1], and hence on activity. Reform cannot therefore deal with what is actually the immediate top-priority requirement, namely stemming the spreading recession.

The real challenge facing Europeans is to reconcile the short term and the long term. The solution proposed so far, general fiscal austerity aimed at restoring the confidence of private actors, which would be complemented by structural reforms intended to increase the potential growth rate, just doesn't work. This can be seen by developments in Greece, as well as in Portugal and Ireland, which are model students of Europe's bailout plans, and also in Britain, Italy and Spain. The fiscal multipliers remain firmly Keynesian (see Christina Romer, and Creel, Heyer and Plane), and any "non-Keynesian" effects on expectations are limited or nonexistent.

Growth can neither be decreed nor established instantly, unlike the deflationary austerity spiral in which more and more European countries are currently trapped.

Growth is likely to materialize only if fiscal consolidation is neither immediate nor drastic – in fact, only if the consolidation required of countries in difficulty is spread over time (beyond the year 2013, which in any case will be impossible to achieve) and if the countries that are able to carry out a more expansionary fiscal policy actually do this in such a way that at the European level the overall impact is neutral or, even better, expansionary. This strategy would not necessarily be punished by the markets, which have shown recently that they are sensitive to the requirement for growth. Otherwise, steps should be taken by the ECB to deal with the constraints imposed by the markets. This short-term support must be accompanied by substantial medium-term investment made through European industrial programs financed by the issuance of Eurobonds – which would mean, finally, a European budget on a scale large enough to handle the tasks facing the Union. This method of coordinating short- and medium-term choices would be an important step towards the establishment of the kind of federal structure that alone will allow the resolution of the "European question".

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[1] R.M. Solow, Introduction to Solow, R.M. Ed. (2004), *Structural Reforms and Macroeconomic Policy*, London: Macmillan).