FES BRIEFING

EUROBONDS AND EUROPEAN CITIZENSHIP

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»This spring Europe will change«
Pino Daniele, Questa primavera

THE EMERGENCY

The coronavirus pandemic will have a powerfully negative impact on the European Union's economies. The exact scale of this impact will certainly depend on how long it lasts, together with the consequent restrictions on productive activities and mobility that the various European countries are progressively adopting (and which demonstrate, by the by, how little they have learned from the experience of the countries affected first). But the economic consequences of coronavirus will also depend on the scale and promptness of the action taken to support economies. We have weeks, not months. It is crucial that a decision be made by Easter.

The US government has approved federal action worth 2000 billion dollars in addition to an injection of unlimited liquidity by the FED. In Europe, after a hesitant start, the ECB has launched a Pandemic Emergency Purchase Programme (PEPP), initially limited to 750 billion euros in 2020 and then made potentially unlimited, declaring that purchases will be »necessary and proportionate« to the purpose of achieving the »mandate's goals«. The ECB also temporarily loosened certain bank supervisory regulations in order to reduce the potential credit crunch. In public spending terms, on the other hand, the Commission has only been able to suspend the Stability Pact – that is, the rules that limit member states' deficits and public debt, particularly those of the euro zone – and to consider action in the amount of 37 billion euros designed to supply liquidity to small businesses and the health sector. This is clearly an entirely insufficient sum even for the emergency alone, which encompasses not only health but also the incomes of millions of self-employed people, those without fixed contracts and small and micro businesses – among others – which have been brought to a sudden stop as a result of the pandemic.

WHAT WE DON'T WANT

To overcome these very narrow restrictions from multiple sides a more powerful tool has been proposed to protect the European Union – or at least the euro zone – to be used on an even larger scale than in the 2008–2009 and 2011–2012 crises. Some commentators have argued for the need to resort to Eurobonds or Coronabonds, European bonds to be guaranteed by the Union's new »fiscal capacity«. We believe that this is the right path. But there have been many objections, above all from Northern European countries, which may slow down or even block the adoption of this solution in the necessarily brief time frame required by the health and economic crisis.

Without going into the rights and wrongs of the political legitimacy and ethics of these objections, we believe that they are due to an underestimation of the scale and costs of the pandemic and an overestimation of nations' fiscal capacity to deal with it. The upshot would be an acute moral hazard that risks rebounding on their own citizens, not to mention those of Europe as a whole, to the extent that any country that will not be able to tackle the health and economic crisis with all possible means will constitute a serious threat both to itself and to others.

To overcome these objections we will attempt here to outline a Eurobond issue proposal of a scale capable of effectively taking on the health and economic crisis in all countries and initiating a recovery, while at the same time creating the safe asset that Europe and its financial system so desperately need. It is worth clarifying right away what the Eurobonds we are suggesting are *not* and what they will *not* do.

(i) They are *not* new individual state bonds; and

(ii) Neither are they ESM loans, loans aimed at tackling the present financial crisis of individual states rather than the gigantic common shock of the coronavirus pandemic. ESM funds must remain available for their original purpose, with the conditions foreseen, above all after the pandemic crisis has peaked and states' debts will in any case have grown.

(iii) The Eurobonds we are proposing do *not* mutualise the various states' existing debts: the »virtuous« states would not be guaranteeing the previous debt of the »less virtuous« states.

(iv) The resources made available by Eurobonds proposed here would *not* constitute temporary or permanent transfers from one country to another because the key to spending and the necessary back-up is the adult population.

THE PROPOSAL

We will present our proposal in point form in the hope that the resulting greater clarity will more than compensate for the inevitable costs of brevity.

a. Any Eurobond issue will have to be shored up by a guarantee. We believe that this guarantee must be *new* and *shared*. It must not touch states' capital, the capital that currently guarantees their national public debts and must be supplied by the European Union with its dedicated fiscal capacity. It could take the form of a special purpose fund within the EU budget.

b. This fund would be fed by a yearly »citizenship contribution« proportionate to the number of adult citizens in the Union, which would thus distribute the burden equitably among member countries.

c. The citizenship contribution would be calculated by multiplying each adult citizen (>18) by 50 euros. Estimating that adults constitute approximately five-sixths of the total population, the revenue for the EU would be around 18.5 billion euros per year. For example, Italy would contribute 2.5 billion euros, Germany 3.46 billion, France 2.8 billion, Spain 1.9 billion and so on.

d. This fiscal capacity would be used entirely to guarantee the payment of interest on fixed-coupon open-ended or very long-term Eurobonds (*perpetuities* or *consols*) and would be inter-generational (100 years).

e. In the case of perpetual bonds, at an interest rate of 1% it would be possible to issue up to 1,850 billion of these Eurobonds, including in various instalments. At a 2% interest rate up to 925 billion could be issued (bn 18.5/0.01=bn 1,850; bn 18.5/0.02=bn 925)

f. Interest rates and contributions could be indexed if inflation goes over 2% (1%) in order to ensure a positive yield.

g. Spending the revenues collected from issuing these Eurobonds would be based on a programme decided on and controlled by the Commission, proportionately to each country's adult population. This would amount to around 125 billion euros for Italy, 165 billion for Germany, 139.5 billion for France and over 97 billion for Spain, with a 925 billion issue and double that for a 1850 billion issue.

h. Each European citizen's initial contribution would thus be multiplied by 50 or 100 (depending on the interest rate), making right away per capita spending of 2,500 euros possible. It is a very high multiplier, which would transform a small initial fiscal effort into an extraordinarily profitable investment.

DISCUSSION

1. The fiscal guarantee and real return assured by these Eurobonds would make them safe assets, attractive to banks and institutional investors (insurance companies, banks, pension funds) and purchasable by the ECB on the secondary market, in full accordance with its mandate.

2. The guarantee would be even stronger in the event that European countries agreed to give the Commission a full-blown power to tax, thus transforming these contributions into the EU's »own revenue«.

3. This would mean the advent of fiscal union which, at least for the euro zone, would represent the necessary completion of monetary union. But launching full-blown fiscal union immediately is not necessary.

4. The fiscal guarantee means that Eurobonds could be used to fund urgent current rescue and recovery expenses, and not solely spending on profitable investments.

5. The fact that each state's contribution would be calculated by multiplying a fixed amount (50 euros) by the adult population does not imply that it must necessarily take the form of a per capita European citizenship tax (a poll tax), the equitability of which can be disputed. The adult population is simply the key to this scheme for the purpose of dispelling fears of potential state to state transfers.

6. The annual fiscal cost would be 0.11% of the EU's 2019 GDP, 0.13% of Italy's, 0.10% of Germany's, 0.11% of France's and 0.15% of Spain's.

7. It is a very small fiscal cost and would decrease over time if real GDP grows over the coming years, once we have left the pandemic recession behind.

8. The benefit of the scheme in spending terms (at 2%) would be 6.64% of the EU's 2019 GDP, 7% of Italy's, 4.8% of Germany's, 5.77% of France's and 7.8% of Spain's. This would double if the rate was 1%.

9. The fiscal cost of this scheme per country would be far lower than purely national plans on a similar scale. The positive financial implications are clear and this is even truer of the potential spending implications.

10. The cost/benefit differences between countries in GDP terms are obviously to be explained by the respective differences in per capita GDP. This underlines that the key to the scheme is population, not revenue. In fact, in the medium term the pandemic's impact on individual countries will be proportionate to population. The scheme is designed to assist Europeans as such, not European countries.

11. The technical issue of these Eurobonds could be entrusted to an entity such as the EIB or the EFSM (it still exists!), which is a fully EC wide institution. The use of the ESM is more problematic. The ESM is an inter-governmental institution over which the parliaments of the individual states have veto rights. Thus any ESM issue would be subject to a complex, potentially paralysing decision-making process. In order to use the ESM profound changes in the present methods of issue and conditionality would be required. And each of these changes would be subject to one or more states' veto power.

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