



FRANCE STRATÉGIE

ÉVALUER. ANTICIPER. DÉBATTRE. PROPOSER.

Reforming the euro area: Where do we stand

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Time to get serious (again)

Brexit

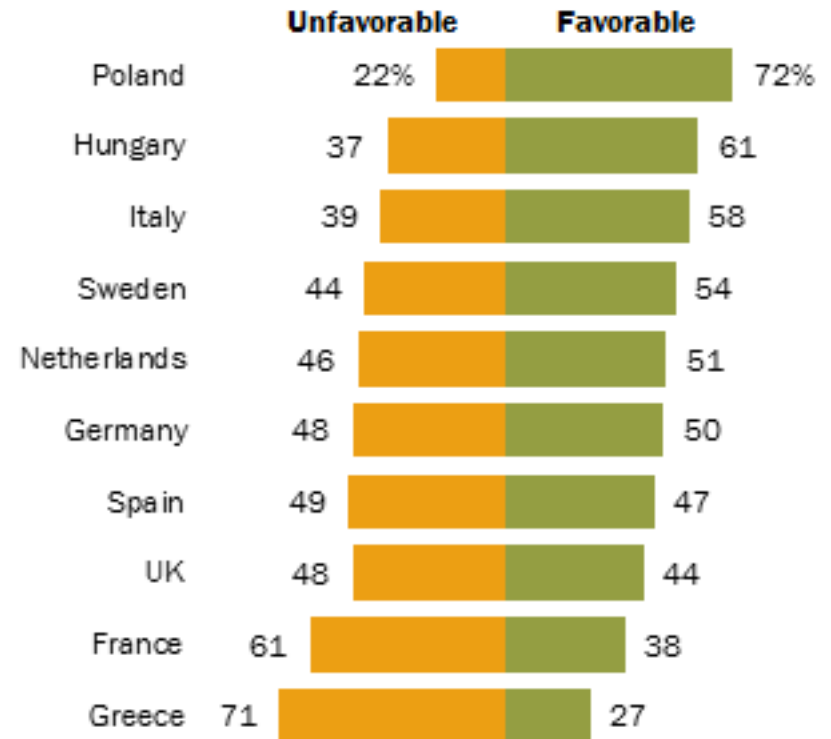
- Economic risk
- Political risk
- Market risk

On the agenda

- Economic revival
- Economics of currency union
- Politics of monetary integration

EU favorability varies widely in Europe

Views of EU



Source: Spring 2016 Global Attitudes Survey. Q10c.

"Euroskepticism Beyond Brexit"

PEW RESEARCH CENTER



What problems?

Infrastructure

- Integration within European market
- Economic resilience
- Growth potential

Legacy

- Debt
- Banks
- Real exchange rates
- Unemployment

Policy principles

- Supply / demand
- Individual responsibility / risk sharing
- Governance model



Where / why do we disagree?

Not fundamentally on infrastructure

- Domestic agenda and EMU agenda largely coincide
- Issues to be solved:
 - Integration (pan-European banks; labour mobility)
 - Reform commitment

A lot on legacy issues

- Creditors vs. debtors
- Skeletons in the cupboard

Question: can we find agreement on policy principles?

- Cognitive dissonance (alternative crisis models)
- Preference heterogeneity
- Compatibility with domestic political systems

5P report: the wrong strategy

Rather: blueprint first, then address legacy issues



Supply / demand: an economists' dispute

- French and German economists argue at length over the appropriate fiscal stance

In reality:

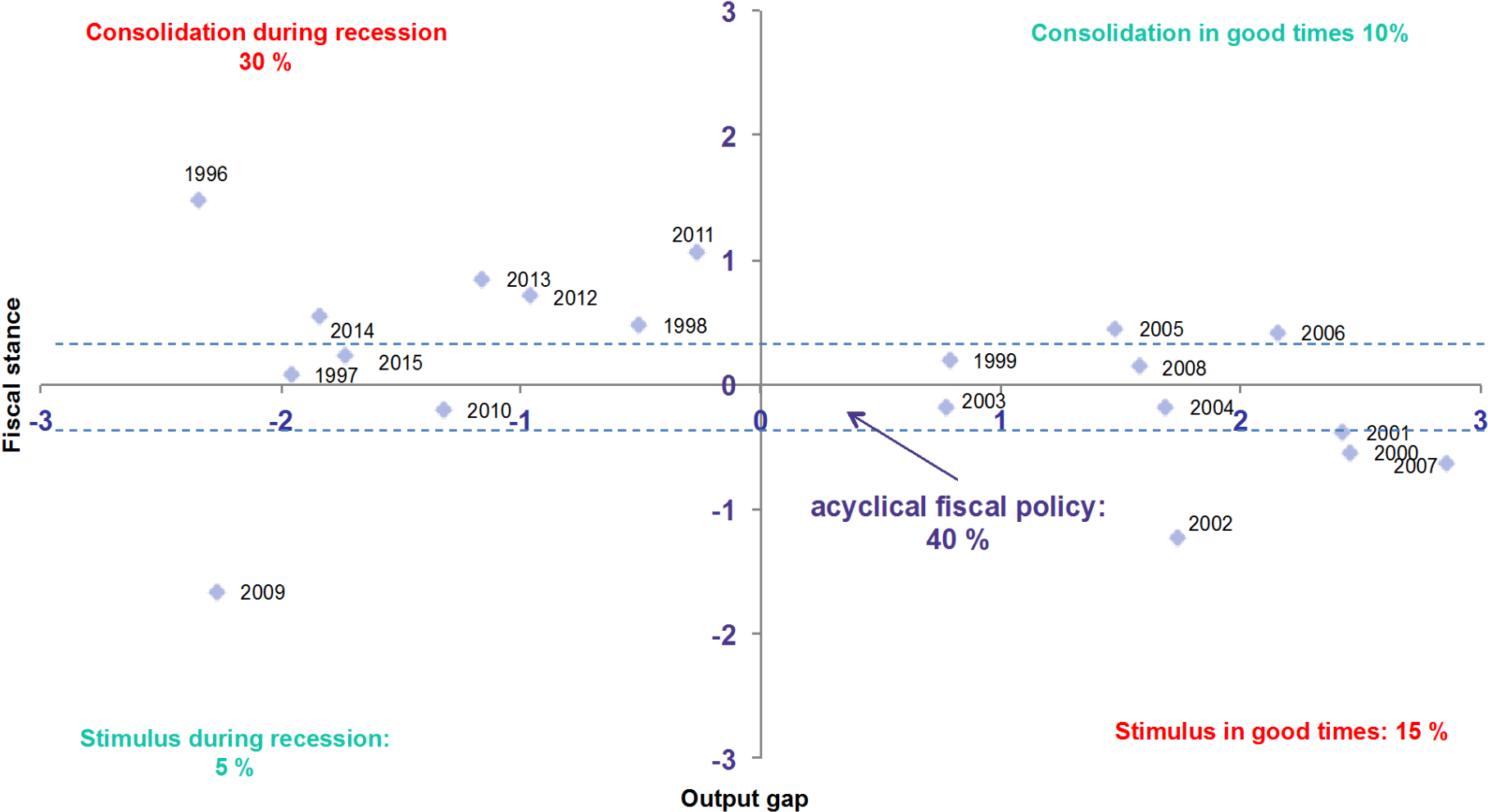
- French fiscal policy not that stabilising (especially bad at consolidating in good times)
- German fiscal policy not that procyclical (especially good at consolidating in good times)

Implications:

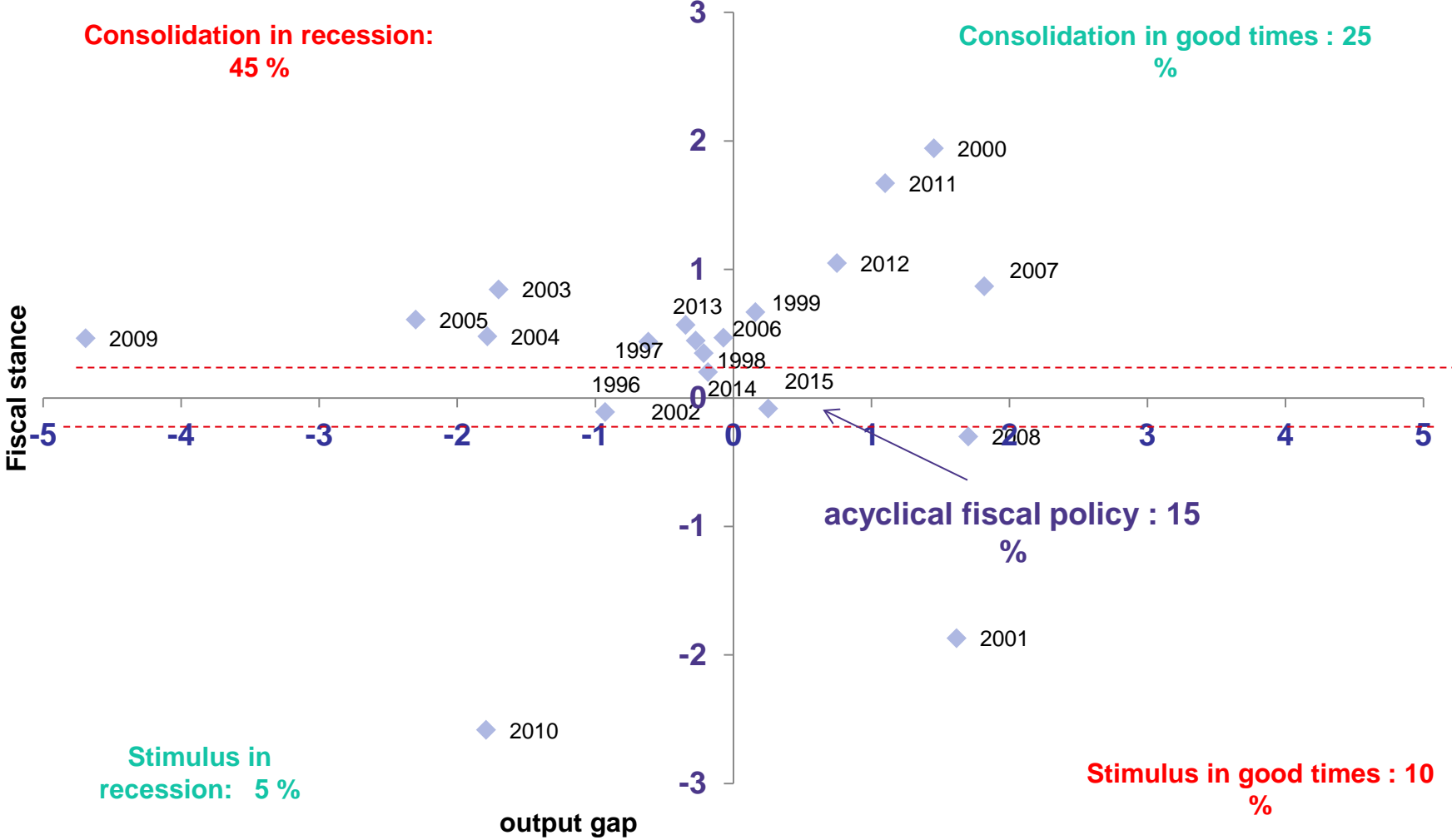
- Do not overestimate practical importance of differences in policy philosophy
- Room for agreement on policy principles



Fiscal stabilisation in France, 1996-2015: 15/45



Fiscal stabilisation in Germany, 1996-2015: 30/55



Individual responsibility / risk sharing: Room for (good) compromise

- German view emphasises moral hazard, adverse effects of bail-outs
- French view emphasises solidarity as a quid pro quo for discipline

Key in discussions on:

- Fiscal regime
- Banking union
- Reforms

A balanced compromise:

- Debt restructuring scheme based on ESM
- Full banking union with deposit guarantee and fiscal backstop
- Common safe asset
- Fiscal discipline rules



Governance model: Room for triangulation

- French view emphasises **discretion** and **coordination**
- German view emphasises **rules** and **competence delineation**

Both often inconsistent:

- F reluctant to rules-based coordination
- G reluctant to delegation to EZ level

Result: messy, ineffective and illegitimate governance

In reality **three possible models**:

- a) Full decentralisation and market discipline (*à la* Ashok Mody)
- b) Common targets + coordination (e.g. Villeroy's MOF)
- c) Federalisation and common institutions (EZ budget)

Problem: hard to compromise between (a) and (b) but F and G reluctant to (c)

Room for clever **triangulation**?

- Hub and spoke model for national fiscal policies: strong common institutions, strong national institutions (fiscal councils, productivity councils)
- Limited fiscal capacity at EZ level for spending on common public goods and **contingent aggregate stabilisation**



Thoughts on legacy issues

- Significant efforts to address legacy issues without fiscal transfers (see e.g. recent CEPR report)
- Useful attempts but do not design the permanent regime with a view on addressing legacy problems
- Better pay one-off price for legacy than accept permanent design flaw

