A SYMPOSIUM OF VIEWS

Did Europe Just Experience Its "Hamiltonian Moment"?

The reference of course is to America's first Treasury Secretary, Alexander Hamilton, who consolidated the war debt of the thirteen colonies with the issuance of common debt. German Finance Minister Olaf Scholz described the €750 billion reconstruction package with a historical reference to the former American Treasury secretary.

Is Europe moving in the same direction? The European Union has agreed to a coronavirus relief plan based on the issuance of common debt.

Is this the completion of the final phase of the "European Experiment"—fiscal and political integration? Or were the European Union's actions strictly a Covid-19–related initiative likely never to be repeated short of another pandemic? Further, what would be the implications if any for Europe's sovereign debt market and the euro were the EU pandemic rescue effort to become the permanent policy model?

Over thirty noted observers offer their views.

The politicians of the European Union have put the cart before the horse.

THOMAS MAYER

Founding Director, Flossbach von Storch Research Institute, and Professor, Witten/Herdecke University

German Finance Minister Olaf Scholz celebrated the €750 billion European reconstruction fund as Europe's "Hamilton moment," and one of his advisers spoke of a great gesture of solidarity between the states of the European Union. It seems to me that "Euromanticism" has turned the heads of our finance ministry.

If Scholz had been a little more concerned with American history, he would have known that the takeover of the states' debts by the U.S. federal government in 1790, which was pushed through against fierce resistance in Congress by Alexander Hamilton, the first U.S. Secretary of the Treasury, proved to be a mistake. In the years that followed, the socialization of debt was considered a precedent that would be applied in principle to states in financial difficulty.

This changed in 1842, however, when the states in the West and South of the United States had raised considerable sums of money to finance the development of these regions. The debts were to be serviced from fees for the use of newly built infrastructure facilities. But when the U.S. economy fell into recession in 1839–1843 in the wake of the financial panic of 1837, the hoped-for revenues failed to materialize. The states got into financial difficulties and asked Congress again for financial aid.

But this time Congress refused the bailout. Nine of the then–twenty-nine states and territories went bankrupt (but still paid back their debts afterwards to regain access to the financial markets). It was not Hamilton's socialization of the debt, but the refusal of "bailouts" by Congress that set the precedent for the American fiscal set-up. After the experience of the "no bailout," many states wrote balanced budget amendments into their constitutions or finance laws. After the Civil War, states extended the principle of "no bailout" to their communities.

In contrast to the United States, the politicians of the European Union have put the cart before the horse. They started with requirements for fiscal policy discipline in the Stability and Growth Pact and bans on bailouts and monetary financing of state debt at the central level.

However, as a critical number of euro states failed to summon up the strength for fiscal discipline, the bans were undermined during the euro crisis of 2010–2012. In the coronavirus crisis, they have now been completely abandoned by the European Central Bank's government bond purchase programs and the EU reconstruction fund. The European Union distributes grants without strict conditions and the European Central Bank takes the necessary flexibility in its bond purchases to keep the interest rate spreads between the bonds of euro states with very different credit ratings very low.

Socialization of the debt of sovereign states introduces the soft budget constraints well known from the socialism of the Soviet era. Monetary financing becomes essential as lavish debt issuance exceeds available savings. Actual or repressed inflation rises and the currency is debased. The system collapses when people rebel against economic decline caused by increasing economic inefficiency.

It would be misleading to praise this as "Europe's Hamiltonian Moment."

JÖRG ASMUSSEN

Member of the Board, German Insurance Association, and former Member of the Executive Board, European Central Bank

In response to the coronavirus pandemic, EU leaders agreed in July to establish an EU Recovery Fund (Next Generation EU). The initiative draws extensively on the Merkel-Macron proposal and thus once again underlines the importance of German-French cooperation for the European Union.

As the pandemic is having asymmetric economic effects across member states, the fund should prevent a deeper economic divide within the European Union. There is no doubt: the fund represents a major paradigm shift in the European Union's institutional architecture. Crises in the past have served to develop and deepen the institutional architecture. For the first time, the European Union will issue bonds on a large scale, a measure long rejected by Germany and others, and provide grants in particular to the member states that are most severely affected.

For a long time, the European Central Bank has called for a stronger role for fiscal policy. The agreement on the Recovery Fund is an important sign of European solidarity. In addition, there are strong economic interests with respect to the importance of the EU single market and the role of the European Union globally.

The EU Recovery Fund is often compared to America's first Treasury Secretary Alexander Hamilton's 1790 agreement on public borrowing. The agreement dealt with the mutualizing of legacy debt from the Revolutionary War of thirteen loosely confederated former colonies, and was one of the major steps in founding a federal union.

However, the current Recovery Fund does not go so far. In its framework, each member state is only liable up to its own financial contribution. This is an important distinction from Euro bonds that include joint guarantees.

The establishment of the Recovery Fund is not a full fiscal union. However, within the existing EU Treaty, the EU Recovery Fund is a significant step as it contributes to a deeper integration of EU member states and is at least a step toward a fiscal union, which has already been discussed in the context of euro area reforms for some time. Moving forward in this direction would also require a closer political union with more democratic accountability by the European Parliament.

Nevertheless, the recent change in the EU institutional architecture will have important implications. In the next severe crisis calling for EU-wide action, the Recovery Fund will provide a blueprint. It can be expected that this fiscal mechanism will be deployed again to fight the next recession.

At the same time, issuing bonds on a large scale by the EU Commission provides a new liquid debt instrument, which will also be attractive to institutional investors such as insurers. After Brexit, this will be an important step to strengthen EU capital markets.

To sum up, even if the establishment of the EU Recovery Fund represents a major—and in my view necessary—paradigm shift for the European Union, it would be misleading to praise this as "Europe's Hamiltonian Moment."

Trust in government is at an all-time low. Populist sentiments are at post-war highs. The vision that inspired the "Hamiltonian moment" does not yet seem to be broadly shared.

WILLIAM R. WHITE

Former Economic Adviser, Bank for International Settlements

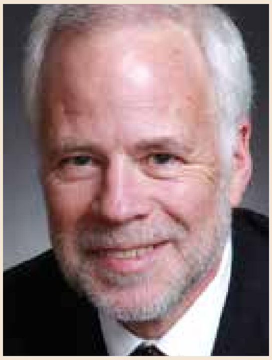
This is far from being Europe's Hamiltonian moment. Consolidating the debt of the thirteen colonies, and giving the federal government the power to tax, were seen by both Washington and Hamilton as indispensable to the construction of a strong federal government.

No such vision drove the establishment of the European Recovery Fund and associated increases in the seven-year community budget. Rather, these developments seem more in the old tradition of "muddling through" in response to whatever crisis threatened to tear the community apart. Moreover, the one-off initiative to deal with crisis-related spending through debt issued by the European Commission, and the limited commitment to "explore" new sources of central finance, fall far short of the permanent measures taken by the Founding Fathers of the United States in 1790.

Yet there are aspects of the recent deal that are remarkably different from Europe's response to the European crisis that began in late 2009. The strong and joint leadership by France and Germany recalled memories of an earlier age in the Community, with Germany accepting policies that it had earlier totally rejected. The normal rules forcing fiscal discipline on member states have been temporarily withdrawn. Not only has there been an acceptance of more community debt, rather than a prescription of austerity, but that debt was for the first time to be issued in size by the Commission itself. Indeed, suggestions for establishing a market "yield curve" implied that further such issues might follow. In addition, some concrete proposals were made, albeit "exploratory," as to how the center might also raise tax revenues on a more permanent basis. Finally, for those wishing to see them, there were welcome hints that the governance of the European Union might be shifting cautiously away from the traditional reliance on "unanimity."

It might be that all these changes have arisen from a new sense of "solidarity" in which northern, richer countries have come to the aid of southern, poorer countries harder hit by the pandemic itself. If so, these changes will persist only as long as the pandemic itself. In contrast, it might finally be sinking in that the European construct is of benefit to everyone and that creditor countries serve their own interests in helping other members of the community. This would imply that the movement towards fiscal union might become more sustained and that it would also encourage banking, economic, and eventually political union in turn.

The arguments for greater European integration are clear. European trade and financial integration benefits all countries, but trade and other such ties imply that policies to stabilize the economic and financial system are best directed from the center. A large, centrally guaranteed market for European "safe assets' would enhance the role of the euro as a reserve currency with all its attendant privileges. A united Europe could also fill the current moral gap in global leadership, promising the rewards of leadership and support for sustainable development goals. Yet the impediments to greater union are also clear. Trust in government is at an all-time low and inward, populist sentiments are at post-war highs. The vision that inspired the "Hamiltonian moment" does not yet seem to be broadly shared.



What made for the United States' own "Hamiltonian moment" was its own resources.

BARRY EICHENGREEN

George C. Pardee and Helen N. Pardee Professor of Economics and Political Science, University of California, Berkeley

What made for the United States' own "Hamiltonian moment" was its own resources. Not only did the federal government assume the Revolutionary War debts of the now thirteen states, but the Congress agreed to create the U.S. Customs Service to collect import duties. The federal government thus had a dedicated source of funds that would expand with the economy and ensure that the government's debt-servicing capacity expanded along with it. This relieved the federal government of the need to go hat in hand to the states each time it had occasion to issue debt.

"Own resources" is of course where Europe's negotiations got hung up last July. Leaders punted the decision of whether to tax financial transactions, large platform companies, digital transactions, or carbon emissions into 2022. They did agree to a modest tax on non-recycled plastic waste, but that decision was heavily symbolic; it won't generate the revenues needed to pay off €750 billion of bonds, much less to issue more. *TIE* will have to ask this question again next year.

I am in favor of a different Hamiltonian moment.

GYÖRGY MATOLCSY

Governor, National Bank of Hungary

Although the common bond issuance in the European Union officially has been adopted as a one-off measure, people speaking about a Hamiltonian moment nonetheless maintain that the genie has been released from the lamp and the emergency measures may consolidate as a regular part of the European toolkit. Historical examples abound, such as the large-scale fiscal programs during the Second World War, which were initially justified by war preparations and war-related expenditures but later became standard instruments. In addition, one can point out that no monetary union was operative in history without centralized fiscal policy, implying that centralized monetary policy with many national fiscal authorities is unsustainable.

In my view, the above arguments do not provide sufficient justification for speaking about a Hamiltonian moment. The case is very different from that in the United States 230 years ago. In Europe, the single currency was a political decision. The euro was created to fulfill the "European dream," born at the historical moment of the break-up of the Soviet Union and the unification of Germany, with the introduction of the common currency seen as the key to deeper integration.

However, it quickly became clear that the single European currency was basically designed for good times, even though it should have survived a series of crises. The common currency was built on shaky foundations. There is no common budget, no common finance minister, no banking union yet, and no proper dialogue on the dangers of a lack of an independent monetary policy. Member states are still too different in terms of culture, traditions, economic development, taxation, and competitiveness. A premature and concealed fiscal union seems unworkable to me on a lasting basis. Member states need to converge with each other beforehand. At present, an enforced fiscal union would just generate further tensions inside the European Union and hamper development. Furthermore, the common bond is actually not that common for the eurozone and for member states with national currencies. For the latter, it is going to be a debt in foreign currency, held predominantly by foreigners. In Hungary, we have learned how dangerous a combination that is.

One can imagine at least three scenarios for the future: a looser cooperation among member states while using the common currency, but following their own strategies; a two-speed integration process, with a faster-integrating core and less-integrated rest of the Union; or much looser cooperation among groups of countries, which share more priorities among them and nurture a closer relationship with each other.

I am in favor of a different Hamiltonian moment. Hamilton urged using fiscal capacities in developing economic capacities to stand up to the challenges posed by the rival imperial and economic powers. Europe needs similar close cooperation between the governments and the private sector to make the transition to the new, sustainable economy. It does not necessitate a fiscal union or common bond issuance, but a new approach to the role of the state: national or federal.

A rising share of national debt owned by the ECB is stealthily increasing the true level of fiscal integration in Europe.

JACOB FUNK KIRKEGAARD
Senior Fellow, Peterson Institute for International Economics

EU leaders in July with their decision to launch a joint post-pandemic economic recovery fund took a significant step forward in fiscal integration in Europe. For the first time, they agreed to issue large amounts of common debt—€390 billion—with the explicit aim of commonly funding new public investments to act in a fiscally counter-cyclical manner and with confined but intentional fiscal transfers between member states.

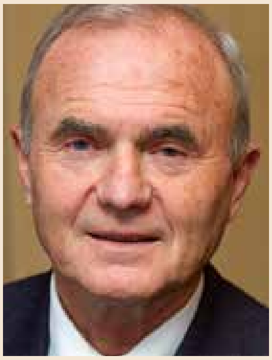
EU leaders during the Covid-19 pandemic identified a shared regional economic crisis warranting the novel issuance of joint debt to address the dire economic and political effects of the virus. This issuance of new joint debt will not consolidate existing member state sovereign bonds into euro bonds, and as such does not replicate Alexander Hamilton's famous 1790 Compromise, which saw the outstanding debts of the U.S. states consolidated into single federally issued securities.

Yet the political argument used by Hamilton to pursue debt consolidation by appealing to the shared nature of the struggle during the War of Independence, which accounted for the vast majority of American states' debts at the time, nonetheless has been repeated in Europe in recent months. Without the historic depth of the related recession and the shared pan-European (with no moral hazard concerns) scope of the Covid-19 pandemic, the political will to break two major political taboos in European fiscal integration—the blocks on joint long-term debt to fund EU budgetary expenditures and explicit fiscal transfers between member states—would not have been present. Hamilton's political arguments hence won the day again in Brussels in 2020.

It is a historical irony that the 1790 Compromise consolidated the debts from a war against the United Kingdom, while the EU decision would almost certainly not have been possible without Brexit. The end of British government influence on a continent hence facilitated both debt events.

Hamilton is rightly heralded for having laid the cornerstone for what finally with Franklin Delano Roosevelt's New Deal by the 1930s emerged as a strong fiscally centralized U.S. federal government. Given the continued lack of EU political integration and the unique circumstances of the pandemic, the implications of the new joint EU recovery fund though are likely to be less momentous. This is not the beginning of a strong federal state in the European Union, a development which would require wholly unrealistic political changes across Europe, and fundamental revisions to the existing EU Treaties.

Yet the new EU recovery fund has an important precedent-setting effect. It is probable that future EU leaders during coming EU crises will look to the decisions just taken for inspiration. The political threshold for future issuances of additional common EU debt to address the crises of tomorrow has surely been lowered. And as EU leaders will also discover, the political path of least resistance in today's negative interest environment once the new joint debt has been issued will—despite current protestations to the contrary—be not to rush to repay the debt, but rather roll it over far into the future. Very gradually, crisis by crisis, a deep and liquid market for common EU debt will in the future therefore likely emerge side-by-side with still-large national debt markets in the European Union. A rising share of the latter, though, is likely to be owned by the European Central Bank, stealthily increasing the true level of fiscal integration in Europe.



The historical analogy is simply wrong.

OTMAR ISSING
President, Center for Financial Studies, Goethe University Frankfurt, and Founding Member of the Executive Board, European Central Bank

According to Jean Monnet, Europe always needs a crisis to make an important step forward. On the one hand, European integration is based on a grand political design. On the other hand, progress in political reality can only be achieved and the manifold obstacles overcome under the pressure of a crisis. Following the motto "never let a crisis to go waste," Covid-19 seems to deliver a perfect case to go ahead. Politicians, among them the German finance minister, and academics, identify a Hamiltonian moment for Europe. This reference is based on two elements comparable with the situation of 1790 in the United States: an exogenous symmetric shock, with asymmetric impact. EU countries with already high public debt before the crisis would run into great difficulties in financing the measures needed to stabilize their economies. Alexander Hamilton interpreted the assuming of states' debt accumulated during the War of Independence as "cement" for the Union.

The opportunity of an Hamiltonian Moment for Europe means to mutualize new debt at the EU level to deal with the economic consequences of the pandemic and provide the financial means to the countries most seriously hit by the crisis. Shouldn't the European Union follow the U.S. example and move in the direction of fiscal and political union?

Indeed, the European Union has broken a taboo. It will raise a large amount of debt (€750 billion) for which there will be a common liability of member states, and distribute the financial means to countries partly as transfers and partly as credits. In addition, own revenues for the European Union via European taxes are planned. Will the political ambition end in a fiscal and finally political union?

"Hamiltonian moment" is a nice catchword (see my article "The COVID-19 crisis: A Hamilton Moment for the European Union?," in *International Finance,* Summer 2020). However, it would be dangerous to create the impression that using the Covid-19 crisis implies the chance for a state-creating moment in Europe comparable with its achievement in the United States. First of all, the historical analogy is simply wrong. The union that assumed the debt in the United States from individual states already existed. If Europe wants to establish a fiscal union by transferring sovereignty on taxation, credit financing, and public spending from the national to the European level, there is only one democratically legitimate way to do so—a change of the Treaty on the European Union that must be ratified by all governments and parliaments, and even confirmed by a referendum in some countries. In Germany, such a decision requires a change to the constitution. Seeking a shortcut by seizing a supposed Hamiltonian moment creates an illusion that might backfire and ultimately undermine popular support for deeper European integration.

Europe must find its own way. And this way to fiscal and finally political union must not use the backdoor of more or less tricky ploys which undermine the democratic accountability of national parliaments. European politics must choose the front door of an open process leading to democratic legitimacy via a change of the Treaty.

Europe could learn from Hamilton another lesson and give the formation of a common foreign and defense policy first priority and resist the temptation to base political integration on a union of common debt.

Europe-wide taxation and a European finance minister are necessary consequences of the new strategy.

KLAUS F. ZIMMERMANN
Professor of Economics, Bonn University, and President, Global Labor Organization

After the onset of the Covid-19 crisis, European institutions remained absent for a long time, leaving relevant activities to the largely uncoordinated national policies of single governments. The European Union only returned with a coronavirus relief plan based on the issuance of common debt after a long delay.

Heavily debated among governments and within the European Parliament has been whether the mutualized debt should be provided as grants or loans, and what the negative financial implications of the rescue would be for the pre-corona European plans of fostering structural change. But the move was also considered as a potential "Hamiltonian moment" of re-creating Europe as the United States of a zone based on fiscal and political integration.

Is such a creative leap conceivable? Can the crisis be instrumentalized to foster the needed long-term structural changes in economy and society, including establishing EU-wide fiscal stability and coordination? Simple political observation says that it pays not to waste a crisis, and no political measure is as permanent as a temporary measure. But the prospect of a new United States of Europe is not only driven by accident and the political logic of muddling-through. It is also suggested by the long-term economic forces and the immense global challenges the world is facing.

The past and future lockdowns of economies and social life will generate a tremendous recession much stronger than the global financial crisis (2007–2008), with substantial long-term negative consequences for the flexibility of government activities and government debt. This has reinvigorated the role of government and macro management.

The burden for coming generations has substantially increased beyond the massive challenges that climate change, demographic imbalances, global refugee flows, and digitalization already present. It is almost impossible to ignore the powerful forces of globalization and international cooperation during such an emergency.

A functioning European Union is not superfluous; on the contrary, it is more indispensable than ever. Solidarity is a global public good, but it will only be realized once common values have been agreed on, including democracy, humanitarian principles, fiscal sustainability, the acceptance of the decisive role of incentives to optimize welfare, and the drive for structural reforms and social change.

Brexit has made this pathway easier for the rest of Europe. The critical role of the "frugal four" (Sweden, Denmark, the Netherlands, and Austria) in the debate has made the new debt policy more credible. Europe-wide taxation and a European finance minister are necessary consequences of the new strategy.

Chancellor Merkel's Christian Democrats are insisting that this analogy is misplaced.

ROLAND VAUBEL

Professor Emeritus of Economics, University of Mannheim, and Member, Academic Advisory Council, German Federal Ministry of Economics

In Germany, the government is split over this issue. While Finance Minister Olaf Scholz, a Social Democrat, has called the agreement on the EU Recovery Facility a "Hamiltonian moment," Chancellor Angela Merkel's Christian Democrats are insisting that this analogy is misplaced because the European Union is not, like Alexander Hamilton, consolidating old debt of the member states and because the Recovery Facility is a one-time exercise limited to the coronavirus incident.

In my view, as I shall explain, the facility is a powerful and disastrous precedent generating incentives for excessive debt financing due to collective responsibility.

No doubt, the scheme will be challenged in the courts for lack of a legal basis. According to the Treaties (notably Article 310 of the Treaty on the Functioning of the European Union) and the Budget Statute, the EU budget has to be balanced. The transfers and loans of the Recovery Facility are to be granted within the official budget but to be financed by contributions raised off-budget by issuing common debt.

In my view, this construction is an illegal way of circumventing the balanced budget requirement. However, I do not expect that the EU Court of Justice will object to it. Like the Marshall court in the United States during Hamilton's time, the EU Court of Justice acts as a motor of integration including political centralization. When the Treaty partners cannot agree on some centralizing amendment, a simple majority of the Court's judges stand ready to adjudicate the centralization. While in the past there has been a strong general presumption that EU debt financing is prohibited, the Court's stamp of approval, which I expect, will open the floodgates for EU debt financing into the future, long after the coronavirus crisis.

The issuance of jointly guaranteed debt has been foreshadowed by the European Union's short-time unemployment insurance fund SURE, established earlier this year. The legislation (Article 10) obliges each member state to guarantee not only its own share of the EU debt but also the shares of other member states which renege on their guarantees.

The new EU bonds will not make much of a difference for Europe's sovereign debt market because the market already trades a large and fast-growing volume of bonds issued by the European Investment Bank and the so-called European Stability Mechanism. These bonds, too, are guaranteed by the member states of the European Union or the eurozone, respectively.

EU spending financed by EU debt will be more tightly controlled than national spending.

NICOLAS VÉRON
Senior Fellow, Bruegel, and Senior Fellow, Peterson Institute for International Economics

The EU budget deal of July 21 marks a historic moment, because it's the first time that the European Union has acquired significant financial firepower of its own. (There was something of that in the original European Coal and Steel Community of the early 1950s, but it was small in scale and soon phased out.) The debt issuance capacity will establish the European Union as a significant player in official bond markets, in the same league as large EU member states in terms of volumes and liquidity over the next few years.

As for semantics, irrespective of whether the moment is deemed Hamiltonian or not—keeping in mind that the institutional development path of the European Union is completely different from that of the United States—that EU debt deserves to be called a Eurobond. Eurobonds were the matter of much debate over the past decade, and widely considered utopian (including by this observer) until German Chancellor Angela Merkel's astounding *volte-face* on May 18, 2020. That's when she and French President Emmanuel Macron jointly announced their support for what has now become the stimulus package, or in Brussels jargon, NextGenerationEU.

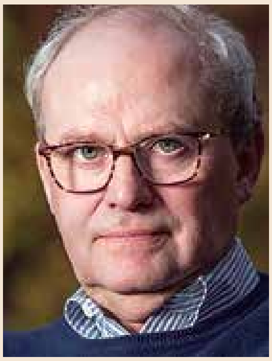
Of course, the official discourse is different: the EU issuance is proclaimed to be a one-off process that does not set a precedent, is thus not a permanent feature, and is thus not a Eurobond. In the short term, this discourse is necessary to ensure political consensus. But investors have already seen through it.

Once established in the financial landscape, EU debt will become such a central reference in the EU financial system that recurring recourse to it will be obviously preferable to alternative options—including but not limited to partial refinancing of the NextGenerationEU debt itself when it comes due.

Euro taxes—or in Brussels jargon, "own resources"—will be discussed for that debt's reimbursement, and there's an ultimate backstop from member states, but the volumes at stake are large enough that full reimbursement without any refinancing won't be the optimal way to deal with it, either from a political or financial standpoint. And new needs will come up for which more EU debt will be the best financing option.

Does that imply fiscal profligacy? Probably not. EU spending financed by EU debt will be more tightly controlled than national spending in many member states, for which it will partly substitute. Meanwhile, the risk of euro area break-up has been dramatically reduced. As a consequence, euro area sovereign spreads are permanently compressed, because that "redenomination risk" accounted for much of the spread volatility of the last decade.

But another medium-term consequence of the emergence of EU debt as the reference safe asset is likely to be more junior status for national sovereign debt, resulting in tighter market discipline. If so, that should be viewed not as a bug, but as a feature.



There are two big problems with the cry for a Hamiltonian moment.

ANDERS ÅSLUND
Senior Fellow, Atlantic Council, and author,* Russia's Crony Capitalism: The Path from Market Economy to Kleptocracy *(2019)

The question of whether Europe just experienced its Hamiltonian moment raises many thoughts. In a narrow sense, it seems true. In 1790, Alexander Hamilton, as the first U.S. Secretary of the Treasury, insisted on the U.S. federal government assuming the states' debts incurred during the War of Independence. In late July 2020, the European Council agreed to mutualize an emergency package of €750 billion.

Yet the amount is small and the difference from the ordinary EU budget of just over 1 percent of GDP is very limited. That budget transfers substantial funds of up to 4 percent of GDP to the poorest East European members, which is more than the new fund will deliver. The European Stabilization Mechanism that was founded in 2012 to manage the euro crisis that erupted in 2010 also involves a mutualization of EU debt.

There are two big problems with the cry for a Hamiltonian moment. It is a mindless idea that Europe has to follow the lead of the United States and that fiscal issues offer a panacea. But Europe's main problems lie elsewhere: poor fiscal discipline, incomplete markets, and slow innovation, resulting in very little economic growth. These are the problems Europe needs to solve.

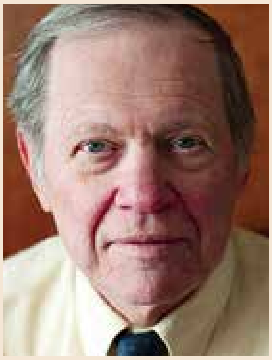
After the euro crisis, the European Union has largely fixed its fiscal affairs. Last year, the composite budget deficit of the European Union was 0.6 percent of GDP, with half the members having budget surpluses. The vast debts of Greece, Italy, and Portugal persist, but the overall situation is under control.

The immigration shock of 2015 has largely been absorbed. At least nine European countries now have a larger share of inhabitants born abroad than the United States. Europe has caught up with the United States not only in immigration but also in tolerance of people who are different.

During the coronavirus pandemic, Europe (eventually) showed its strengths—a strong public health care system, universal medical insurance, good public order, and a strong civil responsibility.

While neoliberalism has become a bad word, the still over-regulated countries Italy and Greece could greatly benefit from substantial deregulation. The new Greek government has gotten the message. Let us just wish it success! Six countries—Italy, Greece, Bulgaria, Romania, Hungary, and Poland—have serious shortcomings in their rule of law. The European Union needs to deal with it.

The big European concern today is low growth, because the high-tech giants develop in the United States and China, but barely in Europe. One shortcoming has been incomplete markets, notably for digital services and capital, but some improvements are under way. Another problem is insufficient skills. Many European universities are good, but few except those in the United Kingdom are top-notch. A closely related concern is insufficient links between universities and business. Clearly, venture capital does not operate appropriately in Europe. These rather than fiscal redistribution are the key European concerns.



The new decision to borrow sets a precedent for any emergency lending, not only in pandemics.

RICHARD N. COOPER

Maurits C. Boas Professor of International Economics, Harvard University

To call the recent EU summit decision on the EU borrowing €750 billion for over thirty years a "Hamiltonian moment" for the European Union is to apply a very elastic interpretation to an historical analogy, and one, like most historical analogies, that can be very misleading.

The U.S. Constitution (1789) enables Congress "to borrow money on the credit of the United States." Alexander Hamilton strongly supported the new constitution, as reflected in his co-authorship of *The Federalist Papers.* But that was not his Hamiltonian moment. That came when as the first U.S. Treasury Secretary, he successfully advocated consolidation of the already-outstanding debt of the diverse American colonies, incurred during the revolutionary war against Britain and during the early years of independence, in name of the new federal government of the United States.

Variants of this proposal to consolidate some part of outstanding eurozone members' debts were made six to eight years ago, during the so-called euro crisis, but they were all rejected by the German government and its allies.

And even in the United States, the consolidation was approved due to its unique contextual background. The federal government has since then declined to assume debts of states, even in default, as in the 1830s. Bonds of Puerto Rico (a financially autonomous U.S. dependency, not a state) are now in default and Puerto Rico bond holders may yet get some federal financial assistance; that remains to be seen.

Whether the new EU borrowing authority will be repeated in the future also remains to be seen. The new decision to borrow sets a precedent for any emergency lending, not only in pandemics, and many emergencies are possible during the normal seven-year EU budget cycle. Of course, future budgets will have to allow for interest payments on the outstanding debt—now exceptionally low—and also for repayment of that part of principal that is given as grants rather than loans to member states.

But there is still no decisive political will and no legal basis for the "United States of Europe."

THOMAS MIROW
Chairman, German National Foundation, and former President, European Bank for Reconstruction and Development

No doubt the decision taken by Europe's leaders in July 2020 to set up a European Recovery Fund of €750 billion, financed by mutual debt, represents a historic step for the European Union.

It is, in the first place, a political milestone. Germany reversed its longstanding position and actively designed, in close cooperation with Macron's France and the European Commission, a powerful new solidarity tool. Chancellor Merkel understood that the pandemic had the potential to destroy the European Union through too-deep disappointment in Italy and Spain about the lack of solidarity when the virus hit them hardest, and too-devastating economic impact of the pandemic on their economies. So something big had to be done to convince the nations of southern Europe that the Union is to their advantage. With the decision taken after acrimonious debates on a four-day summit, the European Union proved its political will and capacity to act.

It is an economic milestone, too. The accelerating difference in growth and sound public finances between the North and South, exacerbated by the pandemic, is a lethal threat to European monetary union. It needs to be reversed, eventually.

Also, Europe will become a major player on financial markets. The volume of European bonds will come close to that of those placed by Italy, France, or Germany. For investors looking at "safe havens," a true European alternative to German bunds will be on offer. This should, very likely, also have repercussions for the role of the euro. Central banks all over the world, until now, have almost exclusively relied on the U.S. dollar for holding reserves. This may—gradually—change.

And finally, many private banks are currently sitting on huge amounts of bonds of their respective home countries, thus creating a dangerous cluster-risk. With a liquid market for European bonds, diversification and risk reduction will get realistic—thus hopefully paving the way for a badly needed agreement on a common European Banking Rescue Scheme.

So does this equate to a Hamiltonian moment? Historic parallels drawn between the United States and the European Union are nearly always misleading. The European Union has to find its very specific path of its own to a united continent. Certainly the mutualization of—new!—debts is an important political and economic catalyst for a closer European Union and it will markedly improve Europe's standing on international financial markets.

But there is still no decisive political will and no legal basis for the "United States of Europe" with a single government, a common treasury, a true parliament, and a shared capital. Chancellor Merkel is bound to step down next year. President Macron's political fate seems difficult to predict. Italy's current pro-European stance appears fragile. Other EU members in the North and East are—for very different reasons—obsessed with their national sovereign rights.

So where Europe will head in the years to come seems nearly impossible to predict—although the dangerously escalating rivalry between the United States and China delivers another compelling argument for Europe to finally unite and forcefully defend its values.

The European Union did not experience its "Hamiltonian Moment."

MICHAEL HÜTHER
Director, German Economic Institute

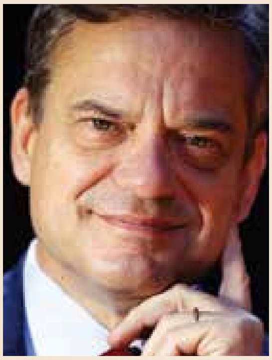
In a negotiation marathon, the EU member states unanimously passed the largest budget and financial package in the Union's history. For the first time, the European community pledged to take up common debt by issuing bonds to finance their EU recovery plan. Even though the frugal five managed to reduce the initial proposal of direct grants from €500 billion to €390 billion within the recovery package comprising a total of €750 billion, fears of mutualizing liabilities eventually leading to a transfer union have entered the policy arena again.

Notwithstanding the great success of striking such a difficult, costly, and controversial agreement, clearly the European Union did not experience its "Hamiltonian Moment." In contrast to the popular view (especially in Germany) that Europe is moving towards an economic United Nations of Europe with complete fiscal integration and debt mutualization, the EU recovery fund mobilizes common resources to tackle a common threat: the pandemic that affects all member states. The fund is, however, a step towards a more cohesive European community. It creates an instrument that can address important structural changes such as digitalization and climate change.

More importantly, it signals Europe's willingness to act decisively and in a comprehensive manner. The political concordance is furthermore going to positively backstop expectations of firms and consumers, stabilize financial markets, and hence significantly support the economic recovery process. Whereas pledged payments will only become effective in the following years and thus do not represent an immediate stimulus package to deal with the current economic recession, the fund builds up new European investment gunpowder supporting sustainable growth in the future.

Member states unanimously agreed on the necessity of common debt issuance for the EU recovery. The main debate rather touched upon concerns about the refinancing of mutualized debt. Namely, would recipients of the funding need to repay their debt individually, or should member states design common tools to refinance liabilities? In the former case, creditor countries would only benefit through lower interest rates and an initial grace period. Finally, member states agreed on refinancing the recovery fund mutually through future EU budgets, however, without mutualizing liabilities as would be the case in a transfer union. In contrast to far-reaching prejudices against countries such as Italy benefiting from a commonly refinanced recovery plan, it needs to be acknowledged that even Italy is a net payer to the EU budget with only slightly lower net payments than France in 2018. Hence, the country is going to actively participate in the recovery program's funding—particularly as it seems highly uncertain that the European Union will come up with its own new revenue sources. Finally, a paradigm shift towards a transfer union—a familiar claim—has never been the goal.

The agreed financing rules are appropriate and involve checks and balances: the funding will be issued in installments and controlled by the Commission and finance ministers of the member states. In fact, for the first time, criteria concerning the rule of law have been introduced. Hence, recipients of the funding will need to immerse themselves in the European political arena. Since 70 percent of the transfer payments are not directly related to the corona crisis, essentially a second EU budget is created that is financed by credit, not taxes. This reveals the main challenge: Will Europe develop enough discipline to employ the newly created funding for collaborative investment projects and create visible added value for Europe? The future for an investment union is paved. It's up to the European Union to handle it with care.



The comparison is not simple.

LORENZO BINI SMAGHI
Former Member of the Executive Board, European Central Bank

Comparing the creation of the European Union's Next Generation Fund with Hamilton's decision to consolidate the existing debt of the thirteen pre-existing colonies is not simple. On the one hand, the recent EU policy initiative does not affect existing debt, which remains the responsibility of the member states. It involves, however, the issuance of new European debt, which is a novelty, for an amount that is not that different, in terms of GDP, from the initial issuance of U.S. federal debt in the early nineteenth century. On the other hand, it should be remembered that Hamilton's decision did not prevent individual states from continuing to issue their own debt, subject to distinct rules, while the EU member states still have to respect the rules of the Stability and Growth Pact, even though the latter has been temporarily suspended. Furthermore, the license granted by Hamilton to the First U.S. Bank was not renewed by President Adams, which laid the grounds for severe financial and monetary instability in the nineteenth century, until the creation of the U.S. Federal Reserve in 1914. In this respect, the issuance of European debt takes place in a much sounder economic and financial environment.

The NextGenerationEU fund is an initiative engineered to address the effects of the Covid-19 crisis. As such, it is a one-off experiment. This does not exclude, however, that it could be repeated, in some form, in case of a new systemic crisis, determined by health or some other factor. This will depend on the success of the action for the following reasons.

First, there is demand for a safe European asset, both from European and foreign investors. The scarcity of safe assets is one of the problems more acutely felt in high-saving countries such as Germany, which explains the negative interest rates on government bonds. The increase in the supply of highly rated European bonds may reduce the savings imbalance and lead over time to more generous returns for the benefit of all.

Second, the promotion of a greater international role for the euro, which is needed to protect European companies from an excessive dependence on the dollar, requires a deep and liquid market for euro-denominated assets.

Third, the aversion of some countries to a common debt instrument derives from the fear of moral hazard, which would also lead to a rise in national debts, as occurred in the United States. Another fear is that the money raised through a common debt instrument would be wasted in unsound programs by some of the member states.

If the experiment proves instead that the skeptics were wrong, and contributes to stronger growth throughout Europe, stronger cohesion, and a greater financial independence, there would be fewer obstacles in the future to making greater recourse to joint debt issuance in case of need.

After all, the U.S. federal budget remained contained to less than 1 percent of GDP until the Great Depression and only doubled afterwards. It reached double digits during World War II.

Hopefully Europe will not need a war to get there.

Learn from Alexander Hamilton's mistake.

JOSEF BRAML
Head of the Americas Program, German Council on Foreign Relations (DGAP)

To succeed in state-building, and to avoid social and political unrest, European decision makers would be wise not to repeat but learn from Alexander Hamilton's mistake.

Hamilton, one of the most admired of the U.S. founding fathers, and the founder of the nation's financial system, was convinced that the communitization of debt—which, he argued, was due to the first War of Independence—would be the "cement" for the new American state. As the collective debt grew during the second war against the British (1812–1815), however, this approach caused a very serious moral hazard problem, and created a bursting bubble followed by a severe recession, laying the economic grounds for a future secessionist war.

When individual states expected that their debts would continue to be assumed by the federal government, loans were increasingly taken out and used to finance infrastructure investments. While this stimulus provided jobs and generated short-term economic growth, it created a bubble in the long run.

The states were willing to borrow because they assumed they themselves would not be responsible for repayment. Since creditors also expected the federal government to protect them, they were content with low interest rates. Credit growth in the second half of the 1820s fed a construction boom. When the economic bubble burst in the mid-1830s and financial markets panicked in the spring of 1837, a recession began that severely affected the young union. The federal government's ability to provide further loans for the individual states was soon exhausted. By 1842, a third of the 29 U.S. states and territories of the at that time had gone bankrupt.

The European Union may face a similar challenge—sooner rather than later. Fiscal deficits in Italy and Spain are rising and debt-to-GDP ratios are increasing rapidly—reinforced by a slower-than-anticipated economic recovery from the Covid-19 crisis. The European Central Bank will need to make even larger debt purchases from these "southern" countries in the foreseeable future, magnifying a moral hazard problem and pitting the "southern" members against the fiscally conservative "northern" members on the ECB's Governing Council—and in the European Union.

Hopefully, the EU member states will be able to manage this conflict and maintain social peace in their own countries and in Europe—and learn from history. It is not a stretch to see a link between the economic troubles in 1842 and the Civil War erupting two decades later in the United States. This war was not only about the moral and institutional questions of slavery and "states' rights," but also about money. Customs disputes and the intractable debt problem surely contributed to the tensions.

Only in the aftermath of the Civil War, with the United States' increasing foreign policy roles, were federal powers significantly increased, while still granting individual states still some degree of sovereignty and responsibility—not at least in financial matters. Yet every subsequent economic crisis gave the federal government further openings to help the member states—and itself. During the Great Depression in the 1930s, the federal government assumed in the New Deal many competences previously belonging to the states, such as road construction and the development of energy and communication networks. Since then, the federal government has supported the increasingly overwhelmed individual states in their tasks with lavish "grants-in-aid" that come with federal strings attached. This way, the dualism ("dual federalism") created by the founding fathers was replaced by a "cooperative federalism."

Europeans have their own historic mistakes to learn from, and unfolding future crises to meet with cooperative federalism. While the creation of the European economic union is the result of lessons learned from two catastrophic European and World Wars, it needs to be finalized with elements of a fiscal and political union in order to manage the tensions and opportunities the Covid-19 world economic crisis will create for Europe.

References to Hamilton make me uneasy.

LUDGER SCHUKNECHT

Deputy Secretary-General, Organisation for Economic Co-operation and Development, and former G20 Deputy and Chief Economist, Federal Ministry of Finance, Germany

The agreement on the European recovery package, covering €360 billion in loans and €390 billion in grants (plus a much-enlarged EU budget), is certainly an important step in the development of the European Union. And the reference to Alexander Hamilton has certainly raised expectations.

What are the hopes? The European Union will be able to issue debt of a much more significant amount than before. As this represents almost half the bund market—for German benchmark instruments—this has the potential of creating much more highly liquid and highly rated debt in Europe.

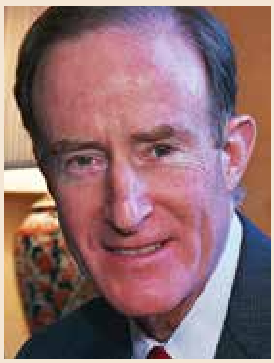
Moreover, given the prospect of a very dire budgetary situation in many member countries, this will allow for financing investment and other spending that might not otherwise happen. The need for a "reform and investment agenda," which will be discussed in European fora, reinforces economic and financial policy surveillance in the European Union. So there should be more reforms and a higher quality of spending.

But for all this to become an important step towards a strong and stable monetary union, perhaps even the "United States of Europe," a few things must fall into place. The additional spending must be productive and must come together with structural reforms. The lack of investment in Europe is rarely a question of insufficient money but more a lack of confidence, slow bureaucracy, and a lack of capacity and processes, which all reinforce the "not in my backyard problem." And often it is better, not more, spending that is needed, given our large government sectors in Europe.

As always, debt is a double-edged sword. Put to the right use, it can help in forging Europe together. But if the underlying problems are not solved, or worse, if this debt creates the expectation of easy bailouts outside European Stability Mechanism conditionality, and if a new support package is needed again soon, citizens and taxpayers in many countries will ask why they should show solidarity. In that case, the agreement in Brussels will ultimately be divisive—a Pyrrhic victory that will have just "kicked the can down the road."

The key question is this: Will there be enough of the right reforms so that growth picks up and the financial situation in all European countries becomes sustainable? If yes, Europe will come out of the crisis stronger. Call that the result of a "Hamiltonian moment" or not, it would be great.

The Hamiltonian moment in the United States was Janus-faced in that it helped solve the financial problems of states after the wars of independence but also precipitated the profligacy and state bankruptcies of later years and, some say, perhaps even the U.S. Civil War. References to Hamilton, therefore, make me uneasy. We in Europe have it in our hands to limit the parallels to the "good" ones.



European patriots should aspire to unification no less than Americans wish it for them.

BENJAMIN M. FRIEDMAN

William Joseph Maier Professor of Political Economy, Harvard University, and author,* Religion and the Rise of Capitalism *(forthcoming)

With the launch of a coordinated union-wide spending program, financed by the first-ever issuance of union-obligated bonds, has the European

Union finally taken the decisive step toward becoming a genuinely unified fiscal entity? Americans should certainly hope so. European unification has been a centerpiece of American foreign policy thinking since the days of Stimson and Kennan and Acheson. The motivation then was unity to safeguard the continent against the threat of Stalinist aggression. Today it is to avoid the potential conflict due to resurgent nationalisms, a threat exacerbated by the European Union's inclusion in recent years of several increasingly authoritarian states, each led by its own mini-Trump. But the objective remains sound, and European patriots should aspire to unification no less than Americans wish it for them.

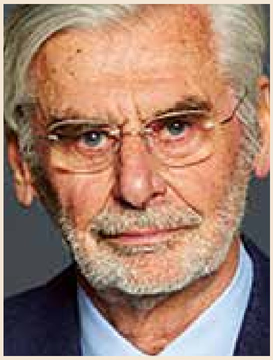
While the primary rationale for European unification is political, the cutting edge of progress on this front has always been economic. The Coal and Steel Community of the early post-war years gave way to the Common Market, then the Economic and Monetary Union, and in turn the European Union itself. A central bank followed soon after, giving most European countries a common currency and monetary policy, and most recently a banking union with a single supervisory system and mechanism for resolution in case of failure (although not yet with serious money behind it). But so far—until now—no real unity in fiscal matters.

Many of us have long thought that this final step would come only in response to some crisis. I expected the 2008–2009 financial crisis, with the threat of widespread collapse in the banking system, to be the trigger; I was wrong. Now the severe economic decline due to the coronavirus pandemic has finally spurred at least one significant step in this direction.

It is worth recalling that America's fiscal integration was not a one-step process either. True, the Constitution of 1787 gave the new federal government the power both to tax (in limited ways) and to spend, and the government's assumption of responsibility for the individual states' war debts—proposed by Alexander Hamilton and adopted by Congress early in George Washington's first term as president—established the principle and the fact of a federal debt. But outside wartime, the federal government's spending was highly limited, and federal revenues came almost exclusively from tariffs and excise taxes, or from the sale of western lands.

The government's modern taxing power dates only to the Sixteenth Amendment, ratified just before World War I. Peacetime government spending on a large scale came only with the Great Depression of the 1930s. The real enlargement of government spending came with World War II.

Within its short lifetime, the European Union has not experienced trauma anything like these formative episodes in American experience—for which we should all remain thankful. Passage of the Funding Act of 1790 was only the beginning of a very long process. Let's hope the European Union's new initiative is indeed a comparable step. But we should not expect it to mean what our own "Hamiltonian moment" didn't.



A monetary union cannot be a stand-alone system, without budgetary support. Now the crisis has forced systemic change.

MICHAEL EMERSON
Associate Senior Research Fellow, Centre for European Policy Studies

Maybe the time for the Hamiltonian moment was at the end of World War II, if Europe had then constituted an economic and monetary union, by analogue with the United States coming out of its civil war in 1790. Still the comparisons and contrasts are stimulating debating material.

The twenty-first-century European Union is now acting on the same macroeconomic scale as the twenty-first-century United States. The European Central Bank was the lone star rescue agent over the 2008 monetary crisis, with little fiscal action. This time it is a balanced package of monetary and budgetary action. Not quite a fiscal union, but a huge systemic step in that direction with massive debt-funded budgetary grant programs and commitments to raise new taxes to repay the debt.

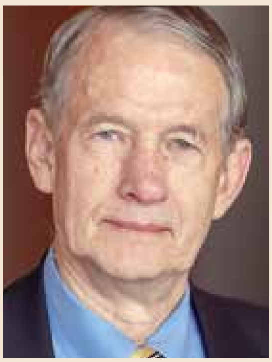
The political prerequisites to get this were formidable, yet realized: some leader had to have the guts to propose breaking the taboos, which French President Emmanuel Macron did. The visceral blocker of further integration had to get out of the way, which British Prime Minister Boris Johnson did. The biggest financial power had to change its position over balanced budgets and fiscal transfers, which German Chancellor Angela Merkel did.

A one-time action, or a ratcheting up of permanent fiscal integration? The political declarations are that this is a strictly one-time action. Not many observers seem to believe this. A one-time response to this unique Covid-19 shock maybe, but there will be other shocks to come, and the case for a structural shock-absorbing capacity in principle was already there in theory, and now has a precedent in practice. The new taxes will be happy to become permanent. Everybody already knew, without saying it, that a monetary union cannot be a stand-alone system, without budgetary support. Now the crisis has forced systemic change.

Of vital importance for the future is whether this recovery program, to be executed largely in the next two years, is done efficiently, or beleaguered with howls about delays, white elephants, and corruption. The main proposal is that the Covid-19 recovery has also to be a future-oriented "Green Deal" recovery, with emphasis on energy-saving and climate-friendly action. This is all waiting now to happen, but the script is good.

One neglected aspect is the collateral benefit for the European Union of the United Kingdom's Brexit. If the United Kingdom were still in the European Union, it would have immensely strengthened the power of the "frugal four" (Netherlands, Sweden, Denmark, and Austria). The frugal four trimmed the proposal. With the United Kingdom it would have been blocked, and never happened.

On the other hand, for the United Kingdom it will be the reverse. Adding the Covid-19 disruption to that of Brexit is going to mean a longer and deeper recession in the United Kingdom than for the European Union, which will in turn—tragically—add fuel to the pressure for a new referendum in Scotland, with increasing support to secede from the United Kingdom and apply to join the European Union.



I'm a skeptic.

GARY CLYDE HUFBAUER
Nonresident Senior Fellow, Peterson Institute for International Economics

Count me a skeptic—at least for another decade. Germany is not about to give the European Commission unconstrained authority to issue debt. Mini "Hamiltonian moments" will no doubt recur as Europe lurches from crisis to crisis. But if the U.S. Treasury had to secure acquiescence from the largest states plus Congress, U.S. national debt would never have reached $25 trillion. Commission authority akin to the U.S. Treasury's writ, even with a debt cap, is something for the European future.

Moreover, amid pandemic, it's easy to forget that inflation has been the dominant monetary phenomenon of the past century. Right-wing and left-wing European populists would welcome large-scale debt financing, and this could ultimately call for higher taxation to curtail rising inflation or shockingly high interest rates. But the European Union's tax powers are deliberately confined to insignificance—and for the moment that's exactly what member states want. Another argument against a true "Hamiltonian moment."

It is not clear whether Europe will eventually adopt greater ongoing fiscal capacity at the level of the Union.

JEFFREY R. SHAFER
Chairman of the Board of Trustees, National Committee on American Foreign Policy, and former Undersecretary for International Affairs, U.S. Treasury

The European collective debt deal has some of the main features as Alexander Hamilton's U.S. debt assumption legislation of 1790. Both were one-time initiatives to issue collective debt and thereby relieve the immediate financial distress of some of the states of the two unions. Both collective debt policies were undertaken in the face of strong opposition from less-indebted states. And neither obligated the unions to take collective responsibility for future debts.

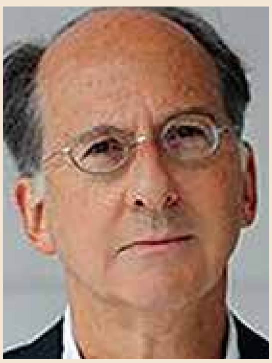
It is important for Europeans to understand what more needed to happen for Hamilton's initiative to become the modern U.S. fiscal structure and what this structure is still not to this day.

It is not a collective debt structure. Hamilton's assumption may have led European investors to believe that there would be a federal backstop of state debt in the future. The Europeans lent liberally to American states to build canals and railroads in the early nineteenth century. But there was not a backstop, and eight states defaulted in the 1840s. Confederate state debts were repudiated by the Fourteenth Amendment to the Constitution in 1868. Arkansas defaulted in the 1930s.

Looking at the debt and pension obligations of several states, it could happen again. There is still no assured backstop. The risk of state default tempers the moral hazard of lenders who would otherwise lend freely to states, leaving the federal government to pick up the pieces.

The United States nevertheless has a strong centralized fiscal capacity. This was not possible until the Sixteenth Amendment of the Constitution was enacted in 1913, which granted the federal government the power to levy direct taxes. Until then, the federal tax authority extended only to tariffs and other indirect taxes although the revenue of the government was augmented by land sales. These were coming to an end by the close of the nineteenth century. The new income tax power of the federal government was not fully developed until the depression of the 1930s and World War II pushed up federal spending and tax needs. Europe has not moved significantly in this direction.

It is not clear to me from the U.S. side of the Atlantic whether Europe will eventually adopt greater ongoing fiscal capacity at the level of the Union. It would make sense. But national governments should not have their debts collectively guaranteed. A collective responsibility to service debt must be tied to collective oversight of spending. The euro would survive a national default as it survived Greek defaults in 2011–2018 despite some collective support. The dollar has survived many sovereign state defaults.



Perhaps a different Hamiltonian moment is in order.

MARK SOBEL

U.S. Chair, Official Monetary and Financial Institutions Forum, and former Deputy Assistant Secretary for International Monetary and Financial Policy, U.S. Treasury

The Dinner Table Bargain of 1790, brokered by Thomas Jefferson between Alexander Hamilton and Virginia's James "Frugal" Madison—a supporter of decentralization and an opponent of Hamilton's vision of centralized power—provided that the federal government would assume state debts and the nation's capital would be placed in the Virginian's backyard.

Europe's leaders deserve tremendous praise for their trailblazing Next Generation EU €750 billion recovery fund accord. But Europe hasn't assumed national debts. Nor has it agreed to halfway proposals to that end—"Blue Bonds" or "ESBies." It's not a Hamiltonian moment.

More relevant perhaps, is the question of whether the recovery fund represents a major step toward fiscal union. Does it cross the Rubicon? Certainly not for the foreseeable and distant future.

Like the Virginians, the German public—and those of the Frugals—fret about subsidizing wasteful profligacy elsewhere. The Frugals bitterly fought the Merkron proposal, perhaps fearing precisely that it could be the camel's nose under the fiscal union tent.

German public opinion naturally constrains Angela Merkel. But when severe air pockets hit European economies, as they did in the global financial crisis and have again with Covid-19, and the precipice of a euro catastrophe appears, Merkel is no Wile E. Coyote. She doesn't plunge over the cliff. She knows many European nations need help and that Germany has too much invested in the euro to countenance failure. Delaying action until the last moment amid squabbles, though, undermines the integrationist momentum that could come with the actions. Additionally, when "normal" times return, it's back to incremental muddling-through business as usual.

Could the issuance of €750 billion in debt be the forerunner of a European safe asset, which ultimately competes with the dollar? Perhaps. But even if the fund will provide major support for European economies, it's still a temporary facility and the amount is small relative to euro-area GDP and the universe of European sovereign bonds. King Dollar will not lose sleep.

Could this be the harbinger of EU taxing authority? It's hard to see that now. A plastic waste tax was agreed, but green and digital taxes were not. It appears member budget contributions will finance repayments. Perhaps a different Hamiltonian moment is in order for Brussels—a "Whiskey Moment"—commemorating when Washington and Hamilton, according to lore, rode their mounts to western Pennsylvania and smote rebellious whiskey producers refusing to pay their sin taxes.

After the global financial crisis, populism, inequality, and nationalism surged worldwide, including Europe. The recovery from Covid-19 will entail severe dislocations and massive policy challenges. The forces of societal angst may further intensify, exerting centrifugal pressures for Europe.

History will ultimately judge whether Next Generation EU proves to be more Madisonian or Hamiltonian.

And back to the dinner table, is there any debate about moving Europe's capital from Brussels to Den Haag, Vienna, Copenhagen, Stockholm, or Helsinki?

A true integration of the European Union would be to first see Greece, Italy, and Spain, in that order, exit the union.

CHRISTOPHER WHALEN
Chairman, Whalen Global Advisors

The European Union has agreed to a coronavirus relief plan based on the issuance of common debt. Is this a breakthrough that will strengthen the Union or merely a necessary concession by the Dutch and Germans?

The reference to a "Hamiltonian Moment" concerns when America's first Treasury secretary consolidated the war debt of the thirteen colonies with the issuance of common debt. But the more important event, Federico Pastor reminded us in the *Financial Times* this past June, was the creation of the federal government as an entity independent of the various American states.

Only by creating an agency that could act on behalf of all of the United States did America truly move towards Union. The immutable fact of Union was forged in the fires of the Civil War, which forever closed the door on states voluntarily exiting the federal republic.

So is Europe moving in the same direction? No, by definition, it is not. First, the need to come together to address Covid-19 does not necessarily translate into a broader acceptance of the end of national autonomy that is required for true union.

For example, since everybody follows the "shock doctrine" of using crises to advance the cause of greater EU integration, there are attempts to push things further because of the Covid-19 pandemic. Proposals such as taking away budgetary rights from Germany's parliament, for example, have so far generated significant resistance. Will such efforts help or hinder EU integration?

"Were the European Union's actions strictly a Covid-19–related initiative likely never to be repeated short of another pandemic?" asks one prominent political observer in Berlin. "Further, what would be the implications if any for Europe's sovereign debt market and the euro were the EU pandemic rescue effort to become the permanent policy model?"

The European Union is clearly trying to centralize more fiscal resources in the new Covid-19 "recovery fund," but the net transfers to Italy or Spain are minuscule. The northern members of the European Union remain reluctant to come to the aid of the dissolute south, which they view as a fiscal and economic disaster. Italy is clearly in need of a debt restructuring, a fact that is likely to make Germans and other northern nations disinclined to go down the road to true fiscal union.

So does Covid-19 provide either the opportunity or the impetus for a true fiscal and economic union in Europe? Not a chance. If anything, this crisis makes more striking the economic gap between north and south without providing a mechanism for change. So long as the Italians or Greeks insist on living as they have in the past, the Germans, Dutch, and other northern European nations are unlikely to come to their rescue on an unlimited and open-ended basis.

Failing a Franco-German occupation of Italy, Greece, and Spain, there is no way to bridge the economic and political gap that exists between North and South. Indeed, the most likely course to a true integration of the European Union would be to first see Greece, Italy, and Spain, in that order, exit the union and, like Britain, become close trading partners of the core EU nations. That is the obvious solution that stares Europe in the face today.

It is probably more Roosevelt than Hamilton.

LORENZO CODOGNO
Visiting Professor in Practice, London School of Economics and Political Science, and Founder and Chief Economist, Lorenzo Codogno Macro Advisors Ltd.

It was not a "Hamiltonian moment." It is probably more Roosevelt than Hamilton. The Next Generation EU package represents a significant boost to public investment and potentially a milestone in EU economic integration. It is a sign of internal cohesion and real solidarity that goes far beyond the actual money involved.

The European Union recognized that there are "public goods" that are better managed centrally, with proper "own resources" in the EU budget. The Commission will borrow to spend on behalf of the European Union. Funds will be repaid starting from 2027 and until 2058, by the introduction of EU plastic levies, carbon adjustment measures, emission trading schemes, and digital taxes.

Countries will have to present their Recovery and Resilience Plans based on the European Semester recommendations, and these will have to be approved by the European Commission, which will allocate the funds. If a country were not perceived to fulfill the "agreed milestones and targets set out in the recovery and resilience plans," there will be a possibility to raise the issue at the level of the European Council.

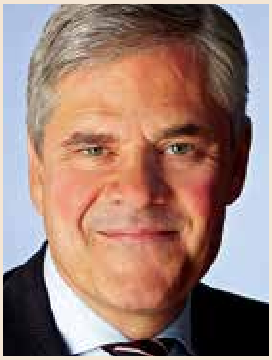
The funds will support public investment and provide incentives for structural reforms, giving laggard countries a chance to catch up in economic terms. Italy will get the largest allocation of resources, on the assumption it can put forward credible projects. As a percentage of national GDP/GNI, countries currently benefiting the most from cohesion funds will get by far the most generous Recovery Plan allocations.

The Recovery Plan is *de facto* a sort oversized "cohesion fund" and an *ex post* insurance program for countries hit by Covid-19. It is a mechanism that the European Union will likely use in the future for similar external shocks if the experience is successful. Seventy percent of the grants will be committed in 2021–2022 according to criteria linked to the level of economic development of a country. In 2023, the allocation of the remaining 30 percent will be based on each country's recorded contraction in 2020–2021 GDP. This allocation addresses both the "resilience" aspect of the package (that is, more money to those countries with the lowest GNI per capita) and the "recovery" aspect (that is, resources to those economies that will suffer the most due to the pandemic shock).

It is not a genuine macroeconomic stabilization mechanism as it lacks automaticity and immediacy. It is part of an overall policy response to address the shock and go beyond it, in conjunction with the intervention of the European Central Bank (and other EU central banks) and the temporary lifting of the Stability and Growth Pact rules. Moreover, there will be a proper EU benchmark yield curve. Once the benchmark is set and it works, it may then become a more permanent feature of the European bond market, with the potential to become a real EU "safe asset" over time.

Overall, it is not the first step toward fiscal union, as there is no *ex ante* risk-sharing or mutualization. It is a different and novel approach, a blueprint opening a different route for economic integration. It also marks a shift from sticks (strict fiscal rules and reform demands) to carrots (incentives with money attached).

There is a residual risk of non-approval by the European and national parliaments. However, they will hardly risk taking such an enormous responsibility as would come from voting down the plan. Once approved, a much more severe challenge will come from its implementation. If the package fails to translate into credible measures to enhance potential growth by helping the green and digital transformation of the EU economy, it will end up being a waste of resources, threatening the sustainability of countries' public debt, and eventually derailing further European integration.



The greatest danger lies in the disappointment of EU citizens.

ANDREAS DOMBRET

Global Senior Advisor, Oliver Wyman, former Member of the Board, Deutsche Bundesbank, and former Member of the Supervisory Board, European Central Bank

The Covid crisis has prompted Europeans to take unprecedented initiatives to protect their economies. The European Central Bank acted swiftly by establishing its "Pandemic Emergency Purchase Program" with an envelope of €750 billion to backstop debt markets. Fiscal policy had to act, too: The EU Council agreed to a €750 billion package of loans and grants. Enthusiastic labels have been attached to this decision calling it an "Hamiltonian moment." Can the measures justify such high praise?

The EU package is a one-off extraordinary initiative aimed at kickstarting economies and at providing funds to compensate for the economic contraction caused by Covid-19. But the hardest-hit European economies also need to address deeply structural issues unrelated to Covid in order to close the gap with the more competitive EU economies. And the European Union still lacks the governance mechanisms of a "true" fiscal union and therefore still falls short of what a "Hamiltonian moment" is all about.

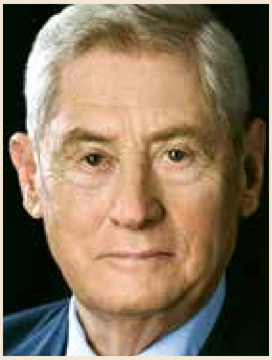
The "noble right" of any parliament in democracies is to decide on budget policy and, residually, on debt. The Council package does not have such a mechanism.

Taxpayers of country A fund the expenses of country B without having a say on their use and vice versa, which was key to reaching Council consensus. The compromise of providing veto powers—given the lack of "real" fiscal governance—may lead to new rifts between members while EU member states continue to be unwilling to cede sovereignty on tax and spending measures to the European Union in the foreseeable future.

The effect of the welcomed Council package will therefore be an important reality check for future ambitions of the European Union. Should it become evident that the committed €750bn is not well spent and does not support tangible convergence of European economies, further steps toward a fiscal union will be even be more difficult to justify. The concerns of the "frugals" therefore need be taken seriously, keeping in mind that similar disagreements prompted the United Kingdom to leave the Union.

The concerns prominently voiced by the "frugals" are widely shared among EU citizens. Integration must be seen as a sustainable path, not as a crisis bandaid without any alternative. Being transparent on consequences, drawbacks, and risks is important for any future buy-in, as an "integration through the back door" could eventually undermine the entire European project. The greatest danger lies in the disappointment of EU citizens.

Conditionality and governance therefore are key. The European Union must ensure that the economic stimulus is spent wisely and supports sustainable recovery and convergence. Strategic targets such as digitalization as well as managing climate and environmental risks may, however, not divert attention from the need to increase productivity in all European countries as well as from efforts to fully utilize and train the workforce in an increasingly complex world.



A design fault in the architecture of the European monetary union makes recurrent crises more likely.

HANNES ANDROSCH

Former Finance Minister and Vice-Chancellor of Austria

In Europe, nothing happens in a moment. Fundamental changes occur minimally and slowly, at best. Thus, great significance is being attached to the fact that the European Commission is authorized—for the first time—to borrow on international capital markets with the full fiscal backing of the European Union. This is novel, and in the views of many experts reaching back to Milton Friedman, long overdue.

As a gesture of solidarity with the countries most affected by Covid-19, it is to be warmly welcomed. It may even be the thin end of the wedge which will lead to further, similar responses in the future. But for now, it is strictly a once-off program and light years removed from the fiscal and transfer union required to support the European monetary union and its currency, the euro.

For one, it is structured as just another program. It fits into what passes for an EU budget but which, in reality, is a rigid framework for (some) collective national expenditures, without scope or need for deficit financing.

Second, it is a tool of the twenty-seven member countries of the European Union, and not of the nineteen members of the eurozone. As such, its responsiveness to the requirements of the euro is likely to be limited. And, more important, it does not confer any degree of fiscal autonomy on an unelected European institution with responsibility for safeguarding the euro. This remains with the heads of government of the EU member countries, whose primary allegiance is to their national electorates. Worse, any such decision by this body would have to be taken unanimously, giving the heel-draggers the final say.

A monetary union requires an adjunct fiscal arm, with fiscal autonomy, to provide support for regions in recession when business cycles are not largely synchronized. Second, a fiscal authority is also important on a union-wide basis when "liquidity trap" conditions prevail. And, in the absence of European treasury-type securities, the development of the euro as a global rival to the dollar is inhibited.

But arguably the main reason why such an institution is essential to the stability of a monetary union is to effect transfers when internal real exchange rates, and thus the competitiveness of regions, are disrupted. Without such transfers, economically weak regions which run payments deficits will become progressively more depressed. In the United States, such transfers are implemented between the economically powerful northeastern states and the poorer southern states. In the European Union, the prosperous states, including Germany, Netherlands, Sweden, and Austria, which benefit most from the union, not least from undervalued real exchange rates, are unwilling to countenance any targeted transfers to the southern (Mediterranean) states which are languishing, *inter alia,* from over-valued real exchange rates.

The United States and European Union provide a telling contrast. In the United States, total government expenditure amounted to 34 percent of GDP (2018), with 55 percent accounted for by the federal government and 45 percent by state and local governments. In the European Union, almost all public expenditure is undertaken by country governments, 45.8 percent of GDP on average (2019), with EU Commission expenditure accounting for about 1 percent of GNI. In the United States, unlike the European Union, almost all discretionary spending is undertaken by the federal government. The EU budget does provide for transfers but they are not designed to remedy situations of cyclical or competitive disparities.

A federal fiscal authority alone does not guarantee the avoidance of monetary crises. But this design fault in the architecture of the European monetary union makes recurrent crises more likely. Until this has been rectified, the new securities will remain a curiosity rather than lead to the emergence of new financial markets.

The crisis has forced Germany to abandon its near-obsession with domestic fiscal caution.

JIM O'NEILL
Former Commercial Secretary to the Treasury, United Kingdom, and former Chairman, Asset Management, Goldman Sachs International

As the famous phrase goes, time will tell. And as another one goes, never let a crisis go to waste. What is certainly clearer five months into this pandemic is that Europe is responding to the challenge better than the United States. As the northern summer creeps on, this is something financial markets are taking note of, as the dollar loses some of its excessive strength, with the euro playing its own role along with other currencies.

Since the financial crisis of 2008, with the absence of a shared fiscal debt instrument, the weakness of the euro project has been only too stark. In the earliest days of this crisis, with Italy at its epicenter, it was quite clear that unless euro policymakers acted in a different way, we could be headed for a new version of the recent Greek crisis, but on a much grander scale. In this regard, I have often believed that there would come a point where core European policymakers, especially in Germany, would be forced to declare a stronger hand on whether they want to commit to support to Italy or not. I suspect this point has now come.

As a founding member of the European Union, Italy has always been at the center of contradictions about the EU project, and when it became a founding joiner of the euro, these contradictions become more stark. Many have often found it difficult to understand why Italy was in the euro.

Due to my own earliest experiences of understanding the broader nature of the euro project, however, especially its historical context and its geographic and social nature, it was clear to me that Italy was highly likely to join the euro, and would become a source of frequent turbulence.

One of my more fun memories of my most active days in financial markets was at the top-floor restaurant in a beautiful hotel in Rome where we hosted around twenty top U.S. fund managers in early 1998. They had all just arrived from Frankfurt on day four of a European tour to consider the prospect of the euro coming into existence at the start of 1999. A mere two of them thought, after arriving from presentations at the Bundesbank, that Italy would be in. I offered to bet them all that they would be wrong. None of them took me up on it, unfortunately!

Italy has had a poor track record for decades on economic policy, with each of the two crucial ingredients—poor demographics and poor productivity—responsible.

If this weren't bad enough, for the first twenty years of the euro's existence, Italy has been constrained by the euro macro policy framework, the "just below 2 percent" inflation target mandated for and by the ECB and the 3 percent deficit limit. Both of these, interpreted in Germany as though it has to show the best leadership on both, constrain many other members to almost persistent nominal GDP constraints, if not outright deflation.

Not surprisingly, this has tested even the most committed euro fans in Rome and Milan and elsewhere. With the horrific shock of Covid-19, something had to change. It has, and I applaud German Chancellor Angela Merkel for not letting this crisis go to waste, and embracing more fully that Italy—and everyone else—are collective members of the euro, and not just some bolt-on that German exporters can constantly benefit from.

So I don't know if this is a Hamiltonian moment, but it might be. Equally important, the crisis has also forced Germany to abandon its near-obsession with domestic fiscal caution. This together with the new EU fund raises the genuine hope that not only could the euro framework have a more credible path in coming years, but the European Union might not be as dependent on external growth in the decade ahead. Germany and the rest of the continent could generate some internal growth which will be sorely needed given the challenges elsewhere in the world.

The agreement will help to do for the evolution of the EU what Hamilton's ideas did for the United States.

JAMES E. GLASSMAN
Managing Director and Senior Economist, JPMorgan Chase & Co., and Head Economist, Chase Commercial Banking

The European Union's summer fiscal agreement, whether it was a "Hamilton moment" or not, will be remembered in the future as yet another important step towards greater economic and political integration that kept Europe's historic experiment on course. And it will defuse Covid-19 pandemic stresses that would widen the economic gaps among the twenty-seven members.

The significance of the summer agreement isn't its unique response to the Covid-19 crisis, although it was unique. It contained two components. One was the regular EU budget (referred to as the multi-annual financial framework, or MFF) worth about €1.1 trillion spread out over seven years. Another component was an unprecedented one-time "Next Generation EU" fund of €750 billion to help countries recover from the Covid-19 shock. It consisted of €390 billion of grants with the rest debt-financed.

The significance of the agreement wasn't that it delivered what a fiscal union would (the European Union has yet to design such a system), although it effectively did that. And that complements national countercyclical programs like Germany's popular Kurzarbeit ("Short Work") Program that has been around since the Weimar Republic and guards businesses against short-term disruptions.

The significance of the agreement wasn't that it broke some taboos, although that it did. Europe's leaders agreed that the European Commission, acting on behalf of the member states, may incur debt at an unprecedented scale. The NGEU will be funded by debt issued over six years that can have maturities out to 2058. And the €390 billion of grants breached a "red line" that had been assumed for intra-EU fiscal transfers.

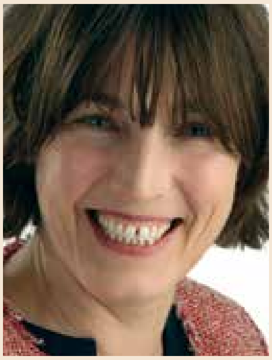
The significance of the European Union's summer agreement wasn't in its size, although the size was impressive. The €750 billion total NGEU amounts to about 5 percent of EU GDP (it will be spread out over several years) and complements national countercyclical programs. The funds fill the budgetary hole left by the United Kingdom's exit from the European Union.

The significance of the agreement wasn't that it followed up on the European Central Bank's pleas to balance its monetary activism, what would be expected of a country that has at its disposal monetary and fiscal tools. But it did that.

The significance of the European Union's summer agreement wasn't that it will provide investors with a steady stream of safe assets like that of the U.S. fiscal authorities. But it will do that.

And the agreement didn't assume national debts like Hamilton's plan did in 1790. And the new common debt will not enjoy joint-and-several guarantees. And the question of how to repay it is left for later. But it opens the door, even if governments have long been unwilling to hand tax-raising powers to Brussels, because the money must be found to repay the new debt.

The European Union's summer agreement qualified as a "Hamilton Moment," because, like the many steps before it that have created the European Experiment, including Mario Draghi's unforgettable "do what it takes" declaration on July 28, 2012, amid growing speculation that the European Union would splinter, it demonstrated a commitment to the idea, born out of a tumultuous history seventy-five years ago, that the region's shared interests far exceed national ambitions. The commitment to the idea is more important than when and how the remaining pieces of the policy architecture—a fiscal union and a banking union—come together. So surely the agreement will help to do for the evolution of the European Union what Hamilton's ideas did for the United States.



A Hamiltonian moment? No.

MERRYN SOMERSET WEBB
Editor-in-Chief, MoneyWeek

If your dream is a United States of Europe, you may not much mind a crisis: it is usually one of these that prompts a new step towards EU integration. So it is with Covid. The strict lockdowns most EU governments adopted as their main pandemic policy have created economic carnage across the continent.

The European Central Bank has done its bit—but also asked and asked for a dose of fiscal intervention as well. The Commission has delivered; its latest seven-year budget is to be bumped up with a €750 billion Next Generation EU Fund to help the worst-affected countries.

This comes with three interesting bits. The first is that €390 billion of the cash is to be distributed as grants, not loans—usually the European Union likes to pretend that it is not in the business of fiscally transferring between rich and poor EU members by dressing transfers up as loans.

The second is that the cash is to be directly borrowed by the Commission with the issue of new bonds with various maturities from three years up (extending to 2058) and guaranteed by its own revenues. Previously, Eurobonds have been jointly guaranteed by the EU countries.

The third relates to the second—if the Commission is to guarantee payback from its own revenues (known as "own resources" in EU speak), it's going to have to bump them up. Right now the Commission gets a smallish flow of cash from the EU countries in the form of customs revenues and a percentage of each country's VAT revenues. That's not enough—so the new deal comes with a new ability for the Commission to raise own resources via new taxes (on digital activities and carbon, for example).

This is all-important. It means the Commission will no longer be just a middle man between national tax revenues and EU spending. It can leverage its own budget with common debt. It also means that it can directly subsidize countries for the first time. Neither of these things could have happened (indeed been imagined outside the minds of fanatics) this time last year.

You can argue that this is a one-off, that the amount is not that big (€750 billion is small beer in a money-printing world) and note there is an "emergency brake" in there (allowing countries to object to the way others spend grant money). But the history of EU emergency brakes is not a useful one.

We also know there is little so permanent as a temporary EU scheme that advances the federal cause: note the way in which the European Financial Stability Facility (created as a bailout vehicle in 2010) is still with us. Future crises are bound to be met with similar schemes. And the definition of a crisis will be fast watered down, particularly given the low rates at and ease with which the European Union will be able to borrow.

The NGEU fund does then represent a real moment for the European Union. But a Hamiltonian moment? No. This deal looks as if it brings EU countries closer together—as if it is the kind of muddle-through that makes the European Union's survival more likely than less. But there is a chance that its explicitness does the opposite. Several one-time red lines have already been crossed here—and the own resources one is yet to come. Many EU populations already find their financial obligations to the EU irritating. But at least the cash they send it is non-direct. New taxes levied directly on their activities to pay for things they didn't vote for might make them wonder again about the democratic legitimacy of the European Union.

The European Council President referred to the magic of the European Project when this latest deal was announced. Like all magic, it might work best in the dark.

The comparison to Alexander Hamilton ignores huge differences to the EU plan.

MICHAEL J. BOSKIN

Hoover Institution Senior Fellow and Professor of Economics, Stanford University, and former Chair, President's Council of Economic Advisors

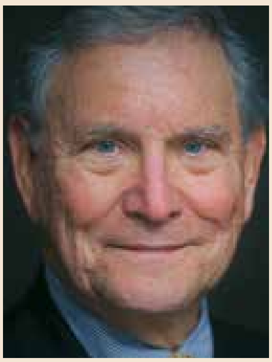
I am not even remotely convinced that the European Union's coronavirus relief plan based on the issuance of common debt is a major move toward more permanent fiscal and political integration. The comparison to America's first Treasury Secretary, Alexander Hamilton, consolidating and assuming the Revolutionary War debt of the thirteen separate colonies misreads the circumstances at the time and ignores huge differences to the EU plan.

First, the common debt issuance is a tiny fraction of the member states' debt. Second, and perhaps most important, Hamilton famously argued that the federal government assuming the colonies' debt was the "price of liberty." Covid-19 is certainly a tragic disruption, but virtually nobody believes the fight to overcome it will be permanent and as costly as, for example, World War I or World War II. Avoiding another conflagration on the European continent was the main motivation of the founding generation of the European Union's predecessor.

Third, while the thirteen colonies thought of themselves as independent colonies, accurate history suggests a sizable fraction of their populations wanted reforms, but not independence from Great Britain. Unlike most EU member states, America's states had no long history as independent nations, with often brutally antagonistic histories and religious and language differences, not to mention conflicting territorial ambitions. So while substantial obstacles had to be overcome in forming a common political union—Washington and Jefferson had to travel the country to build up support for ratification of the Constitution—these were trivial compared to those to forming a real robust political union for the European Union. Indeed, the European Union's requirement of consensus, legally meaning unanimity, creates huge hurdles for moving much further in the direction in fiscal and political union other than in a temporary emergency situation.

A glance at the European Union's complex jerry-rigged organization structure, with those in and out of the euro, the Schengen area, two associated trade zones, and the like reveal how difficult it is for complete agreement. Add in the history of violation of Maastricht Treaty deficit and debt requirements and the difficulty of enforcing them.

Finally, the European Union adds a third supranational layer on top of the fiscal and other responsibilities and resources division between central and subnational governments already under substantial strain in several EU sovereign nations. Witness the Catalonia independence movement and similar threats from Venice and the Veneto, and before Brexit, Scottish devolution. Similar strains exist in the United States. So it is a huge stretch to envision citizens surrendering even more authority to the supranational European Union.



A shift from antiquated short-term individualism to forward-thinking generationalism is occurring.

ROBERT DUGGER

Co-Director, University of Chicago Human Capital and Economic Opportunity Global Working Group, former partner, Tudor Investment Corporation, and co-founder, ReadyNation

The European Union's Covid recovery fund is a Hamiltonian moment, but not for the reason many people think. Yes, the fund's creation has similarities to Alexander Hamilton's 1790 proposal for handling U.S. Revolutionary War debts. However, there is a more fundamental reason than simply developing a deep liquid government debt market. A shift from antiquated short-term individualism to forward-thinking generationalism is occurring. The shift is revolutionary.

For Hamilton, the main social, political, and economic challenges of America in the 1700s required escaping the dead grip of aristocratic and church rule. The answer was a philosophy of individual and business liberty and a war to obtain it. Challenges of comparable scale today include climate change, government debt, and elite political control. These challenges affect generations. To address them, the work of the current century is to establish that individuals and businesses have unalienable obligations to communities, society broadly, and future generations.

Hamilton was aware of the tension between individualism and its short-termism and the needs of society and future generations. His life was an expression of Enlightenment Revolution aspirations. He supported the goals of the U.S. Constitution's Preamble including the last and most important, "to secure the Blessings of Liberty to ourselves and our Posterity."

However, in the explosive expansion of industrial capitalism in the 1800s, the United States drifted away from the Preamble's generational concerns. Captains of industry supported securing liberty for themselves but opposed having to consider the interests of "Posterity." They steadily persuaded politicians and judges that the Preamble is substantively meaningless. By the end of the century, as William Treanor, Dean of the Georgetown University Law Center, concludes, "the Supreme Court came to view the Preamble as simply introductory fluff." The generational reference, "our Posterity," became meaningless.

The European Union's fundamental laws acknowledge generational interests explicitly. The French constitution, for example, says "… the needs of the present generation should not jeopardize the ability of future generations … to meet their own needs." The German constitution says the state must be "Mindful also of its responsibility towards future generations…". While the context of these provisions is environmental, the principle would apply to policy areas that impact future generations in other ways, including government debt burdens, income inequality, and elite political control. The emerging EU constitution recognizes generational interests comprehensively. It says the European Union exists to "secure a free, peaceful and sustainable future for generations to come."

Viewed through this lens, generation-spanning challenges are not limited to climate change or government debt. They also include many aspects of transportation, internet infrastructure, and EU security, and some aspects of nutrition, education, and family support.

Covid-19's impact on longer-term EU economic conditions, and potentially its political stability, makes the disease a generational challenge. The Covid fund is a step in the direction of generationally responsible policymaking. Because solving long-term problems is key to global competitiveness, the European Union is making clear progress.

The United States lacks a generational commitment and is suffering the consequences. The European Union's generational commitment is strengthening. Its competitiveness will no doubt do the same.

Eurozone voters must never be left feeling helpless again.

RICHARD C. KOO

Chief Economist, Nomura Research Institute, and author,* The Other Half of Macroeconomics and the Fate of Globalization *(2018)

Many elected leaders of eurozone countries and their voters have been shocked to find that they have no fiscal or monetary policy levers with which to fight the Covid-19 recession, the fastest and deadliest economic collapse in living memory.

Member states willingly gave up sovereignty over monetary and exchange rate policy to the European Central Bank when they joined the euro. But they also lost sovereignty over fiscal policy—not only because of the Fiscal Compact, but also because of the ease with which capital can flow between the eurozone's eighteen different government bond markets, all of which use the same currency. Under this arrangement, any member government deviating from the norm established by the best fiscal performer is punished by capital outflows and higher interest rates.

In contrast, countries outside the eurozone have been able to fight the public health crisis and the recession by increasing their borrowing, especially from investors who must hold high-quality bonds denominated in the domestic currency. Some, like the United Kingdom, have even been given the opportunity to borrow from their own central banks on an emergency basis. They can also boost the economy by allowing their exchange rate to weaken.

As more European voters began to realize that their helplessness stemmed from their membership in the eurozone, support for the European project quickly began to dissolve. Fortunately, German Chancellor Angela Merkel and French President Emmanuel Macron were politically astute enough to recognize this existential threat to the project and led the negotiations on a €750 billion package to help the helpless.

Whether this package constitutes a Hamiltonian moment or not depends on how the leaders of member states viewed the negotiations. If the four-day ordeal gave them the sense that there is enthusiasm for a fiscal union, such an outcome may actually be realized. But even if they believe a fiscal union is out of the question, they must still make sure that eurozone voters will never be left feeling helpless again.

To ensure that member states and their voters are empowered to decide their own future, a new mechanism is needed to contain the capital flight between government bond markets that has robbed member states of their sovereignty over fiscal policy.

One somewhat counter-intuitive solution to this problem is a fiscal dis-union, whereby member governments give up their rights to sell bonds to foreigners in exchange for complete fiscal freedom. As I proposed in "How to Save the Euro" (*TIE,* Winter 2020), this approach addresses the capital flight and fiscal sovereignty problems that are unique to the eurozone by making fiscal financing an entirely internal matter of individual countries. Another, less drastic, solution may be to introduce different risk weights to reduce the near-perfect substitutability of bonds issued by member states.

By combining such a policy with the Euro-wide bond issuance authority already made available by the recent package for challenges requiring a region-wide response, it may be possible to advance the European project with greater support from voters. ◆

THE INTERNATIONAL ECONOMY

THE MAGAZINE OF INTERNATIONAL ECONOMIC POLICY

220 I Street, N.E., Suite 200
Washington, D.C. 20002
Phone: 202-861-0791 • Fax: 202-861-0790
www.international-economy.com
editor@international-economy.com