

Eurozone: Signs of life from the French-German axis

Just when you thought it was all over for eurozone reform, the French-German axis returns with a proposal for a eurozone budget



The German Chancellor and French President, July 2017

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Eurozone finance ministers meet again over the weekend to discuss possible measures for further integration in the eurozone. Remember that a deepening of the monetary union was high on the agenda in the second half of 2017 after Emmanuel Macron had won the French presidential elections, but was then paralysed by German politics (and the unwillingness of other countries). Another attempt for further eurozone reform was made in the first half of this year, leading to a half-baked decision to make the ESM a backstop to the European bank resolution fund. There were also ambiguous declarations of intent and even more vague plans to finalise a banking union, start a eurozone budget and morph the ESM into an EMF. The question is how many precise results will eurozone finance ministers be able to present to their government leaders, who in turn hope to present – next to Brexit – some positive European news at the December summit.

Time is clearly running out and the latest Italian fiscal escapades have done little to increase the appetite for more fiscal integration or additional transfers of any kind. Therefore, our expectation is still that the December summit will not produce any significant breakthrough, besides making the ESM a financial backstop to the bank resolution fund (SRF), probably with some strings attached.

Any additional decisions would be a surprise but who does not want to be surprised, shortly before Christmas?

New details on the eurozone budget proposal

In the category “potential positive surprises”, last Friday's reports of a French-German paper on a eurozone budget were remarkable. The two-pager outlines a possible structure of a eurozone budget, following up on the Meseberg Declaration of France and Germany. In a nutshell, such a eurozone budget should foster convergence and incentivise reform implementation by co-financing public expenditures. The eurozone budget would be part of the entire EU budget but would be managed by the eurogroup and eurozone government leaders through another inter-governmental agreement. The French-German paper does not say anything about its possible size and remains vague on the revenues for such a eurozone budget. Remember that Angela Merkel once said she envisaged a small double-digit billion sum for such a budget. Given the inter-governmental nature of the budget in this proposal, the idea of a eurozone finance minister seems to have been killed already, while at the same time, the deficit of too little democratic accountability has not been tackled either. The European Parliament would be sidelined.

Will it fly?

It will now be interesting to see how the other eurozone countries react to the proposal. Don't forget that the so-called New Hanseatic League, the Netherlands, Ireland, Nordic and Baltic countries, have opposed most reform proposals, particularly those involving more money, in recent months. We remain sceptical that the next few weeks will really deliver more than the backstop option for the ESM, but the lower the expectations, the higher the chances for a positive surprise. Even a small eurozone budget would fall into this category.

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