EXECUTIVE COMMITTEE

Brussels, 1-2 December 2010

Agenda item 5c

A New European Debt and Investment Initiative

Annex:

- A transfer of national debt to the ECB and a European New Deal

The Executive Committee is requested to agree to take this initiative forward in discussions with European authorities.

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A New European Debt and Investment Initiative

1. Attached is a note with an idea to try to get Europe off the road to austerity and on to a highway to growth.

2. It draws on the experience of President Rooseveldt's New Deal of the 1930s and the experience of Marshall Aid, and develops the case for
   a) Transferring a major share of national debt to the ECB, and
   b) Net European bond issues to finance the European Economic Recovery Programme.

3. It should be seen alongside other ETUC proposals for a Financial Transaction Tax, a tax on excessive bonuses and a tax on business profits not being used for reinvestment. It also aims to steer the pressure away from deflationary wage and pension cuts and onto sustainable growth, which will require increased spending power.

4. The Executive Committee are asked to agree that the ETUC opens discussions with the European authorities or this initiative. Clearly, at present, some member states will be opposed as they will regard the proposals as infringing their sovereignty but as the debates about economic governance develop, it is important that the ETUC seeks to draw the focus away from concentration on tougher fiscal rules and more towards growth and solidarity.

5. The aim would be to hold a conference on the subject with invited guests from the Council, Commission, the ECB and employers to invite Commissioner Rehn to a future meeting of the Executive Committee, and to feature the initiative at the Athens Congress.

<u>**Annex:**</u>

A TRANSFER OF NATIONAL DEBT TO THE ECB AND A EUROPEAN NEW DEAL

Summary

Cutting debt, deficits and wages poses a major crisis for both European governments and the European project. The ETUC calls for a twin strategy to stabilise the current crisis by (1) transferring a major share of national debt to the ECB and for (2) net European bond issues to finance the European Economic Recovery programme. In so doing it draws on the precedent of such a strategy in the US New Deal whose success inspired the postwar European Recovery programme of Marshall Aid and inaugurated three decades of full employment, consensual social partnership and prosperity.

Clear and present dangers.

Europe needs a New Deal. The dream of 'ever closer Union' and of a single currency risks becoming a nightmare for 16 million registered unemployed, millions more who do not quality for benefits, and the risk of a lost generation of young people whose prospects of long-term employment now range from low to nil.

People realise well that the incidence and scale of the current debt crisis in some cases is due to the irresponsibility of European member states, but that this has been dwarfed by the speculative greed of banks and hedge funds whose client rating agencies deemed them as safe as US Treasury bonds until they collapsed.

Few people may know that the commitment of the 1986 Single European Act, the first revision of the Rome Treaty, was to the 'twin pillars' of both an internal market and economic and social cohesion.

But they had presumed that a single currency would add value rather than detract from it, and are disposed to abandon the European project if its leaders cannot show that they can make a reality of its earlier ambition for a Social Europe which can safeguard them against a financial crisis that risks a double dip recession, if not a second slump.

We therefore call upon the European Council and Ecofin, with support from the European Parliament and the European Commission, to adopt a proactive response to the current crisis by two key measures:

1. To endorse a **tranche transfer** of the national debt of Eurozone member states to Eurobonds held by the European Central Bank similar to US Treasury Bonds which do not count on the debt of California or Delaware and which need not count on the debt of European member states.

To do so for Eurozone debt of up to 60% of GDP which is the national limit allowed by the Stability and Growth Pact.

To require member states to service their share of the ECB Eurobonds but thereby enable the most exposed to do so at lower interest rates, avoiding the risk of serial defaults which would damage the whole of the European economy.

Thereby stabilise the Eurozone and attract purchase of Eurobonds by the central banks of surplus economies and sovereign wealth funds, securing the euro as a reserve currency and contribute to the more plural global reserve system which is one of the principal aims of the emerging economies.

2. To support an **investment led recovery** funded by the European Investment Bank and national public credit institutions both through their own financing and by drawing on Eurobonds, thereby fulfilling the commitment of member states and the European Parliament to a European Economic Recovery programme.

While the EIB only co-finances investments, the ECB should on-lend the investment in EU Bonds by sovereign wealth funds and the central banks of surplus economies to national credit institutions such as the Kreditanstalt für Wiederaufbau, the Caisse des Depôts et Consignations and the Cassa Depositi e Prestiti to enable matching finance for the recovery programme.

Such a recovery programme would counter current risk of a beggar-my-neighbour deflation, enable a rising level of EU employment, respect the commitment of the Single European Act to economic and social cohesion, and contribute to a balanced global recovery which is a central aim of the G20.

Rationale

A European New Deal

The Roosevelt New Deal gave the US the confidence to fund the Marshall Aid programme from which Germany herself was a beneficiary. The key to it was borrowing to invest through US Treasury bonds. These do not count on the debt of American states such as California or Delaware. Nor need European bonds count on the debt of EU member states.

Many economists have claimed that Europe cannot save itself until it has fiscal federalism to transfer resources from stronger to weaker member states. Germany is strongly opposed to this. Yet Europe neither needs such fiscal federalism nor an 'economic government' to finance a New Deal style recovery programme. The institutions and powers already are in place.

The European Investment Bank - already twice the size of the World Bank - issues bonds which are its liability rather of member states, which is why the major Eurozone governments do not count funding from it on their national debt.

From the Amsterdam Special Action Programme of 1997 the EIB has been given joint cohesion and convergence remits by the European Council to invest in health, education, urban regeneration, environmental protection, green technology and support for small and medium firms.

Since 1997 the EIB has quadrupled its annual lending to €80 billions or two thirds of the 'own resources' of the European Commission. It could readily quadruple this again by 2020 which would be equivalent in funding to postwar Marshall Aid.

EIB co-finance for investments could be matched by net issues of EU bonds or € bonds by the ECB which would attract surpluses from the central banks and sovereign wealth funds of emerging economies and stabilise the eurozone.

Nor does this depend on the ECB rather than governments. Article 282 of the Lisbon Treaty confirms that the ECB's primary objective shall be to maintain price stability. But also that 'without prejudice to that objective, it shall support the general economic policies of the Union in order to contribute to the achievement of the latter's objectives'.

This mirrors the constitution of the Bundesbank which obliges it 'to support the general economic policies of the government' while the European Council also is Treaty empowered to define 'general economic policies' of which one already is the European Economic Recovery programme. With the EU heading for recession there is no risk to price stability rather than a disintegration of the Eurozone.

The Stability and Growth Pact

The revised Stability and Growth Pact of March 2005 also allows exceptions for member states which spend on efforts to 'foster international solidarity and to achieving European policy goals, notably the reunification of Europe if it has a detrimental effect on the growth and fiscal burden of a member state'.

To take four points from these revised terms of reference for the SGP

1. The European Economic Recovery Programme clearly is a 'European policy goal' which has been adopted by governments and endorsed by the European Parliament

2. There has been a 'detrimental fiscal burden' for most member states since they salvaged the toxic debt of major European banks

3. There will be a 'detrimental effect on the growth' of member states if national debt and deficits are cut without a counter recessionary recovery programme.

4. A beggar-my-neighbour deflation when Europe is a third of the global economy will not 'foster international solidarity'

An Ecofin or European Council clarification that national co-finance for EIB projects should not count on national debt therefore is legitimated by the revised SGP.

No new criteria for such national co-finance for recovery investments need to be devised. They already have been remitted to the EIB by successive European Councils since 1994, i.e. trans-european transport and communications networks (Essen, 1994); health, education, urban renewal, urban environment (Amsterdam and Luxembourg, 1997); green technology, support for small and medium firms, and convergence and cohesion (Lisbon 2000).

Approval and monitoring of the investments and their co-finance would be by the EIB, which it has done with notable success since Amsterdam. The ECB thereby would remain the guardian of stability. But the EIB, with national co-finance from Eurobonds, can safeguard growth and cohesion.

A 'TrancheTransfer'

A 'tranche transfer' of national debt of up to 60 per cent of GDP to the ECB would not be a debt write-off. The member states whose bonds are transferred to the ECB would be responsible for paying the interest on them, but at much lower rates.

Such a transfer has been proposed by the Brueghel Institute in Brussels, recommending a new institution to manage the transferred debt (Bruegel Policy Brief 2010/3. www.brueghel.org).

The criteria for such a tranche transfer of debt would be a ratio of remaining national debt to GDP at the time of the transfer.

Thus, if an investor holds a billion euros in Italian government bonds and Italian debt is 120% of GDP, half of these bonds of whatever maturity is transferred to the ECB. The investor gets a lower interest rate but a more secure investment.

In our view the optimal institution to hold such a tranche transfer is the ECB. But if one or more member states remain opposed to such a transfer, it is open to others to invoke the provision for enhanced cooperation within the Lisbon Treaty and to establish a new institution to manage the transfer, as in the Brueghel proposal.

Enhanced cooperation in the EU Treaties is nominally adopted only by a minority of member states. But the creation of the euro itself was a *de facto* act of majority enhanced cooperation, since it was not imposed on the remaining minority. Article 329 of the Lisbon Treaty provides that any member state may 'request to establish enhanced cooperation'.

17 November 2010