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One for all, all for one? Better not

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Moritz Kraemer -- Chief Economist

LBBWResearch@LBBW.de

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Now is not the time to ruminate about more joint EU debt

The financial media reported that Chancellor Scholz signaled a German willingness to continue issuing joint debt in the EU on the sidelines of the first XXL summit of the so-called European Political Community.

Hopefully that statement was "taken out of context", as the saying goes. Even if one felt positively inclined towards further socialization of European sovereign debt – and we certainly are not! – now is not the time for bold experiments. Just ask the British Prime Minister! Accordingly, Berlin has already rowed back.

Scholz's signal on further EU joint debts was a mistake

Some context

Shortly after the outbreak of the Covid pandemic, the EU decided on a massive community issuance program to put Europe's "reconstruction" on a solid financial footing throughout the continent. Through the EU Next Generation (NGEU) program and its little sister, the SURE program, the EU can issue over €800 bn in bonds. A significant portion will flow as non-repayable grants. The EU debt is to be repaid by future transfers from all member states to the EU budget.

This unnecessarily reawakens a dormant controversy

Debt socialization was explicitly conceived as a one-off exception. Otherwise, the approval of the "frugal" northern European member states would not have been conceivable. The chancellor knows this. As finance minister, he was closely involved in the design of the Covid emergency funds at the time.

It is not clear why Chancellor Scholz, who otherwise does not have a reputation for wearing his heart on his sleeve, expressed a possible willingness on Germany's part to take a further step into a European debt community. Perhaps it was an attempt to counter European criticism of his €200 bn "double ka-boom".

Why the signal comes at an inopportune time

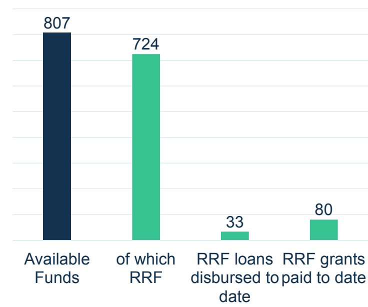
First, there is currently no shortage of Community funding at all. Only a little over €100 bn has been disbursed from the NGEU program (see chart). So there is still a multiple available. Money is not in short supply. In any case, it is premature to talk about extending debt socialization before one can be sure that NGEU has been a resounding success.

Politically, the move is also unhelpful. Peace within the traffic light coalition has become brittle as never before. Scholz will know that a further step toward debt union is a red line for his liberal finance minister. All the more so because the FDP has been intent on raising its own profile since the Lower Saxony elections. This is not the way to hold a fragile coalition together.

Legally, a defeat before the Federal Constitutional Court could be imminent if one were to march further in the direction of Eurobonds. In a preliminary decision in April 2021, the Karlsruhe court stated that NGEU could be constitutional as long as it was a one-off measure.

The proposal seems to be off the table for the time being. That is good. It is important that the German government takes a clearer position in the future. Please do not open Pandora's box.

Next-Generation-EU-Programm, bn EUR



RRF = Recovery and Resilience Facility

Source: IMF, LBBW Research

Another step towards debt union endangers the traffic light coalition

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