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European Monetary Union

European integration at its heart

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It is a set phrase to say that the Economic and Monetary Union (EMU) needs a political union to survive. This is almost a consensus among EU experts (De Grauwe, 2009a; Matthijs & Blyth, 2015; Draghi, 2019). But there is no such consensus when explaining why this is the case. In order to shed light on this issue, it is useful to go back to the different theories of money. If one conducts this exercise, it becomes clear that the orthodox theory, which emerged with Adam Smith (1776) (and still dominates modern Economics), has some gaps, while the heterodox theory developed by Schumpeter (1929) and others clarifies our understanding much more (Goodhart, 1998; Ingham, 2004). Money, just as any language, is an indispensable component in the creation of a political community. This is one of the reasons EMU needs to be considered from a holistic and multidisciplinary point of view. To restrict the discussion on the euro and EMU to economists only is a mistake (McNamara, 2017; Moro, 2013). The euro, as any other currency, is a reflection of how the political community using it is organised and, consequently, cannot be analysed from a strictly economic point of view but considering social and institutional implications, as well as the impact on the Union's foreign policy (including its security [Sweeney, 2021: in this book] and defence [Oikonomou, 2021: in this book] ambitions).

It is important to understand that, from the monetary power point of view, the creation of the euro is a defensive response to the instabilities produced by the dismantling of the Bretton Woods system in the late 1960s and early 1970s marked by the Vietnam War and the consequent de-anchoring from the dollar-gold parity, fixed exchange rates and capital controls (Henning, 1998). By belonging to small and open economies, continental Europeans have always been sceptical of the Anglo-Saxon need for floating exchange rates (Padoa-Schioppa, 2010). Avoiding abrupt movements has always been pursued, and that is why the "Snake in the Tunnel" of exchange rate bands emerged in the 1970s and the European Monetary System in the 1980s, both dominated by the Deutschmark as the monetary anchor of reference (Marsh, 2009). Having a common agriculture policy (Gravey et al., 2021: in this book), whose budget was (and is) shared, and thus requires a stable unit of account, has only reinforced this sentiment. Ultimately, and metaphorically speaking, in the presence of the constant waves and storms of an ever more intense and volatile international financial and monetary system, the euro represents the construction of a larger and more stable ship that can better withstand the possible shocks, or even tsunamis, coming from the dollar area.

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Precisely the greatest "dollar shock" in the last 80 years took place in September 2008 with the Lehman Brothers' bankruptcy. That was the moment when the new, grand ship called "the euro" was put to the test and when enormous gaps in its design were made evident, leading to the near-exit of Greece from the union (so-called Grexit) in 2012 and 2015. Such was the challenge that the mere existence of the euro is still in doubt, despite the great efforts made in the past ten years to "fill the holes". Will these repairs be enough to save the ship? Will the euro stay afloat in the current COVID-19 crisis (potentially an even bigger storm than the 2010–2012 debt crisis)? If the answer is no, what should be fixed for the euro ship to resist this crisis and the ones that will undoubtedly follow? In other words, how can the euro survive for another 100 years?

Getting the historical record straight

Since its birth, there have always been many doubts about the rationale behind the creation and future survival of the euro. Rudiger Dornbusch (1996) thought of it as a bad idea based on economic fantasies, and Martin Feldstein (1997) went even so far as to predict that European monetary union would lead to a civil war on the Old Continent. As a matter of fact, there is a long list of works written by US (or US-based or educated) scholars that consider the euro's creation economically irrational and politically dangerous. Lars Jonung and Eoin Drea (2009) put it accurately in a paper for the European Commission entitled "The Euro: It Can't Happen, It's a Bad Idea, It Won't Last. US Economists on EMU, 1989–2002". Interestingly, 30 years on (1989–today), the list keeps growing, with the works of Stiglitz (2016) and Mody (2018) as the latest additions to this 'euro-doom' tower of scholarly work.

The striking part is that this economics literature does not engage with the international political economy (IPE) literature that has studied international and European monetary affairs for over 40 years, such as 'international monetary power' and the 'dollar weapon', also known in the economic literature as the 'dollar shock' (Andrews, 2006). The creation of the euro is presented as strictly an endogenous affair, even by economists who try to include the political side of the story (Spolaore, 2013) without considering important, for some, decisive, exogenous factors such as US dollar hegemony. As Randall Henning (1998) has explained in his essential article entitled "Systemic Conflict and Regional Monetary Integration: The Case of Europe", the creation of the euro is above all a defensive move by the Europeans against the monetary power (including the dollar weapon) of the United States. There is a strong consensus in the international political economy literature on the subject, with Benjamin J. Cohen (2015) – who has done the most to develop the concept of international monetary power over the years – in the lead. But even non-IPE scholars who have chronicled the evolution of European monetary integration over the past decades, like David Marsh (2009), treat the US external factor as decisive.

Prominent authors like Mody (2018), who was deputy director of the Research and European departments at the IMF, argue that there were no good economic or political reasons to create the euro and dismiss oft-cited arguments such as the common agriculture policy (CAP). He writes that this was not the reason for creating the euro because it was not written in any official documents. But this is misleading. With the erosion of the Bretton Woods system in the late 1960s, and the ultimate repudiation of it by the United States in the 1970s, exchange rate volatility became the norm. What the CAP needed was to have stable exchange rates. This explains the European obsession with the snake in the tunnel and the European Monetary System and the Exchange Rate Mechanism (ERM). Mody also says that the (irrational) fear of competitive devaluations could not be a reason, because that was not written in any of the documents either. However, one wonders whether the memory of the drama of the devaluations in the 1920s and 1930s was still so strong in the 1960s and 1970s that policymakers did not have to make a written reference to acknowledge its negative consequences. As Barry Eichengreen (2008), professor of both economics and political science at Berkley, and perhaps the most renowned monetary historian of our times, has pointed out:

> Europe, not the United States or Japan, was where floating currencies had been associated with hyperinflation in the 1920s. Europe was where the devaluations of the 1930s had most corroded good economic relations.
>
> *(Eichengreen, 2008:150)*

In describing the reasons for further monetary cooperation in Europe, apart from, of course, pointing to instabilities from the dollar area, Eichengreen (2008:151) also highlights that "the desire to avoid jeopardising the CAP, whose administration would be complicated by frequent and sizable exchange rate movements, was a source of support for the Werner Report [1970]".

When it comes to finding logical reasons behind the creation of the euro, a lot of the economics literature (Friedman, 1997; Krugman, 2011; Stiglitz, 2016) has also overlooked the desire of many peripheral countries, even France, to buy Germany's price stability culture. Here the essential book is Kathleen McNamara's (1998) *The Currency of Ideas*, which explains how in the 1980s and 1990s, there was an emerging consensus among central bankers that the Bundesbank model was the one to follow and that through that model, European countries other than Germany would regain part of the monetary sovereignty by creating a supranational central bank. Marsh (2009) refers to this as the way to overcome the "tyranny of the Mark". In the same vein, there was also a strong desire in Europe, especially in France, to restrain or tame German power. This, again, is well explained not only in Marsh's account but also in other works by well-known political economists and experts in EMU like Amy Verdun (2000) and especially Kenneth Dyson and Kevin Featherstone (1999) in their *Road to Maastricht*. German Chancellor Helmut Kohl himself agreed with this taming strategy, as explained more recently by Thomas Klau (2018).

Then there is the controversial claim by Mody (2018) and others that there was never a quid pro quo between German reunification and the creation of the EMU. This is a fascinating issue, because it is possible that a myth has been created around this interpretation, despite the historic evidence pointing in another direction. Thus, in order to get the historic record straight on this very important aspect of the creation of the euro, it is useful to read the works of David Marsh (2009) and Kenneth Dyson and Kevin Featherstone (1999), who have explored this historic moment in depth. According to Marsh:

> There was never a formal bargain under which Germany gave up the D-Mark in return for unification. Mitterrand, by far the most powerful and resourceful politician among Germany's neighbours, knew by autumn 1989 that German unity was unstoppable; his aim was to manage it, not to hold it up. However, fusing of the two Germanys, and the birth of the single currency, are intimately intertwined. If unification had not happened, it is highly unlikely that France would have been able to persuade Kohl to agree the EMU timetable to replace the D-Mark by the Euro.
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> *(Marsh, 2009:133)*

In a similar vein, Dyson and Featherstone (1999) write that when Mitterrand convened a special informal meeting of European Communities' heads of state and government on 18 November 1989 (hence just nine days after the Fall of the Berlin Wall), his

> intention was not only to placate domestic criticism of French activism [vis-à-vis the possibility of a powerful united Germany] but also to subject Kohl to pressure, to soften him up so that he would be more susceptible to French influence. There was no explicit discussion of German unification or any linkage to EMU. But the atmosphere was, from a French point of view, suitably uncomfortable for Kohl: and linkage was in the minds of Mitterrand and Dumas [then French foreign minister].
>
> *(Dyson & Featherstone, 1999:196, brackets added)*

Further on, these same authors write that:

> Mitterrand viewed EMU as following the single European market and preceding political union [a longstanding demand by the Germans]. His strategic preoccupation was to establish parallelism between EMU and German unification. . . . Right up to the Strasbourg meeting [on 8 and 9 December 1989, when a concrete timetable for EMU needed to be agreed on] he kept up the pressure, telling Kohl on the telephone that too great a preoccupation with inner-German relations at the expense of priority to European unification could lead to Germany's isolation.
>
> *(Dyson & Featherstone, 1999:198, brackets added)*

Eventually, Mitterrand's pressure on Kohl worked. At the historic European Council Meeting in Strasbourg on 8/9 December, 1989, hence just one month after the fall of the Berlin Wall, the French president "had attained his prime strategic objectives – to bind Germany into EMU by setting a clear date for the IGC [Intergovernmental Conference which led to the single currency] and to prevent conditionality of EMU progress with political union" (Dyson & Featherstone, 199:198, brackets added).

Indeed, sometimes you need not to make an objective explicit to attain it. It is essential to highlight that Mitterrand used German unification to achieve EMU without a political union first, and this latter point is particularly important and again overlooked by some of the literature. Authors such as Mody (2018) and Stiglitz (2016) criticise – and rightly so – the German insistence on an orthodox framework for EMU based on 'sound money' and the full independence of the ECB, without acknowledging, as Geoffrey Ingham (2004) does in his analysis of the euro, that this orthodox construct was necessary to give credibility to a currency that would not have a political union behind it (more about this in the next section), because the French resisted such a move. The blame in this case should go to the French rather than the Germans, at least until Emmanuel Macron arrived at the Élysée Palace (Otero Iglesias, 2017). In any case, the stability culture was not just a German notion. It was the period's *Zeitgeist*, as McNamara (1998) has documented.

Interestingly, again, the economics literature does not take into consideration that France had long lost its monetary sovereignty to the Bundesbank and the City of London. This is a story well told by Nicolas Jabko (2012). It was this understanding, and the reluctance to submit to a political union, that convinced the French elites to accept the 'sound money' ideology advocated by Germany enshrined in the Maastricht Treaty and reinforced by the Stability and Growth Pact (1997) of no more than 3% annual budget deficits and 60% of public debt agreed on two years before the birth of the single currency.

The significance of the ontology of money

The dominant theory: optimal currency areas

Mainstream economic theory has always considered that the best prism to analyse the creation of transnational currencies is the theory of optimal currency areas (OCA) (Mundell, 1961, 1973). Here the standard textbook is Paul de Grauwe's (2009b) *Economics of Monetary Union*, with its eight editions. OCA focuses on factors of production and economic cycles and establishes that the more convergence and flow of capital and workers there is between different regions, the more sense it makes for those regions to share the same currency. Following this logic, by the end of the 1980s – when the Delors Report (1989) that would lead to the euro was in the process of being written – the French monetary and political elite agreed with the Germans in that countries that would conform the EMU were not an optimal currency area. Still, they argued that it was precisely the creation of a single currency that would be a catalyst for convergence. Unable to devalue, the weaker countries would set out the necessary structural reforms to increase their productivity and competitiveness. Thus, an integration towards an optimal monetary union would take place endogenously (De Grauwe, 2006).

That is exactly what *on the surface* took place during the first decade of the euro. The countries of the periphery grew more, and their per capita income became closer to those of the core countries. However, when the subprime mortgage crisis erupted in the United States, the structural weaknesses of the peripheral countries (with low productivity and faulty institutions) and the euro governance framework (based on an intergovernmental decision-making process) emerged (Matthijs & Blyth, 2015). It was at that moment when the economists who had been critical about the theory of optimal currency areas because it was too economistic gained credibility (Goodhart, 1998). Soon, part of the economic science mainstream realised that maybe money is not a mere neutral means of exchange, as textbooks indicate. There are two interpretations of what money is, and if one accepts the heterodox version (see subsequently), then the OCA theory has great limitations because it does not conceive that money is essentially debt and therefore credit relations need to be studied alongside the factors of production (Otero Iglesias, 2015).

As Goodhart (1998) points out, the theory of optimal currency areas comes from the traditional or orthodox interpretation of the origin of money. According to this version, which dates back to Adam Smith (1776), widely acknowledged as the founder of modern economics, money arose spontaneously out of trade. This explanation of the origin of money, which is commonly found in economics textbooks (Graeber, 2011), could be summarised as follows: at some indeterminate moment in history, in an imaginary small village, producers of goods and services and traders got tired of barter and opted for using a good with intrinsic value, divisible and non-perishable as means of exchange to make economic activity easier. Historically, gold and silver have carried out that function, and that is why we label this school of thought the "metallist" one. Out of the three traditional functions of money, as means of payment, unit of account and store of value, the most important, for this school, is that of means of payment. Under this interpretation, money works just as any other good: it is neutral, and its value is determined by the law of supply and demand. In this interpretation of money, neither politics nor power play a significant role (Martin, 2013).

The euro was precisely conceived on this very premise, that money could, and should, be de-politicised (Issing, 2008) and that what was needed for Europe to compete with the United States and Japan was to create "one market, one money" on the basis of "neutral" economic calculations, as was argued by an influential report by the European Commission (1990).

The heterodox conception: money as debt

Nevertheless, there is a second school of thought on the origins of money: the Chartalist or heterodox approach (Goodhart, 1998; Ingham, 2004). According to this interpretation, money did not spontaneously emerge out of trade because the most important function of money is not serving as means of payment but as unit of account. Money is the scale used to measure value, and it has historically been introduced or imposed by a political power to collect taxes. The little prehistoric evidence we have suggests that the tale of Adam Smith's village never happened (Graeber, 2011). Actually, studies show that money appeared in the Mesopotamian and Egyptian empires around 3000 AC when emperors started collecting taxes from their subjects based on a specific scale of value. This does not mean that there have been no private (near) moneys throughout history. Bitcoin can be considered the latest example. But, normally, the legitimate sovereign political power with the monopoly over the means of violence has been the one stabilising monetary areas in the case of major defaults, wars or pandemics (Martin, 2013). The current COVID-19 health and economic crisis and the response of states all over the world to mitigate it with extraordinary measures and interventions is the latest historic example (see next section).

Money is always debt, and, thus, it is always a social relationship between a debtor and a creditor. Consequently, just as any other social relation, it necessarily carries an implicit power relation. This power relation in modern times is mediated by the state, since it is the biggest debtor (it issues debt to build infrastructure and to provide public services) and the largest creditor (the state collects taxes and will continue to do so in the future, if necessary, through the legitimate and monopolistic use of force). The fact that we live today in a fiduciary, non-metallic monetary system demonstrates that the effectiveness of money is not based upon a tangible good with intrinsic value (like gold) but upon an abstract element: trust. Trust in a certain political community, in other words, trust in the sovereign who issues the money and who will pay back in goods and services the value stipulated in the paper bills ("charta") used to pay taxes (this is where the name of the "Chartalist" theory of money comes from).

The problem is that the euro is not backed up by a European sovereign. In the first decade of its existence, this was thought of as an advantage (Issing, 2008). History shows plenty of sovereigns who manipulated money production to generate growth and inflation and therefore reduce their debt in real terms (Graeber, 2011; Felix, 2013). The de-politisation of the euro and the orthodoxy of the European Central Bank, inherited from the Bundesbank, were perceived as a credibility-enhancing factor and made the European currency attractive as a safe store of value (Otero Iglesias, 2014). But when the global financial crisis mega-shock of 2008–09 took place, and panic and the search for safe-haven assets began, many international investors started asking themselves the question: Which is the political authority who will stabilise the Eurozone? For this type of question, the theory of optimal currency areas has no answers. There are several reasons, but it is mainly due to its orthodoxy when it comes to understanding the origins of money. The theory establishes that a monetary area needs a federal budget to deal with asymmetric shocks, because the mobility of factors of production is never perfect, but it does not explain why or how it should be achieved (Otero Iglesias, 2015). As commented previously, the orthodox interpretation of money leaves no room for politics or power in credit relations.

The euro crisis that began in Greece in late 2009 cannot be explained, however, without analysing the credit flows that happened in the first decade of the single currency (Jones, 2016). With the eruption of the crisis, many economists correctly identified the growing divergence in the current account balances of Northern and Southern countries as one of the factors leading to the crisis. This was due, partly, to inflation and productivity differences. But if some countries import much more than they export, someone needs to finance those purchases. This someone was the creditor countries from the north of the Union. Hence, the problem was the imbalances in the capital accounts (the flow of credit) as much as in the current accounts (trade relations).

As explained before, money is a social relation between creditors and debtors and, consequently, it always entails a power relation. Simultaneously, depending on the intensity of the relation, this generates more friction but also more interdependence. Ultimately, wherever there is an irresponsible debtor, there is necessarily an irresponsible creditor. The euro has created this type of relationship. It simply happens that, by just focusing on the factors of production of the real economy and not analysing the credit interdependencies generated by the monetary union, OCA theory has not been able to identify this phenomenon. On the one hand, the theory has not understood that this same debt/credit was feeding the macroeconomic imbalances that led to the crisis, and, on the other hand, it has not realised that it is precisely this debt/credit interdependence which would make the centre of the Union bail the periphery out, despite being against the spirit (and for many: the text) of the Treaty of Maastricht (Otero Iglesias, 2015).

In summary, by considering money a neutral element that does not influence the development of the real economy in the long term, the theory of optimal currency areas never took the time to analyse the relevance of the credit system, and, thus, it never warned about the need of a banking union. This acknowledgement only arrived when many analysts, investors and politicians discovered that the ECB was the lender of last resort for commercial banks but not for the sovereigns, and that is when it became obvious that a "doom loop" among the ever-weaker national banks and the peripheral states of the EMU had formed (De Grauwe, 2012; Pisani-Ferry, 2012). That is certainly problematic, because, as noted before, the sovereign has historically stabilised the monetary system in the case of a systemic crisis through the control of or collaboration with the central bank (Goodhart, 1998).

Eventually, the logic of money triumphed. If there is credit activity, especially transnational banking credit activity, there needs to be transnational banking regulation and supervision. In other words, a monetary union needs a banking union (Véron, 2015). The question is: can there be a banking union without a fiscal union? If one understands money from a Chartalist perspective, no, it cannot. Just as American, British and German banks had to be bailed out with taxpayer money at the national level in 2008 and 2009 because the crisis was systemic, the same will happen at European level in the next systemic crisis, which at the time of writing could perfectly well be the COVID-19 economic aftermath. That is why a fiscal union with a federal budget will be needed to stabilise the situation (see next section), despite some highly respected economics commentators arguing to the contrary until very recently (Sandbu, 2015).

Nevertheless, the next question is: can a banking and a fiscal union be built without a political union? Once again, the ontology of money as understood by the Chartalist school would say no. What legitimacy do the civil servants at the ECB have to close a bank such as Société Générale? What legitimacy does Olaf Scholz, the current German finance minister, or the Bundestag, have to decide whether a potential bailout to Italy is financed with money from the pockets of taxpayers in all Member States? What legitimacy does Chancellor Angela Merkel have to decide whether Greece or Italy remain or leave the euro? Very little. This is why intergovernmental constructs such as the European Stability Mechanism (ESM) and the imposition of reforms by the so-called Troika institutions (the European Commission, the European Central Bank and the IMF) are highly problematic and unpopular (Ban & Seabrooke, 2017). The history of money is stubborn. Monetary unions do not survive without a legitimate political union, which means a sovereign that can sustain, stabilise and defend said union. Therefore, a political union is unavoidable if the euro ship is to keep sailing.

The political fixes so far

Since 2010, when Greece stopped getting financed by the international markets, political leaders of the Eurozone countries have achieved great advancements in the construction of a coherent monetary union, following the Chartalist theory. The direction, hence, is the correct one to make the construction more stable. There is no doubt that the monetary union is better off by having a European Central Bank that is not afraid of buying sovereign debt in the secondary bond markets (once the sovereign debt has been sold to financial intermediaries) if its inflation target requires so or, if the irreversibility of the euro is in question, which allows us to say that the ECB has indirectly become a lender of last resort for sovereigns. As Mario Draghi (2012) stated in his impactful speech, the ECB is here to do "whatever it takes" to save the euro, which eventually led to the Outright Monetary Transactions (OMTs) provision and the Asset Purchase Programmes (APPs), also called Quantitative Easing (QE). Furthermore, his successor Christine Lagarde has shown the same determination in the current COVID-19 crisis by launching a huge Pandemic Emergency Purchase Programme (PEPP), which has helped to stabilise the financial, and especially the sovereign, debt markets.

One can also argue that some sort of embryo of a fiscal union was created through the ESM, with a lending capacity of 500 billion euros, which was key to bail out Greece, Ireland, Portugal, Cyprus and (partly) Spain in the previous euro debt crisis, and which was also activated during the current COVID-19 crisis. In parallel, budget and macroeconomic discipline was enhanced through the so-called Fiscal Compact, the Six Pack and Two-Pack and the introduction of the European Semester, which looks at the structural weaknesses of every EMU Member State and issues country-specific recommendations. In the banking union, a single supervisory mechanism (SSM) and a single resolution mechanism (SRM), with its single resolution board (SRB) and single resolution fund (SRF) were also established.

However, there is a certain consensus that all of this is still not enough (Pisani-Ferry & Zettelmeyer, 2019). If one looks at the Four Presidents Report led by Van Rompuy (2012),

Table 20.1 Deepening EMU: new measures or institutions since the euro crisis 2010–2012

Monetary union	*Banking union*	*Fiscal union*	*Political union*
LTROs and TLTROs (Targeted) Longer-Term Refinancing Operations	Single Rule Book for banking and financial regulation	Fiscal Compact (Treaty on Stability, Coordination and Governance in EMU)	No real progress thus far
OMTs (Outright Monetary Transactions)	SSM (Single Supervisory Mechanism)	ESM (European Stability Mechanism)	
APPs (Asset Purchase Programmes)	SRM (Single Resolution Mechanism)	Six-Pack with its Macroeconomic Imbalance Procedure	
PEPP (Pandemic Emergency Purchase Programme)	SRB (Single Resolution Board)	Two-Pack with its Draft Budgetary Plans	
	SRF (Single Resolution Fund)	European Semester	

Source: Author's own compilation

which was published just a few months after the European Council agreed on the creation of the banking union and Draghi (2012) delivered his "whatever it takes" speech, it is clear that for a number of years, there was reform fatigue, and the integration process towards a "genuine" EMU stalled. Years later, the European Commission (2017) kept pushing leaders from Eurozone countries to complete the banking union with the design of a plan to solve the creation of a European deposit insurance, a sovereign risk-free asset that can compete against the US sovereign bond, the union of capital markets and, if all the aforementioned were achieved, a sovereign debt resolution mechanism. The basic principle of the Commission proposals is simultaneously sharing and reducing risks, but that would require agreeing on the sequence of reforms, and that has never been easy. The creditor countries wanted a reduction of risks first, and then sharing future risks, while debtor countries argued for years that reducing risks is not possible without some parallel risk-sharing. In the United States, for example, states can go into bankruptcy, but there is a federal budget that covers the costs of unemployment subsidies and social security, which means there are powerful counter-cyclical mechanisms that alleviate the crisis of the bankrupt state (Krugman, 2012).

That is precisely why the Commission (2017), supported by France and Spain, stands for the construction of a fiscal stability mechanism, whether it is through a European investment fund or through a European unemployment benefit mechanism, with the possibility of even creating a Eurozone treasury before 2025. Logically, this would imply many things that demonstrate once again that the EMU is not just any area of EU policy but rather the fundamental pillar of the European integration project that cuts across the broad layers of the Member States' sovereignty. If the European Commission wants to strengthen the European Semester by linking structural reforms to support for convergence and cohesion, if it puts forward the creation of a Eurozone sovereign debt asset, the creation of a Eurozone treasury and the integration of the Eurozone international representation, for example, at the IMF with a single seat, it is demanding a degree of sovereign integration that necessarily requires a parallel process of legitimation and democratic control at European scale, which has not been developed yet and explains why the column in Table 20.1 is still empty.

Completing the ship is not easy

Emmanuel Macron took power in France in 2017 with a great reform plan, but the only thing he was able to achieve was making the ESM a fiscal intergovernmental back-stop of the banking union and initiating the debate on a possible future Eurozone budget, which led to the creation of the Budgetary Instrument for Convergence and Competitiveness (BICC). However, its resources were so limited that it has no macroeconomic stabilising function. In some sense, by early 2020 – hence at the age of 21 years – EMU had reached the point where the banking, financial and fiscal unions were not moving any further without more political union. Therefore, the sequence put forward by the Commission in its 2017 reflection paper did not seem to be the most fitting. History evidences that banking unions do not work without fiscal unions and that capital market unions – and the same goes for the single market of services, energy and defence (which is why the governance of the euro is so multidisciplinary) – are not efficient if there is not a previous and important degree of political determination and integration. This is why the banking sector is so fragmented in national markets and there are so few trans-European mergers.

Logically, political union will not happen overnight. Many small steps are needed. And usually fiscal unions emanate from the necessity to provide common goods to fight wars or deal with economic crises and the necessity to finance those costs (Kirkegaard, 2018).

Putting efforts in the creation of a synthetic European sovereign asset, such as the European Safe Bonds (ESBies) proposal, was never a workable option, despite the laudable efforts of some of Europe's best economists for almost a decade (Brunnermeier et al., 2011; Leandro & Zettelmeyer, 2019). Sovereign bonds are safe because they are backed by the capacity of the sovereign to tax. Thus, from a Chartalist point of view, the proposal of creating "eurobonds" without a federal budget first has always been an oxymoron. Recent events have proven this. In the face of the dramatic impact of the COVID-19 crisis, finally the German chancellor, Angela Merkel, has walked the extra mile towards French President Emmanuel Macron, and both agreed in May 2020 that, to respond to this new challenge, the European Union, through the European Commission, should issue joint debt up to 500bn euros. Again, despite the differences in their macroeconomic cultures – explained by Brunnermeier et al. (2016) extraordinarily well in *The Euro and the Battle for Ideas* – Germany and France achieved a political compromise in a moment of extreme crisis, which moved the European (monetary) integration process forward.

At the time of writing, the EU leaders have just agreed to an historic EU (federal) budget for the 2021–2027 period, and the sums involved are close to the 2 trillion euros mark, with 750bn euros dedicated to the recovery fund to deal with the COVID-19 crisis. This "EU Next Generation" fund will be financed through the joint issuance of debt in the financial markets. The negotiations were certainly hard because the so-called frugal (and net creditor) countries led by the Netherlands wanted to limit the size of the budget and preferred that Brussels give loans to the countries in financial need to secure tougher conditionality and structural reforms, while the European Commission and the four biggest countries in the Union (Germany, France, Italy and Spain) believed that the severity of the crisis warranted a budget big enough to have macroeconomic impact to overcome the recession and also sufficiently large to send a political message of solidarity to the countries most affected through transfers and not loans.

The vision of the big four is also that Europe needs to use this crisis to come closer together and modernise its economy in order to be more competitive, sustainable and autonomous in a world increasingly shaped by the geopolitical rivalry between the United States and China. This means dedicating more resources to digitalisation, the green transition, the convergence of all EU Member States, research and development and strategic capacities (including in key areas such as big data and artificial intelligence [Ulnicane, 2021: this book] and security and defence). Agreeing to jointly issue debt, in what some have already labelled Eurobonds, and repay it until 2058 is perhaps the biggest step in European integration since the creation of the single currency.

Indeed, there are many questions still to be resolved. First, there is the issue of whether a larger EU budget precludes the possibility of having one day a budget for the eurozone. In principle, all EU Member States should eventually join the euro except Denmark, which has an opt-out. So perhaps this should be the case. With the exit of the United Kingdom, the euro-outs have lost a lot of influence.

Second, there is the big question on how these new funds will be distributed and used. The European Commission has proposed to use the country-specific recommendations of the European Semester as the basis for reforms and that the European Commission itself would be in charge of the monitoring of the correct use of the funds. But the Netherlands, for example, believes that the European Council should oversee this process in a more intergovernmental fashion, including national veto powers. This is rejected by countries like Italy and Spain. The European Parliament, on the other hand, which has no say in the European Semester, believes that it is the legitimate institution to supervise the correct use of the money given that it has co-decision power on the EU budget. The logic would also say that if the 750bn euros strong recovery fund is financed through debt issuance at the European level, the democratic control of the use of these funds should also happen at this level through the European Parliament.

Third, there is the possible withdrawing of funds or even the imposition of sanctions if Member States do not use the new resources correctly, do not lower their debt levels in the future or do not respect the rule of law and other key values of the Union enshrined in the Copenhagen Criteria. How will this be enforced without proper democratic legitimacy at the centre of the union?

Finally, there is the important issue of who will pay the joint debt issued. Will this be done by national contributions of the Member States or by European taxes (own resources, as it is called in Brussels)? If the latter is the case, that would be another big step in the federalisation of the union and the consolidation of the euro.

Ideally, European money should be used to help solve some of the structural problems of weaker countries, but these structural improvements (or reforms) cannot be imposed from Brussels. They need the ownership of the populations of the receiving countries and the legitimate approval and oversight by national and European parliaments. Hence, as should be clear by now, European monetary union and its sustainability has as much to do with politics as with economics.

Conclusion: the utopia of a "genuine" political union

Despite the criticism of a relevant percentage of the population, looking back, we can see that EMU countries have made great efforts to patch up the holes in the euro ship. In fiscal policy, the Rubicon was crossed. Germany has given in and in the previous Eurozone debt crisis accepted the creation of the ESM, which has a lending capacity of up to 500 billion euros and certain experience now in dealing with debt crises and structural reforms. This is evidenced by the relatively successful bailouts of Ireland, Portugal, Spain and Cyprus, Greece being the exception that confirms the rule. Agreeing to the joint issuance through the European Commission of 750bn euros to fight the current COVID-19 crisis is also an important step toward a genuine fiscal union. It has the potential to create a genuine European sovereign debt market that can rival the US one and therefore make the euro a more attractive international currency.

In monetary policy, the ECB has become the de facto lender of last resort for sovereigns, albeit indirectly. Maybe the most significant change has been that the ECB has passed many policies, including the OMT or quantitative easing, without support from the Bundesbank, showing that, despite being built in the mould of the German central bank, the ECB went through a federal metamorphosis throughout the past decade of crises. It is another example that once created and consolidated, institutions forge their own identity and are willing to fight for their survival, and obviously the survival of the ECB depends on the sustainability of the single currency.

Nevertheless, from the perspective of the Chartalist theory of money, there is still a lot to do to fix the euro ship so that it can keep sailing for the next 100 years. To save the single currency, European states have given up major parts of their sovereignty. The single banking supervision, the European Semester and the Troika are the most significant examples, but this technocratic "executive federalism" (Habermas, 2012) increasingly dominated by Germany has faced a lot of rejection, because it does not have the necessary legitimacy to be sustained by itself. Right now, Italy is the weakest country. If there is a great crisis in Italy in the aftermath of the COVID-19 pandemic, because the recovery (Next Generation EU) fund is just too small, we would have to see whether Italy uses the ESM, with the consequent activation of OMT by the ECB and the structural adjustments required. Many analysts think that it will not, but it is also true that, in the past, only in moments of crisis have leaders been able to cross their own red lines and advance toward an ever-closer union.

In an ever more protectionist and nationalist international environment, with a growing geopolitical rivalry between the United States and China and complex Brexit negotiations (and its consequences), the EU will have to decide in the next decade whether to choose the nativist option of returning to the nation-state, and that would mean the sinking of the euro ship, or if it chooses the cosmopolitan and pro-European path by creating a European sovereign built upon the national identities that make up the Union. The challenge is major but not impossible to face. The EU might evolve into a transnational political union still fragmented on the inside (and thus far from becoming the United States of Europe) but united toward the outside and with the ability of collecting taxes to face future crises. The Union will certainly need pan-European common goods to deal with external challenges, such as climate change and increased great power rivalry. In other words, geopolitics and not economics might make the euro, the currency of the EU, have a genuine federal budget worthy of that name. If the single currency achieves this, it will fulfil the Chartalist premises of money, and the biggest cracks in the euro ship would be sealed.

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