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Merkel fixed on long-term goal of fiscal union

By Quentin Peel in Berlin

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Angela Merkel speaks at the budget debate in the Bundestag

When Angela Merkel, the German chancellor, says there are no quick fixes that will resolve the eurozone crisis, she means it.

Instead, she has set her heart on a far more ambitious goal: to drive the 17 European partners that share the euro as a common currency towards a fiscal union. It will take many months, if not years.

Ms Merkel remains adamant that short-term “financial” solutions – such as introducing jointly guaranteed “Eurobonds”, or urging the European Central Bank to intervene massively in sovereign bond markets – will not solve the fundamental problem of excessive debt in the eurozone that has undermined the trust of investors.

“These are political problems that require a political solution,” she said this week. It is a “step-by-step” approach that will require change in the European Union treaties, but she is convinced it is the only way to restore confidence in the markets.

In Strasbourg on Thursday, after a mini-summit with Nicolas Sarkozy, French president, and Mario Monti, Italy’s new prime minister, the chancellor laid her cards on the table, pronouncing: “We must take steps towards a fiscal union.”

Would she accept Eurobonds in return for EU treaty change? “It is not a question of give and take. It is about a big step towards fiscal union,” she insisted. To introduce joint Eurobonds first would send “a completely wrong signal.”

By fiscal union, she means ever closer co-ordination, and direct supervision, of national economic and budgetary policies in the eurozone. She wants debt and deficit limits enforceable in the European Court of Justice. And she wants a European Commissioner who will be a sort of super-finance minister, with powers to demand changes in national budgets if they break the rules, and to impose automatic penalties if they do not fall in line.

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In effect, it means that the eurozone partners would have to abandon much of the budgetary sovereignty so jealously guarded by their national parliaments. It does not mean they would have to harmonise their taxes, but it would limit their room for manoeuvre.

Germany's own constitutional court has declared that budgetary sovereignty is a fundamental pillar of national democracy. But Ms Merkel says she is prepared to see it restricted by the rules of a future European fiscal union, to ensure the stability and durability of the common currency.

Treaty change is something that many of her EU partners regard with dismay, conscious that it will take many months to negotiate, and would then be hostage to unpredictable referendums in several

member states.

Ms Merkel has launched a diplomatic offensive to persuade them all before December 9, date of the next EU summit in Brussels. She has already won over Mr Sarkozy.

It is also a contrarian path, for the chancellor has set herself against the demands of investors in the financial markets, and many of her partners, who want her to seize more instant and dramatic remedies to the current contagion in the eurozone.

Repeatedly in recent days, Ms Merkel rejected the idea of joint Eurobonds as an instant solution to the borrowing crisis of the most debt-laden states. They could only be considered when the crisis was over – and the rules of fiscal union have been fixed, she said. If they were introduced too soon, they would abolish interest rate differentials for sovereign bonds in the financial markets, and thus remove the incentive for governments to curb their debts.

She has grave misgivings about the use of massive intervention by the European Central Bank in the sovereign bond markets, too, arguing that it would not answer the fundamental problems of excess debt, and lack of competitiveness. But she will not tell the ECB what to do.

The suspicion remains that Ms Merkel may be prepared to do a deal for fiscal union: some form of Eurobonds in exchange for treaty change. She denies it, but her partners in government – the liberal Free Democrats – are fiercely opposed, and fear the worst.

A deal might be only possible in a “grand coalition” with the opposition Social Democrats, who support Eurobonds. But that would mean a change of government in Germany, and elections are not due until autumn 2013. The markets may not wait that long.

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