A Modest Proposal for Resolving the Eurozone Crisis, *Version 3.0*

Yanis Varoufakis[1] *and* **Stuart Holland**[2]

1. Prologue

For two years now, caught up in a Crisis of its own making, Europe is fragmenting.

A euro in a Greek bank has a lower expected value than a euro in a Spanish bank, which, in turn, trails the value of a euro in a German bank account. There can be no better sign of the common currency's disintegration than this.

And it is not just a matter for the Eurozone. The fallout from a Eurozone disintegration will be so severe, the rise of nationalisms so cataclysmic, that it is pure wishful thinking to believe that the European Union can be preserved, except perhaps in name, if the euro-system succumbs to the centrifugal forces it is now experiencing.

Following a sequence of errors, delays and shenanigans, Europe's leadership has stunned the world by its failure to take joint action. Most commentators lament the incapacity of Europe's political and bureaucratic elites to act speedily and in a coordinated fashion. While there is truth in this, the recent double-edged ECB intervention *vis-à-vis* Europe's banks[3] shows that Europe *can* act decisively. The problem, however, is that, so far, its political leadership has pursued policies which it justifies on the basis of (a) a poor diagnosis of the Crisis' nature and (b) two false dilemmas.

In what follows, we begin by summing up the true nature of this Crisis. Then we present our Modest Proposal for overcoming the Crisis with three simple policies that can be implemented immediately and require none of the moves such as national guarantees or fiscal transfers to which many Europeans (and not only governments) are opposed, nor moves towards federation that entail Treaty changes which electorates are most likely to reject.

[1] Professor of Economics at University of Athens and the Lyndon B. Johnson Graduate School of
[2] Visiting Professor of Economics, Coimbra University; formerly a Member of the House of Commons, UK, and advisor to Jacques Delors.
[3] Taking from them with one hand a large slice of Greek debt, and then immediately compensating them with another hand (with new EFSF capital and a trillion euros worth of LTRO liquidity provided liberally by the ECB).

(e.g. fiscal transfers, federation) that Europeans currently find unfathomable. Finally, we juxtapose the logic behind our proposals against the false dilemmas that currently impede clear thinking and immobilise Europe's policy makers.

2. The Nature of the Eurozone Crisis

The Eurozone Crisis is unfolding on three interrelated terrains.

Banking crisis: While sparked off by events across the Atlantic, and the English Channel, the problem with the Eurozone's banking crisis was never properly addressed. The reason was the terribly odd arrangement whereby governments, that lack the backing of a national Central Bank, maintain national control over global banks inhabiting within a trans-national currency union. At a time when forced recapitalisation of essentially insolvent banks is of the utmost importance, we end up with the unwholesome sight of fiscally stressed member-states (e.g. Spain) borrowing massively on behalf of the nation' insolvent banks. And because this new public debt stresses their fiscal position further, they are abandoned by private creditors and have to rely on ECB liquidity that comes to them (to the states) *via* the very banks that the states are trying to save! It is abundantly clear that this madness cannot continue. *For this purpose, our Modest Proposal suggests a very elegant, simple, instantly workable solution – see Policy 1 below.*

Sovereign debt crisis: Again as a result of a design fault, the sudden and catastrophic loss of liquidity that came to be known as the Credit Crunch of 2008, inevitably turned the eurozone's most cherished principle (of perfectly separable public debts) into the 'popcorn effect' that drove three sovereigns into effective insolvency, before putting at least two large member-states in bankruptcy's antechamber. Suddenly, reality bit back, reminding us that even though a common currency shields us from runs on individual currencies, our perfectly separable debts were bound to lead to a sequential run on member-state bonds, once panic set in the money markets following the financial sector's implosion and the realisation of rating agencies that member-states would not act jointly to address the Crisis. While some of Europe's leadership now understands this, and while Francois Holland has been elected on the basis of countering austerity by growth, there is an understandable reluctance of the surplus nations (mainly Germany) to become liable for the debts of the heavily indebted deficit nations gives rise to a certain paralysis. However, the problem caused by separate public debts can be addressed without asking of the surplus nations either to lend to or guarantee the loans of the deficit ones. *For this purpose, our Modest Proposal puts forward another simple and elegant solution, one that violates neither the EU's Treaties nor the charter of the ECB – see Policy 2 below.*

Under-investment and imbalances crisis: In addition to the banking and sovereign debt crises, Europe is facing (i) a dearth of aggregate investment (which threatens its long term international competitiveness) and, perhaps more

significantly, (ii) an intra-Eurozone balance of payments' crisis. The two are intimately linked. As the various regions within the Eurozone grew apart (in terms of competitiveness, investment, unit labour costs) during the period that led to the Crash of 2008, a well hidden (courtesy of open borders and a common currency) imbalance ensures that, when the global Crisis hit in 2008, the Eurozone risked disintegration. Following the massive loss of liquidity everywhere, the burden of adjustment fell on the regions with lower competitiveness and greater deficits, with swingeing cuts and painful austerity. Coupled with the impossibility of devaluations by these member-states, and the lack of new aggregate demand that would pull the deficit regions[4] out the mire, the scene was set for a flight of capital and negative investment in the regions that needed it the most. Thus, Europe ended up with (A) low aggregate investment and (B) an even more uneven distribution of that investment among its surplus and deficit regions. *To counter both problems at once, the Modest Proposal recommends that three of Europe's existing institutions collaborate in order to stimulate investment in the regions of Europe in a manner that requires no tax-and-spend policies but which succeeds in mobilising idle savings and transforming them into profitable investments – see Policy 3 below.*

3. Three political constraints taken for granted by the Modest Proposal

Designing the solution-concept for the current Euro Crisis resembles a constrained optimisation problem.

- First, we must state the objective: *To arrest the Crisis simultaneously in the three terrains (mentioned above) where it is currently progressing unimpeded.*
- Secondly, we need a realistic catalogue of the constraints under which Europe must find a solution. It is our view that the three constraints Europe is facing presently are as follows:

(a) The ECB will *not* be allowed to monetise sovereigns directly (i.e. no ECB guarantees of debt issues by member-states, no ECB purchases of government bonds in the primary market, no ECB leveraging of the EFSF-ESM in order to buy sovereign debt either from the primary or the secondary markets)
(b) Surplus countries will *not* consent to the issue of jointly and severally guaranteed Eurobonds, and deficit countries will *not* consent to the loss of sovereignty that will be demanded on them without a properly functioning Federal Europe
(c) Crisis resolution cannot wait for federation (e.g. the creation of a proper European Treasury, with the powers to tax, spend and borrow) or Treaty Changes cannot, and will not, precede the Crisis' resolution.

[4] E.g. something akin to US consumer demand growth that, in the mid-1990s, allowed Canada to complete its austere fiscal adjustment program with reasonable success.

The question is: Does a policy mix exist such that it achieves the stated objective without violating any of the three constraints above? We believe that the answer is affirmative. The next section presents the three policies that respect these constraints.

4. **THE MODEST PROPOSAL – Three crises, three policies**

To respect constraint (c), the Modest Proposal introduces no new EU institutions and violates the letter of no existing Treaty; for that would involve new Treaties whose conception, approval and activation will take too long to resolve the Crisis. In short, we propose that existing institutions are utilised in ways that remain within the letter of European legislation but allow for new functions and policies. These institutions are:

- The European Central Bank – ECB
- The European Investment Bank – EIB
- The European Investment Fund – EIF
- The European Financial Stability Facility & the European Stability Mechanism – EFSF/ESM
- The European Banking Authority - EBA

POLICY 1 – Dealing with the banking crisis by means of creating a *Single Banking Area*

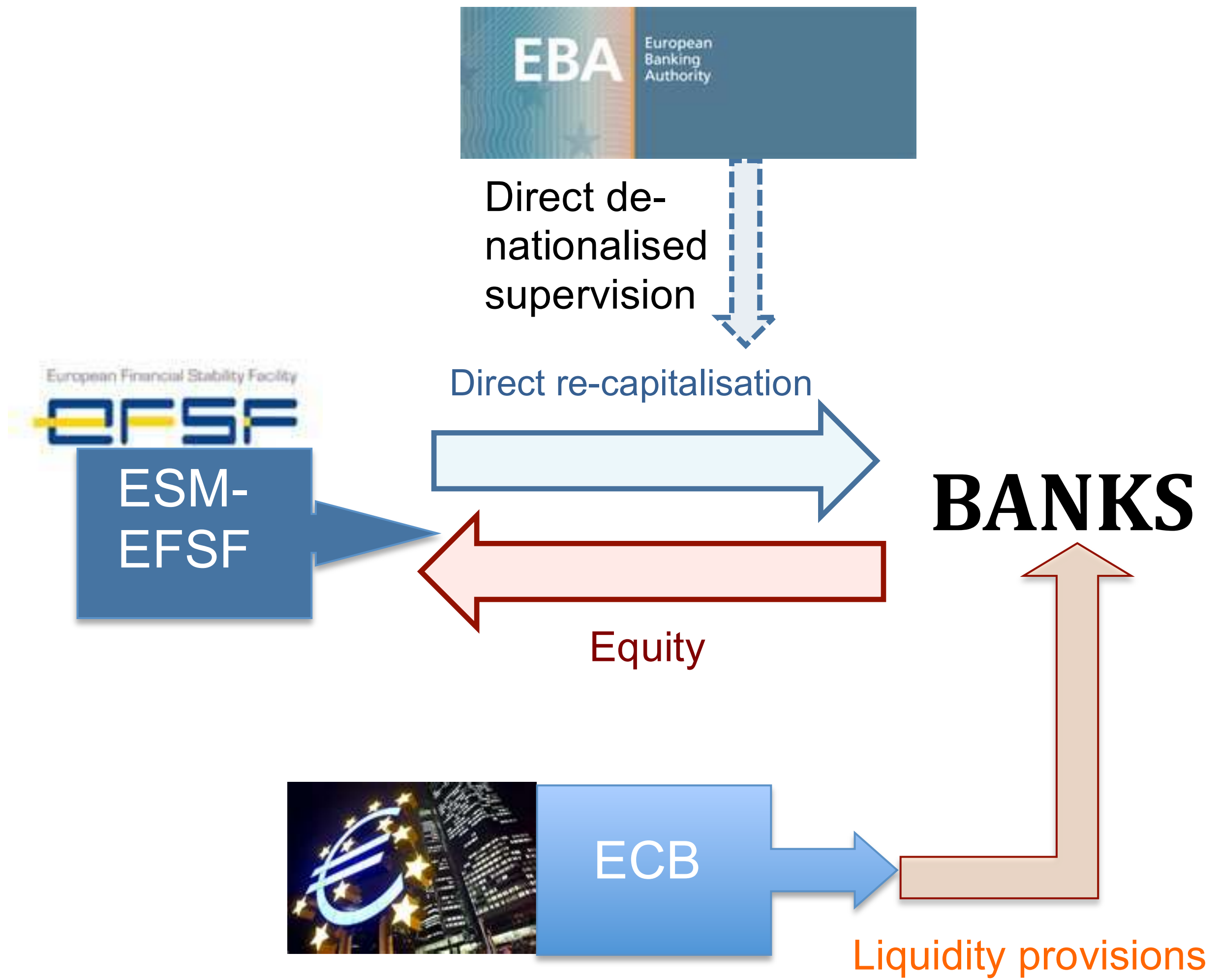
The Eurozone must be turned into a single banking area with a single authority that supervises directly and recapitalises the area's banks. To this purpose, existing national boundaries are to be dismantled, together with national supervisory authorities. The currently confederate EBA is to be re-configured as a unitary agency with a board comprising officials drawn from member-states, plus representatives from the ECB and the EFSF/ESM.

With the EFSF/ESM now relieved of its task to fund the public debt of insolvent member-states, the largest share of its capital is to be used for the purposes of direct bank recapitalisations. These capital injections shall flow directly from the EFSF/ESM, under the supervision of the EBA and the ECB, to the banks but without mediation from the national governments and without these capital injections counting as part of national debt. In exchange, equity in the recapitalised banks is passed on to the EFSF/ESM which is then re-sold to the private sector when the EBA and ECB judge that banks have been sufficiently recapitalised.

In summary (see also the diagram below), banking supervision is Europeanised, the nexus between national (sovereign) debt and banking losses is broken, the 'cosy' (and often problematic) relationship between national politicians and 'national' bankers is interrupted, and in this manner recapitalisation can proceed effectively at the European level.

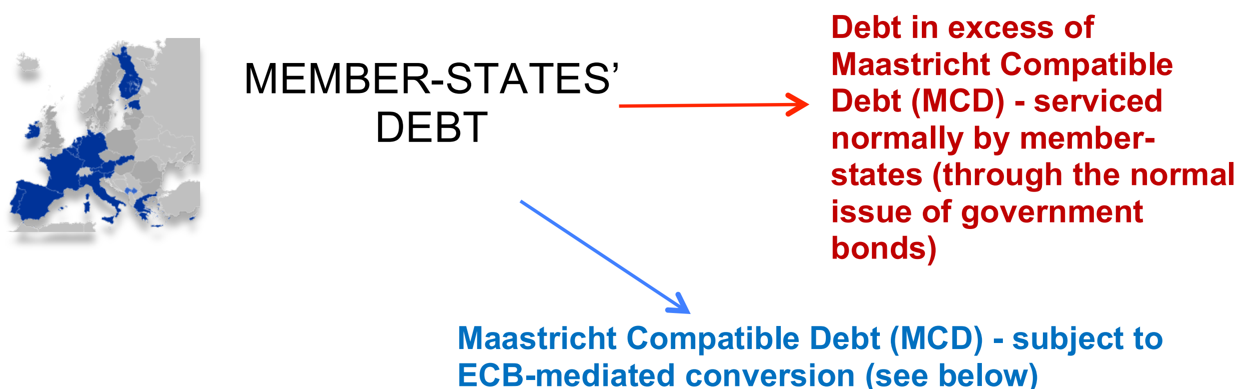
Participating institutions: EBA, ECB and EFSF-ESM

EFSF/ESM-EBA-ECB mediated Single Banking Area



POLICY 2 – Dealing with the sovereign debt crisis by means of an ECB-EFSM/ESM mediated conversion of member-states' Maastricht Compliant Debt

Since the Maastricht Treat and the Stability and Growth Pact, each member-state is permitted, by the Maastricht Treaty, to run up sovereign debt up to 60% of GDP. Since the Crisis of 2008, most Eurozone member-states have exceeded this limit. We propose that the ECB offers member-states the opportunity of a Debt Conversion for their Maastricht Compliant Debt (MCD) but that the national shares of the converted debt would continue to be serviced by member-states.



The ECB, faithful to the non-monetisation constraint (a) above, does not seek to buy or guarantee sovereign MCD debt through monetisation (direct or indirect). Instead it acts as a go-between, mediating between international and European investors, on the one hand, and member-states on the other. In effect, the ECB orchestrates a *conversion servicing loan* for the MCD and for the purposes of servicing their bonds upon maturity.[5]

The *conversion servicing loan* works as follows: Governments that wish to participate in the scheme can do so on the basis of Enhanced Cooperation, which needs at least none member-states but also means that those not opting for it can keep their own bonds even for their MCD. Refinancing of the national share of the debt, now held in ECB-bonds, would be by member-states but at interest rates determined by the ECB. The shares of national debt converted to ECB-bonds are to be held by it *debt accounts* for the member-states concerned.

[5] E.g. for a member state whose debt to GDP ratio is 90% of GDP, the ratio of its debt that qualifies as MCD is 2/3. Thus, when a bond matures with face value, say, €1 billion, two thirds of this (€666 million) will be paid (redeemed) by the ECB.

These cannot be used as collateral for credit or derivatives creation.[6] Member-states undertake to redeem bonds in full when redemption is due if the holders opt for this rather than to extend them at lower more secure rates offered by the ECB.

To safeguard the credibility of this conversion, and to provide a backstop (for the ECB-bonds) that requires no ECB monetisation,

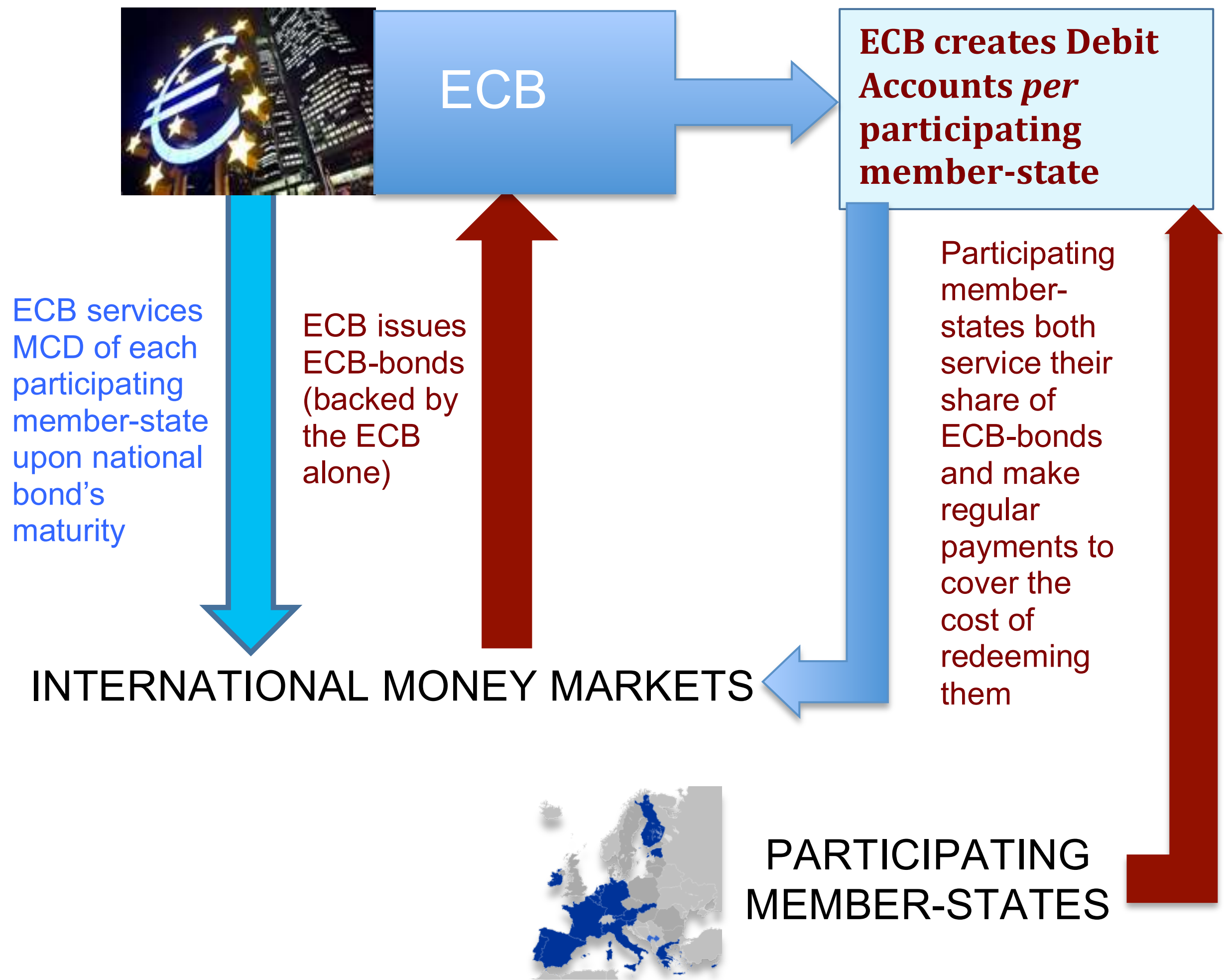
(i) member-states agree to afford their ECB debit accounts super-seniority status, *and*

(ii) the ECB's *conversion servicing loan* mechanism is insured by the EFSF/ESM. E.g. if a member-state goes into a disorderly default before an ECB-bond issued on its behalf matures, that ECB-bond payment is covered by insurance purchased or provided by the EFSF/ESM.

Participating institutions: ECB and EFSF/ESM

The following figure sums up Policy 2.

[6] Any more than a personal debit card can be used for credit.



ECB-bond Assurance Scheme

1. Participating members agree ***super-seniority status*** to their Debit Accounts
2. ESM provides insurance to the ECB in case of insufficient payments by members-states into their ECB Debit Accounts

POLICY 3 – An Investment-led Recovery and Convergence Program

Summary

We propose an Investment-led Recovery and Cohesion Program which is fully Europeanised (just like the banking sector and the Maastricht-compliant debt of member-states). Its twin task: To provide investments that are not backed by the taxpayers of the surplus countries and, additionally, to tackle the intra-Eurozone imbalances through heighted investment in the areas that need it the most. Financed fully by EIB-EIF bonds (along the lines of EIB-bond financing that has a sterling track record), idle savings in Europe and, importantly, internationally can be shifted into productive investments in the European regions where they will help provide essential public and private goods (which are, otherwise, under-supplied), rebalance competitiveness, as well as generate the incomes from which the most precarious debts can be repaid. (See the diagram at the end of this section for a visual summary of the proposed policy.) *Participating institutions: EIB-EIF*

Rationale

Other than the presumption of recent austerity policies that growth comes through rigour alone, when the outcome may be *rigor mortis* for the Eurozone, there has been displacement of what Europe already can do with its existing institutions, and a failure to think in a global context. Thus finance for recovery can be gained by recycling global surpluses into Eurobonds. Investment in them would be by the central banks of emerging economies and sovereign wealth funds. These would not be national bonds denominated in euros but EU bonds. European recovery is vital for the BRICS to sustain their exports. They also want a more plural global reserve currency system to be able to reduce their dependence on the dollar.

An example of displacement of what the EU can do with its existing institutions has been a European Commission proposal for 'Project Bonds' and that these should be guaranteed by member states. This not only assures opposition from many of them, not least Germany, but entirely neglects that bonds on its own account for project financing have been issued successfully the European Investment Bank (EIB) since 1958, without such guarantees. There is no need for new 'Project Bonds'.

Additionally, we ought to note that:

- There are increasing calls for bonds to finance infrastructure, as if this has not been happening through the EIB for more than half a century. There is little to no recognition either that the remit of the European Investment Bank since the Amsterdam Special Action Programme of 1997 has been not only in infrastructure such as transport and communications networks but also social investments in health, education, and the urban environment and its

regeneration. Nor is it recognised that since the Lisbon European Council in 2000 it has accepted a specific remit for cohesion and convergence.[7]

- There is no high profile awareness that EIB investment finance need not count on national debt. None of the major Eurozone economies, nor Greece, Portugal or Ireland does so. Nor need any others, since this is a national decision by governments and their central banks rather than embodied in or needing amendments EU Treaties.
- Nor need Eurobonds count on national debt any more than US Treasury bonds, which do not count on the debt of California or Delaware. Nor do they need a common fiscal policy or fiscal transfers to service them. They can be serviced by the member states that gain from them for project finance, without fiscal transfers between member states.
- Nor need restarting growth through investment projects funded by Eurobond necessarily be long-term. In a trawl of member states in 1994 it was found that projects that already had received planning approval but had been shelved because of the Stability and Growth Pact totalled some 750 bn ecu. Now, after three years of austerity, they are likely to approach or exceed 2 trillion euros, especially if postponed TENs projects are taken into account.
- There is a widespread but false presumption that public spending drains the private sector, when it sustains it. This reflects the 'crowding out' hypothesis without recognising that even for Milton Friedman this only would be the case at full employment. Public investment finance 'crowds in' private investment, income, and employment. Public investment multipliers also are higher than fiscal multipliers – up to 3 or over rather than only 1 plus.[8]
- There is similar false presumption that one cannot solve the crisis by 'piling debt on debt'. It depends on which debt, borrowed for what purpose. Piling up national debt at interest rates of up to 7 per cent is unsustainable. Funding inflows to the Union through Eurobonds is not when the interest rate could be less than 2 per cent,[9] and when this funds investments that generate not only recovery but also direct and indirect tax revenues through growth and higher levels of employment.

Thus debt is only one facet of the crisis. Its inverse is the mountain of European and global savings lacking investment outlets. The task is not to tax-and-spend within Europe but to mobilise both European savings and global surpluses into social investments which both can recovery growth but also enhance economic and social

[7] Europen Investment Bank (2008). *Fifty years of sustainable investment.* Luxembourg.

[8] Creel J., P. Monperrus-Veroni & F. Saraceno (2007), Has the Golden Rule of public finance made a difference in the United Kingdom? *OFCE Working Papers* 2007-13. Paris: Observatoire Français des Conjonctures Économiques..
Creel, J., Hubert, P. and Saraceno, F. (2012) Should the Stability and Growth Pact be strengthened? OFCE blog. February 29th. Paris: Observatoire Français des Conjonctures Économiques.

[9] Bloombergs have indicated to us that US financial institutions could invest in Eurobonds at 1.9 per cent. The central banks of the emerging economies could do so at less since their main concern is not a rate of return but a more secure store-of-value for their surpluses than the dollar.

cohesion by directing them into the deficit regions that are currently buckling under the unbearable weight of fiscal consolidation.

The European Investment Bank

- Since gaining its social investment terms of reference from the European Council in 1997 the European Investment Bank quadrupled its annual lending to over €80 billions. But, despite the EIB's more than half century of success there also are questions whether it can replicate this again without parallel support.
- For the EIB is highly dependent on investments in its bonds from pension funds which are statutorily obliged to invest only in AAA rated finance. It also has had a house rule, rather than a Treaty obligation, to seek co-finance for its investments either from national governments or national partners, both of which have been compromised by reactions to the Eurozone crisis since 2009.
- Eurobonds issued by the EIF can offset this.

Eurobonds by Enhanced Cooperation

One of the main recommendations by one of us 1993, in advice to Jacques Delors that Europe should establish a European Investment Fund to countervail the deflationary effects of the debt and deficit conditions of the Maastricht Treaty. The proposal was derailed in 1994, both because of vehement resistance from the Economy and Finance Directorate of the Commission and the resistance, then as now, of Germany to EU bonds.[10]

Bur Delors manage to get the European Investment Fund established. In recent evidence to the Economic and Social Committee of the EU, both the Fund and the EIB confirmed that it could fulfil its original design aim to issue EU bonds without a Treaty revision.[11]

The Economic and Social Committee then endorsed the principle that Eurobonds could be adopted by 'enhanced cooperation' whose Treaty provisions are that such a policy can be adopted by nine or more member states without a vote on its adoption by others that do not support such a policy.

Article 20 (TEU) and Articles 326-334 (TFEU) provide that:

> "Enhanced cooperation should aim to further the objectives of the Union, protect its interests and reinforce its integration process. Such cooperation should be open at any time to all Member States. The decision authorising enhanced cooperation

[10] Stuart Holland (1993). *The European Imperative: Economic and Social Cohesion in the 1990s.* Foreword Jacques Delors. Nottingham: Spokesman Press, November.
[11] Economic and Social Committee (2012) *Restarting Growth: Two Innovative Porposals.* Brussels, February 23rd. http://www.eesc.europa.eu/?i=portal.en.eco-opinions&itemCode=22257

should be adopted by the Council as a last resort, when it has established that the objectives of such cooperation cannot be attained within a reasonable period by the Union as a whole, and provided that at least nine Member States participate in it".

The Council approval of an enhanced cooperation procedure may be unanimous or by qualified majority. But since all member states rather than only those in the Eurozone could gain from investment finance from Eurobonds which, like EIB bonds, need not count on national debt there is a realistic prospect of its adoption, not least in view of the outcome of the election of François Hollande in France but also because George Osborne has been calling for Eurobonds on the understandable grounds that UK exports will suffer if there is no recovery of the EU economy.

Competitiveness, the periphery and a European Venture Capital Fund

Eurobonds issued by the EIF could finance a European Venture Capital Fund, which also was one of its main design aims in advocating it in 1993 to Delors.

This was based on recognition that interest on loan finance both deters new start-ups and then strangles many of them before they have been able to gain markets. But the design aim was defeated by opposition from the Economy and Finance Directorate General of the Commission and the role of the EIF was reduced not even to loans to SMEs, but loan guarantees.

The Fund's threshold for such guarantees, at 5 million ecu, also was top high for many small and medium firms. It then did not offer these direct but only through national financial intermediaries. The outcome was that the Fund, by 1999, had managed to guarantee loans only equivalent to 1 bn ecu.

But the proposal now that a European Venture Capital Fund could be financed by Eurobonds issued by the EIF has gathered support from both the trades unions and the employers' confederations represented on the Economic and Social Committee of the EU supported the proposal that it should do so in February 2012.[12]

Promoting convergence

This has significant implications for convergence since central European economies such as Germany and Austria already have excellent finance for small and medium firms through their *Mittelstandpolitik.* It is the peripheral economies that need this. Eurobond finance for a European Venture Capital Fund also could overcome the constraints of the Framework programmes for Science and Technology.

One of us, in the drafting of the Fourth Framework Programme, gained acceptance that its programmes should include an institution or enterprise from a Schedule 1 (underdeveloped) region and gain preference for consideration if they also included a

---

[12] Economic and Social Committee (2012), Op cit.

Schedule 2 (depressed urban) area. The aim of this was to bring these close to the innovation frontier of Europe's most advanced regions. But while this was adopted, it was found that 19 out of 20 applications to FP4 were unsuccessful because of lack of Commission Own Resources, while some 700 projects were signed off as meeting scientific criteria but did not create a single new high-tech start-up.

By contrast, there would be no limit in principle to a European Venture Capital Fund financed by Eurobonds.

The periphery also would gain from their financing the TENs. Most of the high speed rail networks needed in the centre have been completed, but not in the periphery because of lack of national co-finance for EIB funding.

Europeanising Investment Finance

The principle here is that investment is Europeanised (just like the banking sector and the Maastricht-compliant debt of member-states) but without the need for debt buy-outs, or mutual national guarantees, or a common fiscal policy since the joint EIB-EIF bonds to finance it would be serviced by individual member states.

In effect, the EIB-EIF investments will operate in a manner similar to Keynes' original idea of a global Clearing Union; only in this case it would be an explicit investment-directed surplus recycling mechanism. But the proposals also are post Keynesian since concerned not only to achieve higher levels of effective demand but also to meet latent demand for such social investment projects which have gained planning and environmental approval

Shifting social investments to Europe also would release a major share of national fiscal revenues to achieve the as yet unrealised commitment of the Essen European Council to 'more labour intensive employment in the social sphere'
and therefore enabling more teachers and smaller class sizes more health workers for an ageing population.
Debt is only one facet of the Crisis. The other is a mountain of idle savings whose owners lack the confidence or the coordination to channel into productive investments. Thus, the task is not to tax-and-spend but to find ways to energise idle savings both in aggregate and, more importantly, to direct them into the deficit regions that are currently buckling under the unbearable weight of fiscal consolidation thus pushing investment into negative territory (instead of imbuing investors with greater confidence).

To deal with the overall underinvestment crisis, the European Investment Bank (EIB) shall continue funding large scale investment programs while the European Investment Fund (EIF) will fund small and medium sized firms and start-ups, offering venture capital for the purposes of kick-starting growth in high technology, green energy, environmental health, education and urban renewal projects.

Why are the EIB-EIF not doing this now? They do, only the volume of investments is severely circumscribed because of the convention that 50% of project funding be financed by member-states. As member-states are fiscally stressed, the EIB-EIF's growth potential is minimised. Our proposal is that this 50% co-financing, which now acts as a mighty break on growth (courtesy of the indebtedness of member-states), comes from additional, net, ECB-bond issues.

Aggregate investment in the Eurozone thus funded (50% by EIB-bonds and 50% by ECB-bonds) could be calibrated to a level equal to some proportion of total Eurozone GDP while the distribution of funding within the various Eurozone regions (and not just countries) should be designed to counteract the internal imbalances of competitiveness and intra-Eurozone (im)balance of payments.[13]

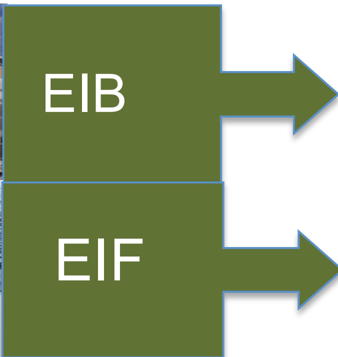
[13] In effect, the EIB-EIF investments will operate in a manner not too dissimilar to Keynes' original idea of a Clearing Union; only in this case it would be an explicit, investment-directed surplus recycling mechanism.

Investment-led Recovery, Cohesion and Rebalancing Program, by the EIB-EIF

EIB funds infrastructural projects plus in investments in education, health, urban renewal and environmental protection

EIF co-finances EIB projects plus provides a European Venture Capital Fund

EIB-EIF Collaborative Funding of Investments



The EIB and the EIF co-finance their projects by issuing their own bonds

PROJECT REVENUES generate repayments to EIB-EIF

5. Epilogue: Three policies representing a gestalt shift that can liberate Europe from debilitating false dilemmas

Two years of crisis have culminated in a clear and present danger that Europe not only experiences another recession and a painful dismantling of the Eurozone but, also, the demise of the European Union, of open borders, of open minds and the risk of a global collapse.

While this process of deconstruction is eating away at the foundations of Europe's potential for shared prosperity, and global cooperation, Europeans are imprisoned by four, false, dilemmas.

- The current terms of reference of the debate are trapped in a dyadic logic of austerity versus tax-and-spend stimulus policies.
- They are trapped also in a presumption that any solution needs to be agreed by Germany whereas the neglected EU provision for decision-making by enhanced cooperation does not need the consent of Germany.
- There is a presumption that the issue at hand is how to persuade Germany and the few other remaining surplus countries to bankroll the rest when this neither necessary nor desirable.
- There is fret over the pros and cons of moving toward federation as if this could be agreed in time to stop what may be an imminent disintegration of the Eurozone.

It is our contention that these are, indeed, false dilemmas that imprison our thinking, immobilise us and are, largely, responsible for delays, false starts, and ill-fated 'solutions'. By contrast ***The Modest Proposal*** counters that:

- the dilemma between austerity and debt-fuelled growth policies is irrelevant
- lax monetary policy on behalf of the ECB, or greater wage/price inflation in Germany and the rest of the surplus nations is unlikely to deal with the crisis
- effectively
- Germany and the rest of the surplus nations need not bankroll either a European Recovery, Rebalancing and Convergence Program nor the management of excessive sovereign debt
- Federal moves and Treaty changes may be desirable but will take too long and are not needed to resolve the crisis from now.

On this basis the ***Modest Proposal***'s three policies are simple and feasible steps by which to deal decisively with Europe's *banking crisis*, the *debt crisis* and the *under-investment, unemployment and internal balance of payments crisis*.

In one stroke (Policy 1), by creating a single banking sector, banking losses are separated from stressed sovereign debt and recapitalisation can proceed properly and rationally.

In another stroke (Policy 2), the Eurozone's mountain of debt shrinks (through an ECB-EFSF/ESM conversion of Maastricht Compliant member-state Debt).

Third, (Policy 3) the EIB-EIF jointly recycle European savings and global surpluses enabling recovery and enhancing the potential for cohesion and convergence.

At the political level, the three policies envisaged by the **Modest Proposal** constitute a process of ***Decentralised Europeanisation***, to be juxtaposed against an ***Authoritarian Federation*** that has not been put to European electorates, is unlikely to be endorsed by them (as evidenced by serial falls of governments since 2009), and, critically, offers them no assurance of higher levels of employment and welfare.

In essence, what we are proposing is that three areas of economic activity are Europeanised: banking supervision, sovereign debt management and a recycling of European and global savings into socially productive investment flows which also will vastly advantage the private sector. However, our proposed Europeanisation retains a large degree of subsidiarity that is:

- consistent with greater sovereignty for member-states than a supra-national federalism, combined with the minimal collective rationality required for the effective governance of the common currency area
- commensurate with the principle of reducing excess national debt (once banks, debt and investment flows are Europeanised)

While broad in scope and ambition, the ***Modest Proposal*** suggests no new institutions and it aims at redesigning the Eurozone with minimal use of new rules, fiscal compacts, or troikas. It requires no prior agreement to move in a federal direction while allowing for consent through enhanced cooperation rather than imposition. It is in this sense that this proposal is, indeed, modest and something on which governments should act.