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#FINANCIALSTABILITY

#MARKETDISCIPLINE

# SHARED SCEPTICISM, DIFFERENT MOTIVES: FRANCO-GERMAN PERCEPTIONS OF A COMMON EUROPEAN SAFE ASSET

## Executive summary

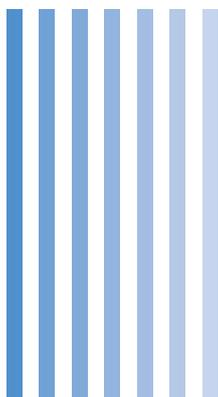
### ■ KRIS BEST

Guest Author,  
Jacques Delors Institute  
Berlin

A common European safe asset is a highly contentious proposal within the Euro area reform agenda. Various safe asset proposals have been put forward since the onset of the Euro crisis ranging from Eurobonds to European Safe Bonds (ESBies), also known as Sovereign Bond-Backed Securities (SBBS), which currently enjoy the institutional support of the European Commission as well as the High-Level Task Force on Safe Assets at the European Systemic Risk Board. Its proponents argue that a European safe asset is required to break the bank-sovereign nexus and limit destabilising capital flows, ultimately improving financial stability in the Euro area. Nevertheless, the concept of a European safe asset remains controversial among national policymakers; some consider the idea promising, while others see it as a threat to market discipline, national sovereignty, or long-term fiscal stability.

In a joint declaration made in June 2018, France and Germany strongly rejected the SBBS proposal, claiming that it presented more disadvantages than benefits. Beneath this superficial agreement, however, a deeper investigation into the safe asset debate in both countries reveals considerable differences in how policymakers engage with safe asset proposals, assess the costs and benefits, and set conditions for its acceptability. These are rooted in more fundamental differences between the two countries in beliefs, values, and interests linked to economic policy. Broadly, while the French debate is heterogenous, technical, and focused on assessing the present effectiveness of a safe asset in improving Euro area financial stability, the approach in Germany is more uniform, straightforward, and focused on avoiding moral hazard and other long-term risks. Nevertheless, there is some evidence that the French position on safe assets has moved closer to the German position over time.

Although the safe asset debate is likely to endure past the Franco-German rejection, the present investigation shows that there are key questions, political as well as technical, which remain to be resolved with any safe asset proposal. At least as far as the debate in France and Germany is concerned, the main points of contention both between and within the two countries concern the degree of joint liability that would be acceptable or necessary for the proposal to work, the regulatory treatment of the safe asset and of sovereign exposures in general, and the appropriate design of the asset to preserve market discipline.



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# INTRODUCTION

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Safe assets as an element of the Euro area reform agenda have seen a resurgence of interest in the last few years, notably through the work of the European Systemic Risk Board's (ESRB) High-Level Task Force on Safe Assets, which presented its findings in early 2018.<sup>1</sup> Nevertheless, a common European safe asset is one of the more contested elements of this agenda: while many economists consider that it could deliver substantial macroeconomic benefits, others are just as convinced that 'safe' asset proposals are unneeded at best and a threat to the financial stability of the Euro area at worst. This is particularly true of the Sovereign Bond-Backed Securities (SBBS) proposal endorsed by the ESRB's High-Level Task Force, which has proven to be highly controversial among national policymakers, especially in France and Germany, the Euro area's largest economies and so-called historical 'motor'.

Since the 2017 French presidential election, the Macron administration has pushed to reinvigorate the long-standing partnership between France and Germany and to put forward a joint proposal for further Euro area reform. In June 2018, a joint declaration and roadmap were proposed at Meseberg, outlining the key elements of the Franco-German agenda – and rejecting the possibility of introducing SBBS, the most prominent safe asset proposal in recent years. A deeper investigation into why that is the case is not only useful in understanding the thinking behind the economic policy decisions of the Euro area's two most influential members, but also casts light on more fundamental divisions in economic perspectives or worldviews which have shaped the Economic and Monetary Union (EMU) since its inception and continue to define debates over the future of the Euro area.

This policy paper explains the concept and policy rationale of a common European safe asset and explores how the various proposals – from Eurobonds to SBBS – have evolved with the debate over time, emphasising the critical issues and points of contention. It then shows how the safe asset debate is viewed differently in France and Germany based on research interviews conducted with 21 high-level policymakers and academic experts representing the key economic, fiscal, and monetary institutions in both countries. It presents a framework for understanding Franco-German economic policy disagreements, identifies the principle areas of disagreement, and describes how these two approaches work together in practice.

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1. ESRB High-Level Task Force on Safe Assets (HLTF), 'Report of the High-Level Task Force on Safe Assets Volumes I & II', January 2018.

# 1. SAFE ASSETS: AN EXPLAINER

## 1.1 Definition of a safe asset

In general terms, a safe asset is a tradeable financial asset, usually a sovereign bond, which is widely perceived to have a low or non-existent risk of default – that is, the asset is widely perceived by market actors to be safe. A safe asset also has certain attributes which are highly desirable in financial markets. Namely, a safe asset:

- Is *extremely liquid* with a deep market, to the point of being a *de facto* cash-equivalent;
- Has a *stable market*, with exceptionally low volatility in price;
- Is *information insensitive*, in that it can be accepted at face value without the need to gather additional information about its riskiness.

As safe assets are highly liquid and provide a dependable store of value, they serve a number of important functions in financial markets. For example:

- *Institutional investors* such as pension funds invest a large amount of their capital in safe assets due to their perceived safety and stability;
- Banks and other financial institutions aim to hold a certain amount of safe assets in their portfolio to improve their *capital position* and to *meet regulatory requirements* (i.e., by creating a buffer against potential losses);
- Banks hold safe assets to ensure an adequate *liquidity coverage ratio* (i.e., ensuring that the bank has enough high-quality liquid assets at its disposal to cover outflows in a temporary liquidity crunch);
- Safe assets are key sources of *collateral* needed for banks to access credit through the Eurosystem, or to conduct short-term repo transactions between commercial banks; and
- Within a given domestic economy, the yield curve on safe assets acts as a *benchmark* from which to determine the appropriate risk premium on other assets.

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A SAFE ASSET WILL ACTUALLY INCREASE IN VALUE DURING PERIODS OF FINANCIAL INSTABILITY

One of the more interesting characteristics of a safe asset, deriving directly from its perceived safety, is that the safe asset will actually *increase* in value during periods of financial instability, at a time when the prices of other assets are falling. This seemingly paradoxical phenomenon results from the ‘flight to safety’ that occurs as investors search for a ‘safe haven’ in which to store their capital; a safe asset has therefore been described as a ‘good friend’ which can be relied upon in difficult times.<sup>2</sup> The fact that a safe asset will not only maintain but actually increase in value during a crisis allows the issuer (e.g. a government) to benefit from a ‘safe haven’ liquidity premium (e.g. guaranteed access to financial markets at preferential borrowing rates), which may be substantial. The safe haven premium on US Treasury bonds, for example, which are

2. Brunnermeier, Markus, Harold James, and Jean-Pierre Landau, ‘The Euro and the Battle of Ideas’ (Princeton, NJ: Princeton University Press, 2016), 182.

considered to be the world's leading safe asset, has been estimated at between 26 and 72 basis points – saving the United States an estimated 0.25% of GDP per year in interest costs.<sup>3</sup>

## 1.2 Policy rationale as an element of Euro area reform

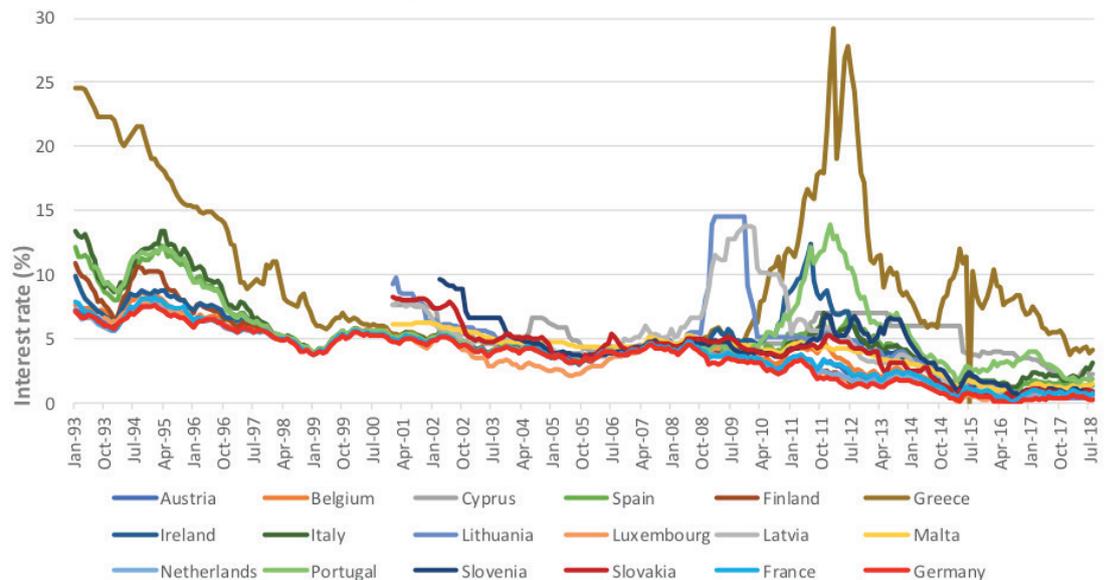
Sovereign debt is the primary safe asset in most national economies. Three factors play a role in the perception of sovereign bonds as inherently safer than other domestic assets such as corporate or local government debt, namely that the sovereign:

- Has *revenue-raising capabilities* above and beyond those of other actors, including the ability to tax its own citizens and borrow internationally;
- Tends to enjoy *de facto control over its domestic currency*; and
- Has access to the domestic central bank as a *lender of last resort*.

Through requiring Euro area members to giving up their domestic currencies and access to a domestic lender of last resort, the nature of the EMU removes the second and third sources of safety for Euro area states and significantly constrains the first with respect to debt issuance. Some economists have therefore argued that the structure of the EMU has reduced much of the sovereign debt in the Euro area to a 'semi-safe' status which cannot hold up in a financial crisis, leaving German government bonds as the only truly safe asset in the Euro area.<sup>4</sup> This interpretation would be consistent with the observed yields on 10-year Euro area sovereign bonds, which converged around the German bund (10-year bond) with the introduction of the Euro, diverged considerably at the onset of the Euro crisis, and have since returned to limited convergence with the German bund after 2012 (Figure 1).

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THE STRUCTURE OF THE  
EMU HAS REDUCED MUCH  
OF THE SOVEREIGN DEBT  
OF THE EURO AREA TO A  
'SEMI-SAFE' STATUS

FIGURE 1 ■ Interest rates on 10-year Euro area government bonds, 1993–2018.



Source: European Central Bank, *Interest rate statistics (2004 EU Member States & ACCBs)*, Long-term interest rate for convergence purposes.

3. Krishnamurthy, Arvind, and Annette Jorgensen, 'The Aggregate Demand for Treasury Debt', *Journal of Political Economy*, 120 (2012), 233–67.

4. Brunnermeier et al., 2016; van Riet, Ad, 'Addressing the Safety Trilemma: A Safe Sovereign Asset for the Eurozone', ESRB, 2017



GERMANY HAS BEEN ABLE TO BENEFIT FROM A SIZEABLE ECONOMIC RENT IN THE FORM OF LOWER BORROWING COSTS, ESPECIALLY AT THE HEIGHT OF THE EURO CRISIS

Illustrating the defining characteristic of a safe asset, namely that it increases in value in periods of economic instability while other asset prices fall, Figure 1 also shows that yields on the German bund – as well as similar ‘safer’ assets such as Dutch and Luxembourgish bonds – did in fact decrease after the onset of the global financial crisis in 2008. This reflects an increase in the value of the bund as investors fled from riskier assets (e.g. Greek, Spanish, or Portuguese bonds) into the ‘safe haven’ of Germany and similar countries. As the issuer of the dominant safe asset in the Euro area, Germany (and the other ‘safer’ countries) has therefore been able to benefit from a sizeable economic rent in the form of lower borrowing costs, even, or rather especially, at the height of the Euro crisis.

Since the onset of the Euro crisis, several different arguments have been put forward by economists in favour of introducing a common safe asset at the European level which would replace the bund as a ‘safe haven’ and benchmark asset and fill the same essential financial market functions that national sovereign bonds do today, i.e. acting as a dependable source of value to meet liquidity needs, collateral needs or regulatory requirements. Although the precise benefits expected from such an asset depend to some extent on its design, the proponents of a common European safe asset tend to centre on two fundamental arguments which are common to almost all proposals:

- *Improving Euro area financial stability* by limiting destabilising capital flows; and
- *Breaking the bank-sovereign nexus* by limiting domestic bias in bank portfolios.

The first argument relates to the ‘flight to safety’ phenomenon described above, in which investors tend to invest in higher-yield riskier countries during good times but shift their capital into lower-yield safe assets in safer countries during bad times. The result is a sharp reversal in capital flows which further increases financial instability and leads to greater fragmentation in national bond markets, as demonstrated in Figure 1 above – a problem which is then aggravated in a common currency area by the perceived ‘quasi-safe’ (i.e. not truly safe) status of Euro area sovereign debt as well as the loss of the exchange rate mechanism as a tool for macroeconomic adjustment. It has therefore been argued that a common European safe asset which brings together the sovereign debt of Euro area Member States in some form would ensure that the ‘flight to safety’ response of investors would not result in large capital flows from one country to another, but rather into a common asset that would prevent further fragmentation in the market for sovereign debt and ensure that crisis-stricken countries maintain access to a stable and low-cost source of financing.<sup>5</sup>

The second argument addresses the bank-sovereign nexus, also referred to as the bank-sovereign ‘doom loop’. Banks tend to exhibit a domestic bias, meaning that they hold large amounts of their own government’s debt. This tendency is further encouraged by current EU banking regulations, which assign a zero risk weight to all EU sovereign debt when calculating capital requirements regardless of how risky the debt may actually be, providing regulatory incentives for banks in riskier countries to accumulate domestic sovereign bonds beyond a risk-optimal level (see box below).

5. Brunnermeier, Markus, Sam Langfield, Marco Pagano, Ricardo Reis, Stijn Van Nieuwerburgh, and Dimitri Vayanos, ESBies: ‘Safety in the Tranches’, ESRB, 2017; Claessens et al., 2012; van Riet, 2017.

*European banking regulations and the zero risk weight for sovereign exposures*

Under the international Basel II framework, assets held by banks are assigned 'risk weights' which determine the amount of equity capital that the bank is required to hold against potential losses. The Basel framework assigns a risk weight of zero to sovereign bonds with a credit rating of AA- and above, indicating that these assets are considered to have the lowest possible risk of default and that no equity needs to be set aside against that exposure (i.e., freeing up equity that can then be used to fund other, riskier assets). While Basel applies positive risk weights to all sovereign debt rated below AA-, an exemption in the framework allows countries to set lower risk weights (including zero risk weights) for their own sovereign bonds issued in the domestic currency.<sup>6</sup> This exemption is used in the European Capital Requirements Regulation to set an area-wide zero risk weight for sovereign bonds issued by the central governments of all EU Member States, regardless of their actual credit rating or riskiness. Since the Regulation treats sovereign bonds from all EU countries as if they were equally safe, banks have an incentive to hold larger amounts of riskier, higher-yield EU sovereign debt than would otherwise be optimal. This is particularly destabilising in combination with the domestic bias phenomenon.<sup>7</sup>

In this context, if the credit risk of the government increases and investors fear a possible default, the value of its sovereign bonds will fall, which in turn lowers the value of the assets held by domestic banks (since they hold large stocks of government debt) and weakens their capital position. If the capital position of domestic banks declines to the extent that their solvency comes into question and a government bailout is expected, investors may doubt the already-stressed government's ability to pay and divest further, causing bond values to sink even lower and concerns over the solvency of both the banks and the sovereign to intensify – hence the 'doom loop'. Proponents of a European safe asset have argued that a common safe asset would encourage banks to replace their excessive domestic bond holdings with the European asset, increasing diversification and lowering risk within the financial system.<sup>8</sup>

While these two points comprise the most common and fundamental arguments for a European safe asset, proponents have also listed a range of other potential benefits, including improved monetary policy transmission; cultivation of an area-wide liquidity premium resulting in overall lower costs of borrowing in the Euro area; increased fiscal discipline through the introduction of additional budgetary surveillance measures to accompany such an asset; and addressing a perceived shortage of safe assets within the Euro area.<sup>9</sup>

6. Bank for International Settlements, 'Discussion Paper: The Regulatory Treatment of Sovereign Exposures', 2017.

7. Schneider, Yannik M., and Sascha Steffan, 'Feasibility Check: Transition to a New Regime for Bank Sovereign Exposure?', European Parliament, 2017

8. Brunnermeier et al., 2017; Claessens, Stijn, Ashoka Mody, and Shahin Vallee, 'Paths to Eurobonds', Bruegel, 2012; ESRB HLTF, 2018.

9. See, for example: Claessens et al, 2012; van Riet, 2017; Gabor, Daniela, and Jakob Vestergaard, 'Chasing Unicorns: The European Single Safe Asset Project', Competition and Change, 22 (2018).

### 1.3 Types of safe asset proposals since the financial crisis

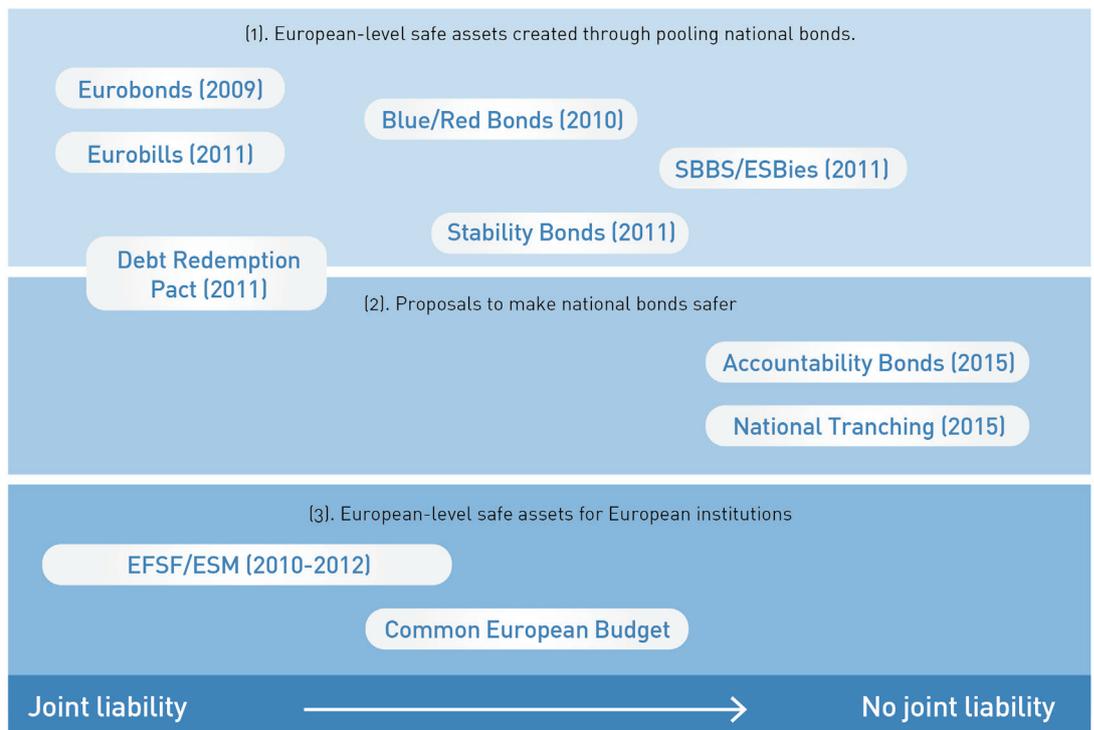
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CALLS FOR A COMMON  
EUROPEAN DEBT  
INSTRUMENT PRE-DATE  
THE CRISIS

While calls for a common European debt instrument pre-date the Euro crisis,<sup>10</sup> it was only after the onset of the crisis in late 2009 that safe asset proposals gained momentum as potential tools for the prevention and management of financial crises. The main proposals, which emerged mostly between the period of 2009 and 2012, had substantial differences in key design elements and consequences. While other authors have compared and classified safe asset proposals in different ways,<sup>11</sup> we can consider safe asset proposals as belonging to three broad groups:

- Proposals that create European-level safe assets through pooling sovereign bonds;
- Proposals that aim to make national bonds safer; and
- Proposals that create European-level safe assets for European institutions.

Proposals within each of these three groups can then be further differentiated by the extent to which they formally imply joint liability among Euro area members, i.e. the extent to which Euro area members would be held liable for other members’ debt obligations. Figure 2 shows the relative orientation of the some of the most prominent safe asset proposals since the Euro crisis, which are then described in detail below.

FIGURE 2 - Common safe asset proposals, compared



10. See e.g. European Primary Dealers Association, 2008; Giovannini Group, 2000.

11. See e.g. Claessens et al., 2012; Leandro, Alvaro, and Jeromin Zettelmeyer, 'The Search for a Euro Area Safe Asset', Peterson Institute for International Economics (PIIE), 2018.

## European-level safe assets created through pooling national bonds

These proposals aim to pool sovereign bonds in some form to create a new, European-level safe asset. These are the proposals most readily identifiable as ‘safe asset proposals’ and form the focus of this paper. Chronologically, these begin with classical Eurobonds featuring full joint and several liability of Euro area debt and have trended towards involving less and less joint liability over time, culminating in the SBBS/ESBies proposal which, in principle at least, does not require joint liability at all. These are described briefly below.

### *‘Classical’ Eurobonds*

The first ‘classical’ Eurobond proposals were put forward at about the same time in 2009 by Gros and Micossi<sup>12</sup> and de Grauwe and Moesen<sup>13</sup> with the aim to reduce fragmentation between national bond markets in the Euro area. The more detailed proposal consisted of a straightforward pooling of government debt through the issuance of a common ‘Eurobond’ with joint and several liability by a public issuing authority at the European or national level. Several variations on the Eurobond concept were then put forward over the following years to address the perceived moral hazard or adverse incentive problems of classical Eurobonds.

### *Blue/Red Bonds*

One of the most influential variations on the Eurobond concept was the Blue/Red Bond proposal put forward in 2010 by Delpla and von Weizsäcker at Bruegel.<sup>14</sup> Under the Blue/Red Bond proposal, governments could issue debt worth up to 60% of their GDP in the form of common European ‘Blue Bonds’, which would enjoy a joint and several guarantee by all participating states. Debt in excess of 60% of GDP would be issued in the form of national ‘Red Bonds’, which would not enjoy a joint or several guarantee and therefore be subject to a higher interest rate and default risk. This would act as an incentive to keep debt below the 60% threshold and thereby address one of the key criticisms of the original Eurobond proposal (namely, that it would encourage excessive borrowing).

### *Eurobills*

Under a proposal made by Philippon and Hellwig in 2011,<sup>15</sup> a European debt management office (DMO) would issue jointly and severally guaranteed ‘Eurobills’ for Member States, which would be similar to Eurobonds but with a maximum maturity of one year and an issuance cap for any individual state at 10% of GDP in order to prevent excess borrowing. Eurobills would also be granted senior status over national debt.

### *Stability Bonds*

Stability Bonds were a set of three options for the joint issuance of debt proposed by the European Commission in 2011 and 2012. These included either full or partial European substitution of national issuance with joint and several guarantees, or partial European substitution

12. Gros, Daniel, and Stefano Micossi, ‘A Bond-Issuing EU Stability Fund Could Rescue Europe’, Friends of Europe, 2009.

13. De Grauwe, Paul, and Wim Moesen, ‘Gains for All: A Proposal for a Common Eurobond, Centre for European Policy Studies’, 2009.

14. Delpla, Jacques, and Jakob Von Weizsäcker, ‘The Blue Bond Proposal’, Bruegel, 2010.

15. Philippon, Thomas, and Christian Hellwig, ‘Eurobills, Not Eurobonds’, VOX: CEPR’s Policy Portal, 2011.

of national issuance with several but not joint guarantees. The Commission released a Green Paper on Stability Bonds in 2011, but the proposal was not pursued further.

*European Safe Bonds (ESBies) / Sovereign Bond-Backed Securities (SBBS)*

European Safe Bonds (ESBies), also referred to by some as ‘synthetic Eurobonds’, were proposed by the Euro-nomics Group of economists in 2011 as a method of creating a European safe asset without debt mutualisation or joint liability.<sup>16</sup> Under the ESBies proposal, a public or private special purpose vehicle would purchase a portfolio of national government bonds and issue common securities in the form of a senior tranche (ESBies) and a junior tranche (European Junior Bonds, or EJBies). The safety of the ESB would derive from the combination of diversification and tranching. ESBies have since been rebranded as Sovereign Bond-Backed Securities (SBBS) and were the subject of the European Systemic Risk Board’s High-Level Task Force on Safe Assets. On the basis of the Task Force results, the European Commission then put forward a proposal to ease the regulatory framework for SBBS in May 2018.<sup>17</sup> Interviewed officials at the national and European levels indicated that SBBS/ESBies are by far the safe asset proposal that has been considered most seriously by policymakers and economists.

## Proposals to make national bonds safer

Unlike the first group, these proposals are not as readily classified as belonging to the family of ‘safe asset proposals’. These proposals are not primarily concerned with creating a new, *permanent* safe asset at the European level as the first group were, but rather with increasing the safety of national bonds.

*Debt Redemption Pact*

The Debt Redemption Pact was proposed by the German Council of Economic Experts in 2011.<sup>18</sup> Under this proposal, all national debt over 60% of GDP would be mutualised at the European level in exchange for a program of strict conditionality and austerity for the indebted countries. In this respect, the Debt Redemption Pact could have been classified within the first group of safe asset proposals, as it pools national debt to create a European-level asset subject to joint liability. However, the program was strictly intended to be a temporary, ‘one-time’ deal with a clear end-point, as all countries would be required under the proposal to reduce their debt to under 60% of GDP within 25 years. The primary intent of the Debt Redemption Pact was therefore not to create a lasting European-level safe asset but to reduce and maintain national debt at a sustainable level.

*Accountability Bonds*

The Accountability Bonds proposal by Fuest, Heinemann and Schröder (2015) suggested that a mandatory junior bond be introduced at the national level for any excess debt issued after

<sup>16</sup> Brunnermeier, Markus, Luis Garicano, Philip R Lane, Marco Pagano, Ricardo Reis, and Tano Santos, ‘European Safe Bonds (ESBies)’, The Euro-Nomics Group, 2012.

<sup>17</sup> See website of the European Commission.

<sup>18</sup> Bofinger, Peter, Lars Feld, Wolfgang Franz, Christoph Schmidt, and Beatrice Weder di Mauro, ‘A European Redemption Pact’, VOX: CEPR’s Policy Portal, 2011.

a country exceeds the structural budget deficit of 0.5% as specified in the Fiscal Compact.<sup>19</sup> Accountability Bonds would lose their value if the issuing country receives assistance through the European Stability Mechanism (ESM) and be subject to additional restrictions as well. The subordination of excess debt in the form of Accountability Bonds acts to ensure that the remaining 'standard' government bonds are safer.

#### *National Tranching*

National tranching was proposed in 2015 by Wendorff and Mahle with a similar approach to that of Accountability Bonds; namely, that national governments would issue their sovereign debt in senior and junior tranches, preserving the safety of the senior tranche.<sup>20</sup> Unlike Accountability Bonds, the issuance of junior bonds would not be linked to a structural budget deficit but based on a pre-determined ratio of senior to junior bonds (e.g. 70/30) to be applied to all newly-issued debt.

### **European-level safe assets for European institutions**

The third group of safe asset proposals consider that a European-level safe asset need not be based on national government bonds, but could emerge at the European level as part of a borrowing capacity for a European budget or for European institutions.

#### *Common European Budget*

The idea of introducing a fiscal capacity for the Euro area with the possibility of issuing its own debt in order to fund some form of stabilisation function is not new, and has recently seen a resurgence of interest under Emmanuel Macron.<sup>21</sup> Under these proposals, bonds could be issued directly at the European level. The debt would presumably be serviced either by Member State contributions or through a European tax.

#### *European Stability Mechanism & European Financial Stability Facility*

As pointed out by interviewees, a European-level safe asset technically already exists in the case of bonds issued by the ESM and European Financial Stability Facility (EFSF), which are guaranteed by Euro area Member States. The safety of ESM bonds is also ensured through the ESM's preferred creditor status.

## **1.4 Current state of the debate over a European safe asset**

The place of a European safe asset within the Euro area reform agenda is not without controversy. There has been significant debate among policymakers and economists as to whether a common safe asset is a necessary element of the reform agenda, with some arguing that on the contrary, certain so-called 'safe' asset proposals, particularly SBBS/ESBies, pose a con-

<sup>19</sup>. Fuest, Clemens, Friedrich Heinemann, and Christoph Schröder, 'Accountability Bonds: Eine Neue Art von Staatsanleihen', *Ökonomenstimme*, 2015.

<sup>20</sup>. Wendorff, Karsten, and Alexander Mahle, 'Staatsanleihen Neu Ausgestalten – Für Eine Stabilitätsorientierte Währungsunion', *Wirtschaftsdienst*, 95 (2015), 604–8.

<sup>21</sup>. Leandro and Zettelmeyer, 2018; Ubide, Angel, 'Stability Bonds for the Euro Area', Peterson Institute for International Economics, 2015

siderable financial stability risk to the Euro area.<sup>22</sup> Accordingly, the topic has disappeared and re-appeared a number of times in the debate over EMU reform. While common debt issuance was mentioned as a potential medium-term objective in the Four Presidents' Report of 2012, the idea of a safe asset disappeared entirely from the roadmap set out three years later in the 2015 Five Presidents' Report, before re-emerging in the Commission's 2017 Reflection Paper on the Deepening of the EMU.

In September 2016, the ESRB established a High-Level Task Force on Safe Assets in order to investigate the feasibility of introducing ESBies, now called SBBS. The Task Force concluded in its final report of January 2018 that 'gradual development of a demand-led market for SBBS might be feasible under certain conditions.'<sup>23</sup> A key question in the ESRB findings and in the broader debate over SBBS related to the regulatory treatment of such assets. Under the current regime, SBBS would not enjoy the same zero risk weight afforded to individual sovereign bonds, but would instead be treated as riskier asset-backed securities (ABS), removing the primary incentive for banks to hold them. In May 2018, on the basis of the Task Force findings, the European Commission therefore presented a proposal for an 'enabling framework' to afford SBBS the same regulatory treatment as individual sovereign bonds. However, this proposal provoked controversy among national stakeholders and was curtly rejected in the joint reform agenda announced by France and Germany in Meseberg on 19 June 2018.

## 2. FRENCH AND GERMAN PERSPECTIVES ON A EUROPEAN SAFE ASSET

The rejection of the current leading safe asset proposal in the Franco-German roadmap unveiled at Meseberg is significant on the practical grounds that France and Germany are the two largest economies in the Euro area, and that their buy-in is essential for EMU reform. Historically, Franco-German cooperation has also been viewed as the 'motor' of European integration, and other authors have previously described how the present structure of the EMU reflects a long series of compromises (to varying degrees of asymmetry) between French and German policy preferences.<sup>24</sup>

At the same time, France and Germany still represent just two members out of nineteen in the Euro area. It is relevant to note, however, that others have argued prominently for understanding the 'French' and 'German' perspectives to be emblematic of competing economic philosophies or perspectives (*Weltanschauungen*) within the Euro area as a whole,<sup>25</sup> with Ger-

<sup>22</sup> For a notable example, see the [Letter from the Chief Economist at the German Federal Ministry of Finance](#) dated 23 November 2017

<sup>23</sup> ESRB HLTf 2018, 2.

<sup>24</sup> See e.g. Brunnermeier et al, 2016; Maes, Ivo, 'On the Origins of the Franco-German EMU Controversies', National Bank of Belgium, 2002; Mourlon-Druol, Emmanuel, Rethinking Franco-German Relations: 'A Historical Perspective', Bruegel, 2017; Pisani-Ferry, Jean, 'Only One Bed for Two Dreams: A Critical Retrospective on the Debate over the Economic Governance of the Euro Area', *Journal of Common Market Studies*, 44 (2006), 823-44

<sup>25</sup> See e.g. Brunnermeier et al, 2016; Gros, Daniel, Daniela Schwarzer, Wolfgang Glomb, Lars P. Feld, Wolf Heinrich Reuter, Mustafa Yeter, et al., 'Frankreich Und Deutschland — Starke Partner Für Ein Stabiles Europa?', *Wirtschaftsdienst*, 98 (2018), 79-99; Hacker, Björn, and Cédric M. Koch, 'The Divided Eurozone: Mapping Conflicting Interests on the Reform of the Monetary Union', Friedrich-Ebert-Stiftung, 2017.

many representing the perspective of the ‘North’ (including e.g. the Netherlands, Finland, and the Baltic states) and France, at least some of the time, representing the ‘South’ (including e.g. Italy and Spain).<sup>26</sup> To the extent that this reflects real policy allegiances,<sup>27</sup> understanding the underlying disagreements that shape French and German policy preferences can therefore provide insights on broader philosophical debates on the future of the Euro area.

In order to better understand the debate between French and German perspectives on safe assets, structured research interviews were conducted between March and May of 2018 with 21 high-level (mostly technocratic) officials in both countries from key economic, fiscal, and monetary institutions, including various branches of the respective Ministries of Finance, central banks, financial regulators and debt management organisations. Interviews were also conducted with academic experts and market actors in both countries as well as with European Central Bank officials involved in the High-Level Task Force at the European Systemic Risk Board. The analysis in the following sections of this paper is based on the results of these interviews.

## 2.1 Understanding policy disagreements between France and Germany

Neither the French nor the German policymakers interviewed were particularly keen on a European safe asset proposal, but for very different reasons. However, before proceeding to a discussion of French and German perspectives on safe assets, it may help to first provide a framework for understanding the roots of the disagreements between French and German policymakers on safe assets in particular and economic policy in general.

Briefly, the disagreements between France and Germany on economic policy matters can be sorted into differences in *beliefs, values and interests*.

### Beliefs and values

Differences in beliefs and values are deeply interlinked: beliefs about how the world works, or more specifically about how the economy works, shape social values regarding what is fair or just, and vice versa. Building on previous research into French and German policy positions,<sup>28</sup> the key differences between France and Germany in terms of beliefs about the economy are summarised in Table 1.

<sup>26</sup>. This classification is necessarily a simplification. Both Brunnermeier et al. (2016) and Hacker & Koch (2017) argue that France rather plays the role of an ‘in-between’ state that exhibits both ‘North’ and ‘South’ characteristics. Nonetheless, both sets of authors place it closer to the ‘South’ point of view than to Germany in debates over EMU reform.

<sup>27</sup>. See e.g. Hacker & Koch (2017), who analyse position papers on Euro area reform submitted in advance of the Five Presidents’ Report and find that Euro area members can be sorted into two likeminded groups, one centred around Germany and the other centred around France.

<sup>28</sup>. Notably Brunnermeier et al (2016).

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DISAGREEMENTS  
BETWEEN FRANCE AND  
GERMANY ON ECONOMIC  
POLICY MATTERS  
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VALUES AND INTERESTS

TABLE 1 ■ Key differences in economic beliefs between Germany and France

	DE	FR
<b>Economic crises result principally from...</b>	Underlying problems of <i>solvency</i> due to irresponsible practices in public finance	Temporary problems of <i>liquidity</i> worsened in situations of financial instability
<b>Policy responses to economic crises should focus on...</b>	<i>Ex-ante risk reduction</i> and crisis prevention in the long-term	<i>Ex-post problem-solving</i> and crisis <i>management</i> in the short- to medium-term
<b>Policy responses should be based on the principle of...</b>	<i>Individual liability</i>	<i>Solidarity</i>
<b>The framework of the EMU should ideally be based on...</b>	States adhering to binding <i>rules</i>	States being free to exercise <i>policy discretion</i>

Both perspectives are internally coherent, but based on different economic worldviews, i.e. different understandings of how economics works. The points above show how each side sees different underlying problems, builds different crisis narratives, and prescribes different solutions that make sense within the context of their own worldview, but not necessarily within the worldview of the other. While the German narrative considers that the Euro crisis is the result of poor public finances and prescribes stricter enforcement of existing fiscal rules and market discipline to bring domestic policies in line, the French narrative considers that the Euro crisis resulted from financial instability problems aggravated by gaps in the economic governance of the Euro area, for which the logical solution is more coordination, more flexibility, and more risk-sharing at the European level. While these beliefs are obviously not held uniformly by either party – plenty of French interviewees emphasised rules and market discipline while several German interviewees emphasised solidarity – the interview results do show that each perspective is clearly dominant within its respective country.

Bridging this gap between the French and German perspectives was the aim of a group of 14 French and German economists who published a joint policy paper in early 2018 calling for reconciliation between the risk-sharing focus of France and the market discipline focus of Germany, arguing that these should be viewed as complementary rather than mutually-exclusive solutions.<sup>29</sup> One of the factors hindering a full reconciliation, however, is the fact that these worldviews are also bound up with a system of values that are coherent *within* but not necessarily *across* the different perspectives. Designing economic policies around the principle of individual liability versus solidarity is one example of a belief that also implies different values regarding what would be ‘fair’ or ‘right’ in a policy response. Additionally, differing narratives of the financial crisis as either a fundamental problem of financial instability (value-neutral) or of irresponsible spending (value-based) also show how a policy issue may be viewed as merely a technical problem to be solved in one country (France), while being viewed as a violation of deeply-held social values in the other (Germany).

29. Bénassy-Quéré, Agnès, Markus Brunnermeier, Henrik Enderlein, Emmanuel Farhi, Lars Feld, Marcel Fratzscher, et al., ‘Reconciling Risk Sharing with Market Discipline: A Constructive Approach to Euro Area Reform’, Centre for Economic Policy Research, 2018.

## Interests

In addition to beliefs and values, France and Germany also have diverging political and economic interests which are specific to the safe asset case. As the issuer of the Euro area's current *de facto* safe asset, Germany stands to lose the safe haven premium from which it currently benefits and would likely be subject to higher borrowing costs if a European-level safe asset were introduced. However, this does not necessarily mean that Germany stands to lose the most from the introduction of a European safe asset. French sovereign debt has an AA rating and is not far behind Germany in terms of the perception of its 'safety'; nonetheless, as France experienced much more volatility in its sovereign bond yields during the Euro crisis, the effects of introducing a European safe asset could potentially carry more risk for the French sovereign bond market than for the German market. On the other hand, German interviewees considered that their country would inevitably be called upon to provide a bailout or guarantee for a European safe asset if it were to fail. In short, Germany faces a number of unique economic disincentives to introduce a European safe asset, while France may have reason to harbour some reservations related to the uncertain effects of the asset on national sovereign bond markets.

## 2.2 Principle areas of disagreement

The interview results are clear in showing that French and German policymakers tend to view European safe asset proposals through the 'lens' of either financial stabilisation or market discipline, and that this lens shapes how policymakers in each country perceive and assess the problems, solutions, costs, and benefits. The following sections examine these differences in detail, before discussing how these worldviews come together in practice.

### Engagement with safe asset proposals

French and German policymakers engage with safe asset proposals differently, according to their values and interests. This is most evident in the extent to which institutions have taken sides in the debate: while almost all of the French interviewees emphasised that their institution did not have an official position on the topic, none of the German interviewees claimed the same, with some explicitly stating that their institution was not in favour of the most recent proposals. Interviewees in both countries considered that **the German position on safe assets was firmer than the French position.**

Differences also exist in the intensity with which policymakers reported working on safe asset proposals and the weight that they assigned to the topic. In Germany, the recent SBBS proposals were referred to as a 'fundamental' issue and had reportedly been subject to intense discussion at a very high level. In France, however, while the issue was clearly being followed and there had been high-level discussion, none of the officials interviewed characterised safe assets as a critical issue, with most stressing that their attention was focused on other reform efforts.

### Perceived costs and benefits

Policymakers in France and Germany differ not just in the types of costs and benefits they associate with a European safe asset, but also in how they assess the costs and benefits, reflecting the key elements of their respective worldviews – namely, a focus on financial stability vs. market discipline – and the extent to which they see the issues as technical/value-neutral or as more fundamental.



FRENCH AND GERMAN POLICYMAKERS TEND TO VIEW EUROPEAN SAFE ASSET PROPOSALS THROUGH THE 'LENS' OF EITHER FINANCIAL STABILISATION OR MARKET DISCIPLINE

*In France*

French policymakers considered costs and benefits primarily with respect to the effectiveness of the proposals. There was no unique ‘French perspective’ on safe assets, although French interviewees tended to adopt one of two main approaches:

- A *technical* approach, focusing on the technical merits of safe asset proposals and weighing possible benefits against costs and risks; or
- A *problem-focused* approach, focusing on the policy rationale for a European-level safe asset and questioning whether it was the best tool to solve the problems at hand.

Interviewees taking the technical approach generated a long list of potential benefits, but an equally long list of potential costs and risks, with a focus on the theme of financial stability (Table 2). They tended to be open to and interested in a European safe asset but questioned how well the proposals would ‘work’ in a technical sense, especially in a crisis scenario. Their key concerns were that the asset might have a distortionary effect on national bond markets (including a risk of increased fragmentation), that it might not be sufficiently liquid, and that there might be a lack of market interest in the new asset.

**TABLE 2 – Benefits and costs/risks of a European safe asset as indicated by French interviewees**

BENEFITS	COSTS OR RISKS
<ul style="list-style-type: none"> <li>• Breaking the bank-sovereign nexus by diluting the domestic bias and breaking the doom loop</li> <li>• Avoiding destabilising capital flows by limiting effects from the flight to safety</li> <li>• Increasing the supply of Euro-denominated safe assets (for collateral etc.)</li> <li>• Improving transmission of monetary policy (easier to implement quantitative easing)</li> <li>• Building a crisis-resilient framework for economic governance in the future</li> </ul>	<ul style="list-style-type: none"> <li>• Negative or uncertain effects on national bond markets (e.g. a reduction in liquidity)</li> <li>• Increased fragmentation in national bond markets (e.g. by crowding out periphery countries not included in the safe asset)</li> <li>• Illiquidity of the ‘safe’ asset (especially in a new market)</li> <li>• Lack of market interest (i.e. an SBBS might be seen as too complex or not safe enough)</li> <li>• Concerns regarding effects on market discipline for issuing governments</li> </ul>

The French interviewees subscribing to the ‘problem-focused’ perspective, in contrast, began from a more sceptical basis by critically examining the safe asset concept and its policy rationale at the European level. Interviewees in this group considered that increasing financial stability was the primary problem that a European safe asset aimed to solve and questioned whether it would be the best tool to accomplish that objective, citing some of the same risks identified by the first group and pointing out that there were many other proposals (e.g. a Euro area budget, bank concentration charges) that could achieve similar results with fewer risks and costs. These interviewees also questioned the political feasibility of a European safe asset and tended to see pooling sovereign debt in any form as an extreme political step which would require justification and evidence that in their view was currently insufficient.

*In Germany*

German policymakers were more uniform in their assessment of the costs and benefits. While some interviewees considered that there could be benefits from a European safe asset in theory – such as breaking the bank-sovereign nexus, preventing destabilising capital flows, lowering financing costs in the Euro area, and possibly lowering the cost of sovereign debt restructuring (the last of which was not noted by any of the French interviewees) – the German perspective tended to focus almost exclusively on the long-run costs and risks.

Only a couple of interviewees mentioned in passing that a European safe asset would increase borrowing costs for Germany. The dominant concern among German policymakers instead related to moral hazard and adverse incentive problems, i.e. that a European safe asset would reduce market discipline, encourage countries to borrow more irresponsibly at a lower cost, and transfer greater credit risk to the European level, thereby increasing rather than decreasing Euro area financial instability and inevitably requiring a bailout. In this context, almost none of the German interviewees believed that the claim of SBBS to avoid joint liability via financial engineering was credible. Most considered that SBBS would carry an implicit guarantee of European or national support, a perception that would only be strengthened if the Commission followed through with its plans to adapt European banking regulations to give preferential treatment to SBBS.

In sum, **policymakers in France focused on the relative effectiveness of a safe asset in addressing financial stability, while the discussion in Germany focused almost exclusively on costs and risks associated with moral hazard or adverse incentive problems.** Where financial stability concerns were discussed in Germany, these tended to be viewed through the lens of moral hazard, with interviewees arguing that safe asset proposals provided the wrong incentives and were likely to decrease financial stability in the long run. In both countries, significant doubts were expressed about whether an SBBS would qualify as a truly 'safe' (i.e. crisis-resistant) asset, although in France this fear tended to relate to the technical properties of the asset whereas in Germany this fear was more directly linked to irresponsible borrowing.

## Perspectives on various safe asset proposals

*In France*

The positions of French policymakers towards a European safe asset have changed considerably over time, depending on the policy trade-offs present at any given point. Interviewees considered that Eurobond-type proposals were quite popular in France at a theoretical level early on in the Euro crisis, but fell out of vogue around 2012 with the introduction of Outright Monetary Transactions (OMT) by the ECB and the establishment of the ESM, which removed much of the pressure on bond markets and consequently made safe asset proposals less attractive to policymakers. While there has been interest in the new SBBS proposals, French policymakers remain sceptical of the net benefits and do not consider SBBS to be a 'game-changer' or 'silver bullet' for the problems faced by the Euro area, especially given the other policy options available.

The question of joint liability proved highly divisive in France, with some policymakers identifying it as the key question in the safe asset debate. Some remained strongly in favour of a Eurobond-type safe asset with joint liability, assuming that the appropriate fiscal accountability mechanisms were in place, while others were just as strongly opposed, arguing that joint liability was out of scope in the present political climate. The divisiveness of the joint liability

question spilled over into a particular criticism of SBBS made by some French interviewees, namely that it appeared custom-designed to avoid fundamental and inherently political choices about the future of the Euro area. In this light, some interviewees argued that SBBS were disingenuous, and that the question of joint liability should be settled explicitly and politically rather than being avoided or hidden through financial engineering.

#### *In Germany*

Attitudes toward safe asset proposals in Germany were more uniform and consistent over time than in France. Interviewees emphasised that all of the proposals suffered from similar moral hazard and adverse incentive problems to some degree, and that their perspective on these proposals had not changed over time (an observation that was confirmed by the French interviewees).

Most German interviewees rejected joint liability outright on the grounds that this would be incompatible with German and European law, and would impose adverse incentives for countries to borrow irresponsibly. Given their concerns over the joint liability question, policymakers were not just opposed to the original Eurobond-type proposals, but were also sceptical of SBBS, which they viewed as carrying an implicit guarantee and therefore *de facto* joint liability. A common criticism therefore referred to SBBS as ‘Eurobonds through the backdoor’ or ‘backdoor mutualisation’. Like their French counterparts, some German interviewees considered that SBBS were simply not transparent enough or targeted enough for what they were trying to accomplish.

**Policymakers in both countries therefore emphasised that the design of a European safe asset was not just a technical question, but reflected decisions that were inherently political, with joint liability singled out as the key question to be resolved.**

### Conditions and forward-looking perspectives

When asked to list conditions under which a safe asset proposal would be acceptable, French responses were again more heterogeneous than those in Germany, to the extent that some French interviewees disagreed on fundamental questions or proposed conflicting conditions. Interviewees in Germany tended not to contradict each other but instead showed a coherent focus on avoiding adverse incentives. **Key points of contention related to the level of joint liability required as well as the appropriate regulatory treatment for the European-level asset.**

#### *In France*

French policymakers focused on conditions around the effectiveness of the proposal, ensuring that the expected benefits would be achieved while minimising possible costs and risks.

On the question of *joint liability* and *debt mutualisation*, policymakers were torn. Some considered that a common asset without joint liability would lack market credibility, while others argued that joint liability would never be politically acceptable.

On the question of *regulatory treatment*, French policymakers were nearly unanimous that the safe asset would need to benefit from the same zero risk weight as national bonds to be viable on the market. However, there was disagreement as to whether this regulatory privileging of the safe asset would need to be accompanied by removing the zero risk weight for national bonds, which some perceived to be necessary and others perceived to be politically out of bounds.

French policymakers agreed that any safe asset proposal would need to maintain market discipline. A key concern in France was also the need to minimise distortion of national bond markets, and in particular to ensure continued liquidity in primary government bond markets, implying that a European safe asset should not significantly raise French borrowing costs. Finally, French policymakers expressed that they needed to be convinced that a safe asset proposal would actually solve the problems they face, and that there would not be a simpler or more politically feasible solution available that could achieve the same results.

#### *In Germany*

German policymakers placed significant emphasis on avoiding moral hazard and ensuring that any proposal promoted the correct incentives. Accordingly:

On the question of *joint liability* and *debt mutualisation*, no debt mutualisation was considered a basic condition of any proposal. Concerning SBBS in particular, most interviewees were concerned about not giving the appearance of an explicit or implicit guarantee. However, some interviewees who were more sympathetic to the concept framed the discussion in terms of balancing financial stability objectives and lower financing costs for Euro area countries on the one side with fiscal responsibility and proper incentives on the other. They emphasised that this balance would need to be built into the design of a safe asset – e.g. through a two-tiered structure with both a safe and non-safe component (e.g. Blue/Red Bonds or EJBies/ESBies) to preserve market signals.

On the question of *regulatory treatment*, the notion of regulatory privilege was a key source of controversy. Almost all German policymakers interviewed were in favour of removing the zero risk weight for national debt, which they considered to be out of line with the economic reality. However, there was disagreement as to whether the European safe asset should receive the privilege of a zero risk weight. While a limited number of interviewees considered that the senior tranche of a SBBS could be granted a zero risk weight if it were truly safe, most considered this inappropriate. They argued that a SBBS was not a 'safe' asset or that giving it regulatory privilege (especially if the zero risk weight were removed for national bonds) would be interpreted by the market as an implicit European bailout guarantee.

Some German policymakers also argued that access to the European safe asset by individual Member States would have to be limited and contingent on the observation of EU fiscal rules. Given these limitations, some interviewees commented that only a private, market-led synthetic bond like an SBBS without any regulatory privilege would be acceptable from their perspective.

**Neither French nor German policymakers were particularly optimistic about the possibility of introducing a European safe asset in the near future;** they were also sceptical that such an asset, if introduced, could achieve a high enough trading volume to be effective. Policymakers in both countries pointed towards other Euro area reform proposals as more fruitful areas for cooperation, although this point given more weight in France than in Germany. Policymakers in both countries considered the current situation in the Euro area to be unsustainable, but disagreed about the next steps, with French policymakers tending to emphasise the need for more stabilisation instruments at the European level and German policymakers tending to emphasise the need for more credible fiscal rules.

## 2.3 Policy cooperation in practice

Given the differences in economic worldviews, it may be hard to picture how the French and German perspectives described above come together in practice – and yet they do. France and Germany cooperate on Euro area economic policy not just in multilateral European forums such as the Eurogroup, the ESRB or the Economic and Financial Affairs Council (ECOFIN), but also in extensive bilateral dialogue through both formal and informal channels. **Policymakers in both countries had a very positive perception of this bilateral cooperation, and emphasised that France and Germany usually try to arrive at a common position on Euro area governance topics.** While disagreements often arise between the parties, it was noted that this was not due to a lack of understanding of the other's position, but rather to **disagreements over the nature of the problem.**

This observation emerges clearly in the safe asset case. Despite reporting that most cooperation on this topic had come through multilateral rather than bilateral channels, policymakers in France and Germany both had a very accurate understanding of the position, reasoning, and main points of contention on the 'other side'. Interviewees were often quick to point out that the French perspective emphasised financial stabilisation while the German perspective emphasised market discipline, or that French policymakers were more open to safe asset proposals yet unconvinced by the merits while German policymakers tended to be more straightforwardly opposed. Despite being cognizant of these differences, however, interviewees on both sides concluded that the parties were not so far apart in terms of the end result – i.e., that neither was particularly enthusiastic about a European-level safe asset.

This seeming agreement on the end result may not be as neutral as it appears. **There is some evidence to suggest that there has been policy convergence away from a safe asset, with France being pulled closer towards the German point of view.** This point was made explicitly on the German side, with one interviewee considering that their French counterparts had become more sceptical towards SBBS over time as a result of German efforts by the German side to convince them of problems with the proposal. Evidence for policy convergence towards the German point of view was also implicit in the choice of argumentation: French interviewees occasionally cited arguments made to them by their German counterparts as reasons for why certain proposals or policy options would be feasible or not; conversely, while German interviewees were all aware of the arguments made by their French colleagues, they did not cite these arguments as grounds for their own assessments.

## CONCLUSION

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France and Germany clearly rejected SBBS in the joint roadmap for Euro area reform presented at Meseberg in June 2018. Nevertheless, this apparent agreement masks much deeper divisions in economic worldviews which have shaped the debate over Euro area reform up to this point and which will continue to do so in the foreseeable future. An inherent difficulty in overcoming these divisions is that each side sees the problems differently – or rather, sees different problems – and proposes solutions that make sense within their perspective, but which may not make sense within the other. Further complicating the reconciliation between these worldviews is the fact that these perspectives are also bound up in strongly-held values as well as specific economic and political interests.

This is well-illustrated in the case of a European safe asset and particularly with respect to the SBBS proposal, which is assessed here from two different points of view. In France, the debate over SBBS is varied, technical, and focused on determining whether SBBS could be effective and whether it is the right tool to improve financial stability in the Euro area given the present policy trade-offs. In Germany, the assessment is more uniform, more straightforward, more consistent over time, and closely linked with values: German policymakers consider that SBBS under current conditions would be a moral hazard risk, do not believe it would be crisis-resistant in the long run, and suspect that such an asset would require an eventual bailout. **The difference between the two countries could be summarised by stating that while most French policymakers are not opposed to a European safe asset in principle, most German policymakers are opposed to a European safe asset almost entirely in principle.** This may be one reason for why there appears to have been French convergence towards the German position but not vice versa.

Despite the rejection by France and Germany at Meseberg, the topic of a common European safe asset is unlikely to disappear from discussions over Euro area reform. Safe asset proposals as a whole continue to attract interest from policymakers and have strong proponents who argue that a common safe asset is a necessary or inevitable piece of the EMU. The main points of contention that remain to be resolved for the issue to move forward, at least as far as the debate in France and Germany illustrates, are the degree of joint liability that would be acceptable or necessary for the proposal to work, the regulatory treatment of the safe asset (tied up with the issue of the regulatory treatment of sovereign exposures in general), and the design of the safe asset to ensure that market discipline is preserved. However, given the observed scepticism in the two largest economies of the Euro area, it would be difficult for a European safe asset to secure a high place on the reform agenda at present.

## ON THE SAME TOPIC

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- Prof. Dr. Henrik Enderlein and Lucas Guttenberg, “Why Meseberg matters – A short explainer”, Blog Post, Jacques Delors Institut, 22 June 2018.
- Lucas Guttenberg and Dr. Johannes Hemker, “A fiscal instrument for the euro area: No escape from politics”, Policy Paper, Jacques Delors Institut, 26 March 2018.
- Jörg Haas, “Sovereign debt: Do we need an EU solution?”, Europa Briefing, Jacques Delors Institut, 22 November 2017.
- Prof. Dr. Henrik Enderlein, Dr. Enrico Letta, and Aart de Geus, “Seizing the moment for euro area reform”, Policy Paper, Jacques Delors Institut, 29 May 2017.
- Prof. Dr. Henrik Enderlein and Paul Berenberg-Gossler, “Financial market fragmentation in the euro area”, Policy Paper, Jacques Delors Institut, 17 November 2016.
- Prof. Dr. Henrik Enderlein, Jörg Haas, and Dr. Katharina Gnath, “Germany and the stability of the EMU”, Jacques Delors Institut, 25 January 2016.

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