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# From Friends to Enemies? The Euro as a Cause of New Nationalism

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# From Friends to Enemies? The Euro as a Cause of New Nationalism

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## Abstract

It is often disregarded that the euro is first of all a public good based on common institutions such the European Central Bank, the Governing Council and a network for executing transactions etc. Establishing a public good is fundamentally different from trade in private goods. A public good needs a coordinated action. All participants have to join their efforts towards the same goal. The more one individual contributes to the public good, the less has to be contributed by the other individuals which is an invitation to free riding. This is an inherent weakness of a public good as compared to private goods. If the partners are badly chosen in the beginning or if they shirk on their contribution, the public good is not produced or it is badly produced and ends in a crisis. No repair is possible. The venture has to be started anew.

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## I. Alarming Trends

The author is thankful to Monika Poettinger and Antonio Varsori for having organized the conference on *"Economic crisis and New Nationalisms".* It is indeed alarming to observe how national egoisms are growing in Europe, while old friendships seem to disappear. Will that be the future of the European peoples? Will yesterday's trust turn into today's distrust? Will yesterday's friends become tomorrow's enemies? The civil society is alarmed, but the public remains passive.

The concerns of the crisis are targeted to the euro. The European leaders – the Council, the Commission and the European Central Bank – have been trying to maintain the euro as a unifying tie around the European peoples for more than five years, but the euro makes no sign of becoming self-sustainable, instead, it depends on a permanent flow of fiscal and monetary transfers from the Northern to the Southern member states. The mixed evaluations of the euro policies by the press compiled by Monika Poettinger (2014) and the warnings of the historian Antonio Varsori (2014) both in this volume underline the worry which is widespread among all Europeans.

## II. A Theory of the Euro Crisis

The new nationalisms are a riddle. But the public discussion does not contribute very much to solving the problem. The more the civil society condemns the new nationalisms, the more they grow in the underneath. Therefore it has to be asked: Does the civil society ask the right questions? Could it be that the problem perceived is upside down and has to be placed on its feet before an analysis can start? Are the new nationalisms a symptom rather than the cause of the crisis? In order to solve the riddle a theory is required explaining the new nationalisms endogenously. Why did the new nationalisms emerge now and not earlier? The hypothesis proposed in this paper is that the euro is the cause of the crisis. New nationalisms are not growing despite of the euro, but because of the euro. This hypothesis may be uneasy for all those who believe in the common project of the euro. They may be disappointed that the goals in which they believe are evaporating. But after all, not the euro, but the friendship among the people of Europe is the goal. The euro is a means, not the end.

Figure 1 summarizes the history of the European Union since its beginning in 1958. It shows that the popularity of the European Union increased during the first half of its existence from 1958 to about 1992 and then declined constantly up to present.

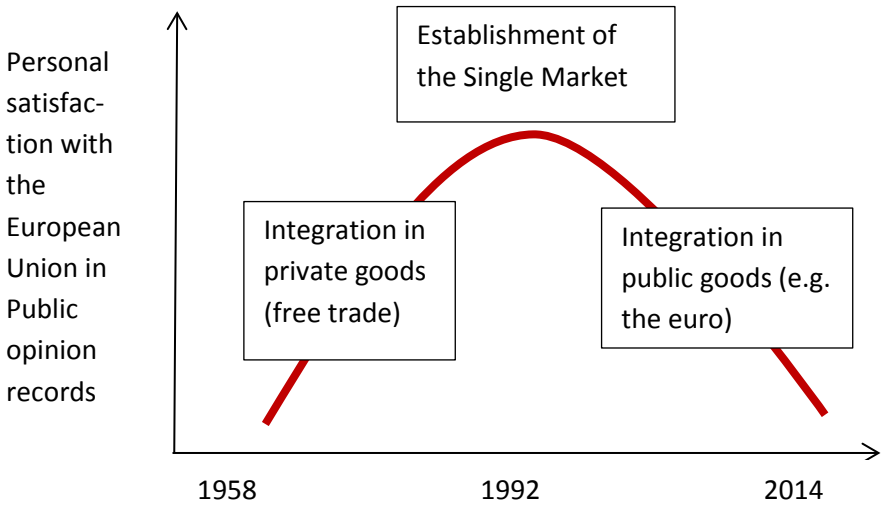
The first period from 1958 to about 1992 may be characterized as the period of European *integration by trade in private goods.* It ended with the establishment of the free internal market for goods, services, labour and capital in different currencies in 1992.

Since 1992 the focus of the European Union has shifted from promoting gains of trade in private goods towards obtaining gains from *integration by jointly sharing public goods*. The Common Foreign and Security Policy (CFSP) and the Common

Security and Defense Policy (CSDP) have been established. But above all, the euro has to be mentioned because it is the most important public good of the Union.

The euro needs two steps to work. First a set of common institutions (a central bank, a number of regulations on a common monetary policy, an enforcement system and a network for executing transactions) has to be established and then trade takes place within this institution. The institution of the euro is a public good shared by all individuals. Trade in the euro is a private good. The principle of self-interest applies only to the second step.

Establishing the public good is fundamentally different from trade in private goods. A public good needs a coordinated action. All participants have to join their efforts towards the same goal. This does not happen by the "invisible hand". For the more one individual contributes to the public good, the less has to be contributed by the other individuals. (With private goods, in comparison, trade is generated if individuals work in different directions, if they specialize and then proceed to market exchange.) A public good, however, needs a prior binding agreement among the participants on who contributes how much. If the partners are badly chosen or if they shirk on their contribution, the public good is not produced or it is badly produced and ends in a crisis. All participants are disappointed and quarrel on who is guilty. So the new nationalisms are generated. This is the central problem of the euro crisis.




Source: Euractiv, several issues

## III. Oil and Vinegar

A simple story may help to understand the problem of the euro as a public good. Since antiquity grocers have used Oil for canning olives and Vinegar for canning cucumbers. The grocers know that they may add Oil to Oil and Vinegar to Vinegar at constant returns to scale, but that they must not add Oil to Vinegar nor Vinegar to

Oil because the resulting mix is useful neither for canning olives nor for canning cucumbers. The mix exhibits strongly decreasing returns to scale down to zero returns compared to Oil and Vinegar in separation. Therefore grocers carefully observe this rule, and so should policy makers when they plan to establish a monetary union. The success or failure of a monetary union depends on its founding members. Countries which are as Oil and Vinegar are not good partners for a monetary union.

This view has been, however, criticized by the adherents of the "Mutual-Stimulation-Thesis" who say that Oil and Vinegar should be deliberately mixed because their differences stimulate each other. So Oil and Vinegar are deliberately mixed to generate a salad dressing. But a closer observation reveals that Oil and Vinegar do not join to an inseparable solution such as salt and water which can only be separated by adding a substantial amount of energy. Oil and Vinegar remain inimical as if they were gladiators in a Roman arena to fight or if the crisis is the purpose of pouring Oil and Vinegar together. After a while the spectacle is over and Oil and Vinegar separate and cluster as useless substances at different places in bottom of the salad bowl. Therefore the Mutual-Stimulation-Thesis is not constructive unless one intends to generate a crisis.

But what should the policy maker do if he has the task to establish a monetary union, but has only Oil and Vinegar as ingredients? In this case he may remember that he learnt in chemistry in school that the incompatibility between Oil and Vinegar may be overcome if an emulsifying agent is added and oil and vinegar generate a new product such as a mayonnaise or a vinaigrette. In the case of a mayonnaise, lecithin – contained in the yolk of the egg – acts as an emulsifying agent. Lecithin dissolves in oil and in water and with these properties it can overcome the interface tension between the two phases. However, emulsions stabilized by an emulsifying agent may nevertheless become unstable if the agent is not deliberately chosen. Then, the emulsions are exposed to flocculation, creaming, coalescence, or Ostwald ripening that alter the internal structure and often worsen their properties.[2] Therefore, it cannot be taken for granted that Oil and Vinegar become compatible. It depends on the capacity of the emulsifying agent.

The European Monetary Union comes very close to a mix of Oil and Vinegar. Some of its participating governments are market oriented and some are redistributive. Therefore the latter exert negative externalities on the former, and the Monetary Union risks to end in a crisis unless the Maastricht Treaty appears as an emulsifying agent unifying Oil and Vinegar. The power of the emulsifying agent must be very strong. Its "lecithine" has to unite the market goals of the Oil country with redistribution goals in the Vinegar country. A Maastricht Treaty which is able to generate an emulsion out of allocation and redistribution has not yet been invented. Therefore a crisis seems unavoidable.

[2] From private correspondence with Prof. Rudolf Blankart.

What can be learnt from this parable? Countries with heterogeneous political systems should not join to a monetary union. A redistributive (Vinegar) system is not compatible with a market oriented (Oil) system. A Treaty as the Maastricht Treaty is not a strong enough as an emulsifying agent to neutralize the externalities generated by Oil and Vinegar. For nobody has the power to enforce the Treaty.

Paolo Savona writes in his "letter to German friends" (Savona 2014 in this volume, p. 50): "I would like to urge you to show greater commitment to prevent another tragedy in Europe".

My answer is drawn from natural sciences, which teach us that the right setting at the start is necessary for a good outcome. A tragedy cannot be resolved by improving an undesired outcome ex post. Too much salt in a soup cannot be compensated by adding more sugar. It is too late. Preventing a tragedy means to set things right before the process starts.

The reader will ask: How could the founders of the euro overlook this basic condition? How was it possible to slip in this fallacy? The euro negotiators have discussed ten years (from the summit of Hanover in 1988 to the irreversible fixing of the national exchange rates of 31 December 1998) to make the best of all treaties. Indeed though the way to the Treaty was carefully drafted the negotiators forgot to discuss how to enforce it once it is in force. Therefore Vinegar was not banned out of the euro. It was still there with its destroying power when the euro started.

In the retrospect one may ask: Why has nobody warned the politicians? Where were the professional economists who should have known better? The fact is that economists did not remain silent. In February 1998 155 German economics professors (including the author of this paper) launched an open petition to the German government entitled: "The euro comes too early." They wanted to say that the euro project needs more rethinking (Frankfurter Allgemeine Zeitung, 9 February 1998). The petitioners' opinion was shared by a large part of their academic community in Germany and worldwide. The most prominent support was given by Milton Friedman whose opinion has been recorded in 1999:

*"I am very negative about the euro and I am very doubtful about how it will work out… What most troubles me … is that members of the euro have thrown away the key [no revision clause]. Once the euro physically replaces the separate currencies, how in the world do you get out? It's a major crisis. As a result, I would strongly agree … that the euro should be abandoned before January 1, 2002. At the same time, the odds are very great that it will not be abandoned. The defects of the euro will take some time to show up; nothing happens very rapidly in this area. There are fewer than three years to go. Even if difficulties deriving from the euro occur in those three years, the political system is unlikely to react quickly enough to end the euro. As a result, I think it would be very desirable for some systematic thought to be given to devising some way to get out of the straitjacket of the euro after 2002." (Martino 2008)*

Once it is understood that the euro is the result of a process, one arrives at the conclusion that it is irreparable. If we want to restore the friendship among the European people as it was until the appearance of the euro it does not make sense to repair the ill designed euro. For as long as Vinegar cannot be eliminated as a player the euro remains a permanently defective institution.

It is also wrong to say that an exit out of the euro is too expensive. Most politicians agree that, could they step back to the year 1990 and had they the knowledge of 2014, they would vote against the euro because they expect a larger rate of growth of GDP without the euro than with the euro (Krämer 2014). If their calculus was right for 1990 it is likely to be right also right today, only that we have to account for the transitory switching costs. We can conclude: Whatever the switching costs are, there is a point in the future where the GDP without the euro (including transitory switching costs) crosses thedevelopment path of the GDP with the euro from below and then permanently exceeds the GDP with the euro ceteris paribus. In this case, the present value of all future GDPs is larger without the euro than with the euro under the same rate of interest.

Thus, the task of the responsible policy makers in Brussels and Frankfurt should be to develop alternative ways of a least costs exit instead of exclusively searching for ways to save the euro. It is indeed paradoxical to see how much money is invested in research that is exclusively directed to repair the failed construction of the euro, while practically no public money is directed into Milton Friedman's problem of how to get out of it. Some private researchers propose that leaving the euro needs the same procedure as entering the euro: parallel currencies and slowly adjusting exchange rates (Die Parallelwährung 2012). It is not claimed that parallel currencies are the best and unique way of an exit. It is rather suggested that policy makers – Council, Commission, Member State Governments and ECB – should stop to negate the exit question. Improvements can only be come from comparative economic studies of all alternatives, not from their one-sided exclusion. Therefore the great philosopher Karl Popper warns that no issue must be a political Tabou in an Open Society (Popper 1945).

## IV. Learning from History: The Emergence of the German and French National Fiscal Systems

The central argument of this paper is a theoretical one. It is argued that Oil and Vinegar countries cannot coexist in a monetary union because they exert mutual externalities leading to a permanent crisis with high social costs, inimical excesses and political unrest. Oil and Vinegar continuously destruct each other.

In this section (IV) Oil and Vinegar will be identified in history. The histories of Germany and France are shown to come close to Oil and Vinegar, but not from the beginning, only since the French revolution of 1789. Section V describes the destinies

of earlier monetary unions from the Latin Monetary Union of 1869 up to European Monetary System (EMS) of the 1980ies and 1990ies. Section VI explains the political reasons of the euro, the Maastricht Treaty, the subsequent destruction of the Maastricht Treaty and the emergence of the status quo. Section VII proposes the conclusions of the paper and the consequences for the euro.

Looking back to the Middle Ages, there existed no difference in the fiscal regimes of Germany and France. In fact, Germany and France did not exist as nations. Instead the region North of the Alps was split in many small domains of regional and local vassals who protected the peasants in their domain from attacks by roaming and robbing hordes of Normans and Huns. In return for protection the peasants provided labour services to the vassals. The vassals, in order to protect their domain from larger attacks, were reinsured by their seigneurs who could mobilize additional vassals for support (Volckart 2002).

This tripartite system of seigneurs, vassals and peasants functioned from 700 until about 1500. As literacy, contract and money slowly reappeared after about the year 1000 the seigneurs begun to arrange themselves with the vassals at the costs of the peasants who became assessable for the seigneurs whereas the vassals became functionless paladins at the courts of their seigneurs. So the appearance of the seigneurial system survived beyond the Middle Ages.

A real break, however, came with the French Revolution of 1789, when the French National assembly formally abolished the seigneurial system on 4 und 5 August 1789 and replaced its taxes by a unitary national tax system which financed the unitary central national budget. The idea was that centralization should make the budget of public expenditures and taxes more rational. The contrary was the case. The central budget of France became the nation's common pool which was never sufficient to fulfill the demands of all interest groups. Therefore, a permanent shortage of means was built in the French system. Increasingly more resources were needed from outside sources, from secularized Church property, from money creation and from plundering in wars. So France became a "Vinegar State" dependent of attracting off-budget resources from wherever it was possible. As inflation played an important role, the French came out of the revolutionary wars with a smaller public debt than England.

The French system of government was admired for its Cartesian logic by the political leaders of the emerging national states of 19$^{th}$ century Europe. They enthusiastically followed the French example and established centralized Vinegar states, in particular in Italy, Spain, Portugal and Greece. Only Germany was an exception. Germany was unified in 1871 as a Federal State whose subcentral state governments had and still have to pay for their budget by own means. So Germany played and plays Oil, whereas France and the other States play Vinegar.

Still, however, French Vinegar did not come into conflict with German Oil. For both countries were sovereign and financially independent states. Germany and France

had trade, but they operated on their own costs. “They went Dutch.” Each government had to break even. A mutual bailout was out of question.

## V. The Forerunners of the Euro

The euro is not a unique historical example of a monetary union in Europe. There were many previous monetary unions allowing politicians of today to learn from history. In all cases it can be seen that monetary unions collapsed if politicians tried to mix Oil countries with Vinegar countries.

### V.1 The Latin Monetary Union

In the 19th century the Latin Monetary Union brought Europe very close to a true monetary Union had not Vinegar interfered and destroyed the union. In these times cross-border flows of gold or silver regularly compensated trade balance disequilibria. There was no escape from this logic. All countries had to play Oil. In France the idea emerged that an international standardization of gold and silver coins would facilitate these transactions and could in fact establish a monetary union. In 1865 France, Belgium, Italy, and Switzerland agreed to mint their national currencies in a standard of 4.5 grams of silver or 0.290322 grams of gold (a ratio of 15.5 to 1) and make them freely interchangeable. A monetary union was established. But the drafters forgot Vinegar. Vinegar’s first attack came from the fixed price ratio between gold and silver. As the international free market price of gold increased compared to the international free market price of silver towards the end of the century, speculators sold silver to the union member states in exchange of gold at the officially fixed Union exchange rate of 15.5 to 1. Thus, countries like Switzerland had to accept large amounts of silver and lost gold until the international market prices recovered. A second and ultimate attack against the Latin Monetary Union came from paper money which begun to circulate towards the end of the century. Now, vinegar governments could simply print money and refuse or postpone its conversion into gold or silver. This attack was no more sustained by the Latin Monetary Union. It collapsed in 1926.

The conclusions are obvious: If in a monetary union one or several countries permanently play Vinegar by printing paper money while the other countries play Oil, the system reaches a point where it cannot be repaired and collapses.

### V.2 The System of Bretton Woods

But the dream of a worldwide monetary union remained awake despite of the repercussions of World War II. In 1944 the world monetary system of Bretton Woods has been established. It required each participant government to maintain a fixed exchange rate of its currency to the US Dollar which was priced at 35 Dollars per ounce of gold. So, Bretton Woods was close to a monetary union. If a government decided to finance its budget by money creation (Vinegar) it soon had not enough

Dollars to maintain the fixed exchange rate to the US Dollar and was therefore constrained to return to a balanced budget policy. Hence, each country had an incentive to practice budgetary discipline and so to play Oil.

This rule was, however, not binding for one country: the United States. If the US decided to go off balanced budget policy, they could simply print Dollars without consequences. In particular after they gave up their promise to convert dollars into gold at the fixed rate of 35 Dollars per ounce of gold in the 1960s the US could play Vinegar without consequences while the other countries still had to play Oil. In fact the other countries bore the costs of the US fiscal deficit. In 1973 the participant countries of Bretton Woods refused to buy any longer dollars at the statutory exchange rate and hence caused the collapse of the system.

Again, the conclusion is that a monetary system cannot survive when one country permanently plays Vinegar and generates externalities which are shifted on the Oil countries. Such a monetary system cannot be repaired and it is determined to collapse. In fact, the collapse is the best remedy because it facilitates to adopt an alternative system as the existing system is irreparable.

## V.3 The European Currency Snake

In 1972 when the Bretton Woods system was already in disarray the heads of the EU central banks decided to establish a system of limited exchange rate fluctuations between their currencies and the US Dollar illustrated by a “snake creeping in the tunnel” (of Bretton Woods). After the ultimate collapse of Bretton Woods in 1973 the snake crept out of the tunnel. It was decided among the European governments that each central bank had to buy or sell its own currency in order to maintain the exchange rate within a band of +/-2,5%.

In the so called “Werner Plan” the EU governments opened further talks on harmonizing the fiscal policies underlying their common exchange rates. However, no binding decision has been reached. Therefore, the Werner Plan could not work. The policy makers missed to make the underlying fiscal systems compatible.

Germany practiced a fiscal breakeven, whereas France did not. Therefore, Germany was able to maintain its exchange rate and to stay in the snake, while France and most other countries have lost foreign reserves and dropped out. Eventually only Germany, the Benelux, Denmark and Norway were able to keep their exchange rates within the snake, while all other member states dropped out.

## V.4 The European Monetary System (EMS)

The European currency snake was amended by a three months monetary assistance mechanism of 1.4 bn. European Currency

Accounting Units (later ECU) (Bernholz 1998: 792). This help was enough to cope with frictions on the foreign exchange market, but insufficient to absorb asymmetries as those between the German and French fiscal systems.

Therefore, President Giscard d'Estaing came to Germany in 1978 in order to convince Chancellor Helmut Schmidt to extend the existing currency assistance program open-endedly in anticipation of a future monetary union whose central bank should be equipped with enough money to balance all member states' fiscal accounts comparably to the Banque de France which balanced the fiscal accounts on the French national level. This conception of a central bank was initiated by the Belgian-American economist Robert Triffin (1960) who, as an advisor to the European Commission in the 1960s, pleaded for a European reserve pool to support national Governments' budgets. Germany's central bankers, in contrast, pointed to the Bundesbank law which strictly prohibited such support programs as the Bundesbank had to maintain price stability in the first place. This view of a central bank was, however, completely alien to French politicians who thought that a central bank without the capability of balancing budgets is useless. The Bundesbank again rejected this view.

After some negotiations the German and French governments agreed jointly with the other member state governments on a financial support program for countries which had difficulties in maintaining exchange rate stability. The resulting European Monetary System (EMS) should consist of the following four stages:

a) First stage: A short term repayable financial support program as known from the European Currency Snake extended to 11 bn. ECU.
b) Second stage: A medium term repayable financial support program of another 11 bn. ECU.
c) Third stage: A realignment of the exchange rates should take place in case of a fundamental exchange rate disequilibrium.
d) Fourth stage: An automatic exit occurs if the first three options do not succeed.

The EMS was a good compromise to unite Oil and Vinegar countries. Germany caused no problem with its exchange rate because it had balanced budgets. France was not constrained to abandon its fiscal system inherited from the past, but was nevertheless warned not to overdraw it. It could count on monetary support, but it was made clear that support was limited.

It is often said that the currency crisis of 1992-93 was a crisis of the EMS. However, this view is not correct. The crisis occurred because the UK and Italy who were hit by balance of payment deficits resisted against realignments according to the third stage and therefore had to leave according to stage four. France was in a similar situation, but it achieved a broadening of the exchange rate bands to +/-15% and therefore escaped from a realignment. All in all, the

EMS was a success. The exchange rate volatility has declined within the EMS since the Sterling crisis of 1993 as shown in Blankart (2013).

## VI. The Political Reasons of the Euro

The decision to abandon the EMS and to go towards the euro was purely political. No economic need required to give up the EMS. The political problem was the dominance of the German Bundesbank. If n-1 countries of n participant countries of a fixed exchange rate union intervene to maintain their exchange rates at the agreed level, the exchange rate of the n-th country is also fixed regardless of its monetary policy. The n-th currency will be the reserve currency. Which country's currency will turn out to be the reserve currency depends on its reputation. In order to be on the safe side, the countries attached themselves at the country with the highest reputation for price stability. Accordingly, the D-Mark became the reference currency for all other currencies. Whenever the Bundesbank increased the rate of interest, France had to follow and, hence, experienced a restraint of economic growth. Therefore, France wanted to get rid of the so called "diktat allemand" and demanded a European Monetary Union in which all EU governments were allowed to take part in the monetary decisions.

At the summit of Hanover in 1988 the Heads of State or Government decided to draft a road map, the so called Delors Plan, indicating the necessary steps to get from the status quo to the European Monetary Union. The Delors Plan was adopted a year later at the summit of Madrid in 1989. On the one hand all participating states will lose their monetary and some of their fiscal autonomy, on the other hand they will have to comply with the monetary regulations of the European Central Bank and with the fiscal rules of the stability and growth pact. The principles of the ECB were closely aligned to those of the Bundesbank. So the monetary order of the Bundesbank which the French government wanted to get rid of reappeared in the European Monetary Union. The French government was not amused. It avoided an open conflict by adopting a "yes-but-wait-and-see" position.

With these reservations in mind, President Mitterrand of France signed the Maastricht Treaty on 7 February 1992. The other Heads of State or Government signed as well. But President Mitterrand of France immediately recognized that the Maastricht Treaty lacked an enforcement mechanism once it is in force. Therefore three mental reservations have to be remembered:

(1.) The central bank should not be independent, but under political control
(2.) The political control should be French.
(3.) Mutual fiscal bailout should make sure that national governments cannot go bankrupt.

President Mitterrand expressed his *first reservation* already 7 months after the solemn signing of the Treaty of Maastricht. In an important and politically decisive

television talk of 3 September 1992 just before the French referendum on the Maastricht Treaty he revoked the core principle of the European Monetary Union, central bank independence. When the President came to the issue of central bank independence he said: "No, this is not true. [...] The monetary policy belongs to the European Council and the application of the monetary policy belongs to the Central Bank within the decisions of the European Council."[3]

But words had to be followed by deeds. Mitterrand's *second reservation* was the control of the ECB. The European Central Bank (ECB) had to be brought under French control. Though, Wim Duisenberg (the governor of the Bank of the Netherlands), has already been elected as President of the European Monetary Institute (EMI) and the subsequent ECB, with approval of the heads of State or Government in 1996 the new French President Jacques Chirac insisted thereafter on a second vote in which he injected a veto (despite of the already existing decision and despite of the vote by qualified majority rule). For he wanted the Frenchman Jean-Claude Trichet to become President of the ECB and not Wim Duisenberg. Chirac coerced Duisenberg to step down more or less involuntarily of his office after four years of his presidency and to be replaced by Jean-Claude Trichet.[4] The procedure enforced by Chirac was a clear violation of the Treaty: First an existing decision has been cancelled (outside the rules) and second a new decision of a four year presidency is inconsistent with the Treaty (art. 109a (2) (b) EC = art. 283 TFEU) which states that the President of the ECB is elected for eight years and not for four years (Warleigh 2002). This was a very bad start for the euro, but a consequence of the Maastricht Treaty for whose enforcement nobody is responsible.

Trichet, once in office, was not able to change the statutes of the ECB alone. But with the banking crisis of 2007-2008 the Southern members of the governing council became hungry for credits whatever the Treaty required. Their political demand for liquidity and their majority in the Council encouraged Trichet to start his securities markets programme (SMP) monetizing public debt of some States at the costs of all States. Some say that Trichet did not violate art. 123 TFEU because he intervened on the secondary and not on the primary market of government bonds. But in 1993 already, the European Council has clarified that this separation must not be misused for monetizing public debt. The Council said: "Purchases made on the secondary market must not be used to circumvent the objective of that Article".[5] Though SMP was inconsistent with the Treaty, it has nevertheless created a new status quo, which once in existence could

[3] Quoted from Issing (2008).

[4] In fact Trichet could not become president of the European Central bank immediately because he had to survive a court trial on a financial scandal of the state owned bank Crédit Lyonnais which he was in charge to control as a part of his political office in the French Government.

[5] Council Regulation (EC) No. 3603/93

no more be defined away. Indeed SMP can be seen as the trailblazer of ECB's later Outright Monetary Transaction Program (OMT).

Trichet has transformed the ECB (following Mitterrand's political testament) into a bailout institution for member states with balance of payments difficulties. He legalized Vinegar for some while the others had to play Oil.

*Mitterrand's last reservation* was the abolition of the no-bailout clause of art. 125 TFEU. Here again Trichet was the driving force. As Greece has become insolvent in the end of April 2010 the European Council decided that the no-bailout clause shall not be applied in this specific case. But a week later (on 7 and 8 May 2010) Trichet convinced the European Council that the situation is so dramatic that the no-bailout clause had to be abolished immediately for the euro zone as a whole and that it had to be replaced by a general bailout fund financed by all member states off-budget via a private company located in Luxembourg (Ludlow 2010). Obviously the Council was not empowered to de facto abolish the no-bailout clause of art. 125 TFEU. But Trichet was satisfied that the financial burden of the crisis has been distributed from some member states on all euro states collectively. The paying Member States were the Oil states. Their citizens were reluctant because they had to pay taxes for other member states. The receiving member states were the Vinegar states which were disappointed too because they received the money only under the condition of an austerity policy generating hardship and unemployment at home.

## VII. Summary and Conclusions

Friendship cannot be bought by money. But it can very well be destroyed by money. This danger highlights the problem of the euro. Friendship has grown in the European Union as long as the EU has promoted trade in private goods and every citizen could participate at private costs and private benefits.

European leaders believed that this success story will automatically continue with the euro. But they forgot that the euro is first of all a public good which has to be generated by coordinated action, not by trade. The public good offers an invitation to shirking because the more of the burden some participants contribute, the less have to be contributed by the other participants. Insofar as some member states are able to shift the burden of the monetary Union to others, the more the monetary union deteriorates into a transfer union.

If the participants of a monetary union consist of Oil and Vinegar governments such burden shifting seems to be nearly unavoidable. But a monetary union based on shirking and burden shifting cannot work. It is cause of distrust and hate and should therefore be dissolved to prevent a further deterioration. It is also impossible to improve the results ex post because the design at the outset is improper. This hypothesis is confirmed by history which shows that monetary unions consisting of

Oil and Vinegar nations always collapsed. Their collapse was not a disaster, but an opportunity to a new start under a proper design.

Transfer unions cannot survive unless under dictatorship. But a dictatorship does certainly not improve the friendship among the European peoples. Therefore the alternative of a dissolution of an existing Oil-Vinegar Monetary Union and a new start seem to be reasonable alternatives to restore European friendship.

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