

Beware of taking the ECB out of the Troika

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Finally, some good news for the Eurozone. The Advocate General of the EU's Court of Justice (ECJ), the Spaniard –but European as to his official duties– Pedro Cruz Villalón has declared that the **ECB's Outright Monetary Transactions (OMT) programme** (which gives it the power to buy unlimited amounts of government bonds in the secondary markets) might be legal under certain conditions. The use of the conditional here is important because the 'opinion' of the ECJ's Advocate General is only a recommendation and hence, although in 90% of the cases the ECJ follows his advice, is not legally binding.



The ECJ, which has its headquarters in Luxembourg, will publish its verdict in the autumn. If it follows Cruz Villalón's recommendation and ultimately the German Constitutional Court –which doubted the OMT's legality in the first place– accepts the decision, this would be a big step towards the Euro's 'irreversibility'. The OMT saved the common currency at the peak of the Euro crisis in the summer of 2012 when Spain –which was too big to fail and too big to be rescued– asked the European Stability Mechanism for a €100 billion rescue credit-line to bail out its banking system.

Shortly after that, in July 2012, Mario Draghi uttered his much-quoted statement that the ECB will do 'whatever it takes' to save the euro, and after the summer he outlined the conditionality attached to the OMT programme. The countries that would require OMT purchases would need to negotiate a rescue programme with the ESM and accept the reform plans drawn up and supervised by the Troika (in other words, they would need to give up part of their economic sovereignty).

In addition to conditionality, the ECJ's Advocate General now adds his own conditions, which are all controversial and will spark considerable debate: (1) the use of the OMT needs to be proportional (an ambiguous term that will trigger an intense debate between lawyers and economists); (2) The ECB needs to provide a proper legal and detailed reasoning for its support (this might be advisable, but sometimes –in order to prevent market panic– a central bank cannot disclose all it knows); and (3) if an OMT programme finally takes place, the ECB cannot be part of the Troika.

This makes a lot of sense. **The ECB is the only institution in charge of monetary policy** (and in this respect both European and national –even German– judges should themselves refrain from interfering because they lack the necessary expertise and experience in this domain, Cruz Villalón argues), but when it comes to economic policy the ECB has no competence whatsoever. Thus, it should not be at the negotiating table as part of the Troika with the democratic representatives of the Eurozone member states that are in financial need.

However, excluding the ECB from the Troika can be problematic. First, fiscal, economic and monetary policies are not watertight compartments. This is the reason why in the US the Secretary of the Treasury and the Governor of the Federal Reserve meet on a regular basis. Dispensing with the ECB's expertise from the Troika would be to short-change it. Especially after the creation of the Single Supervisor, the Eurosystem is the institution that is best informed about the state of the financial sector in a given country, and thus it can hardly be a good idea to do without its input.

Is it possible to assess the state of an economy, and to decide how to fix it, without taking into account the credit system? Certainly not. Europe should avoid falling into the trap of becoming too legalistic and dogmatic about how best to deploy its macroeconomic policy.

The second concern is that throughout the Euro crisis the ECB has been the only institution which has looked at it from a truly European perspective. In fact, the IMF is not a European institution and the Commission has all too often done the bidding of the most powerful member states, such as France and Germany. Undoubtedly, the ECB lacks the democratic legitimacy necessary to decide on the economic policies of member states, and this needs to be remedied. But do the IMF, the Commission, the EFSF or even the Eurogroup have such a legitimacy? Again, not really.

The reality is that because **the Eurozone does not have a democratically legitimised European treasury** –which should do the job of supervising the rescue programmes– the ECB has been forced to fill the gap. The solution, therefore, cannot be to take the ECB out of the picture without creating a legitimate institution to fulfil that necessary role.