



# THE ADEMU PROJECT: *Findings and Proposals*



Horizon 2020  
European Union Funding  
for Research & Innovation

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A DYNAMIC ECONOMIC AND MONETARY UNION

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# INTRODUCTION

*By Ramon Marimon, Scientific Coordinator of the Horizon 2020 ADEMU project*

*At the outset of the Horizon 2020 Programme, in 2014, there was a call for research on “Overcoming the Crisis: New Ideas, Strategies and Governance Structures for Europe.”*

This seemed to be a call that European macro research economists could not ignore.

By 2014, research in this area was blooming. In response to the euro crisis, the overall fiscal and monetary framework of the EMU was being revamped and further developed.

**The ADEMU project, aimed at linking “the supply of new ideas” and “the demand for reassessing the fiscal and monetary framework of the EMU”, was a successful applicant to that call.**

The project started in June 2015 with a network of eight groups of research economists from leading European Universities, coordinated by the European University Institute, where a group of research lawyers also joined the project.

In these three years, many things have happened in Europe. On the bright side, the euro crisis is finally part of history. However, differences across the euro area remain, with the legacy of debts and loss of human and physical capital, in most of the ‘stressed countries’.

On the dark side, we had Brexit. Not only is it the first step back in the construction of the EU, it has also shown that one cannot ignore dissatisfaction with the EU and the leading role of the states within the Union.

The EMU framework cannot be fragile to survive. The ADEMU research agenda is more alive now than it was when we started, and we are very pleased to report, now that the project comes to an end, that in these three years progress has been made.



**Ramon Marimon**  
ADEMU Scientific Coordinator  
[www.ademu-project.eu](http://www.ademu-project.eu)

Our detailed findings and proposals can be seen in our eBook produced in collaboration with VoxEU at <https://voxeu.org/content/emu-after-euro-crisis-lessons-and-possibilities-findings-and-proposals-horizon-2020-ADEMU-project>

Ramon Marimon, ADEMU  
Scientific Coordinator

**The views contained within this publication are the views of the authors of the research, and do not necessarily represent the views of the European Commission.**





# THE ADEMU PROJECT

ADEMU (A Dynamic Economic and Monetary Union) is part of the European Commission's Horizon 2020 framework ([www.ec.europa.eu/programmes/horizon2020](http://www.ec.europa.eu/programmes/horizon2020)), formed to establish resilient and sustainable economic and Monetary Union in Europe (EURO-1-2014\*). The objective of ADEMU is to reassess the overall fiscal and monetary framework of the EU and, in particular, the euro area.

In response to the European debt crisis and associated deep recession, a number of important steps were taken towards redesigning the institutional architecture of the Economic and Monetary Union in Europe, based on the roadmap outlined in the Van Rompuy Report of 2012.

However, there was a noticeable gap between policy-oriented analyses of the precise EU challenges and the major developments in dynamic macroeconomic theory of the past three decades.

**ADEMU brought together eight research groups from leading European institutions\*\* with the aim of closing this gap. Over the course of three years, ADEMU has conducted extensive research to address the gap and propose solutions that will benefit member states.**



Ana Gouveia, Banco de Portugal and formerly Portuguese Ministry of Finance

## ADEMU CONTRIBUTORS

The project has benefited from the experience of esteemed economists and academics, as well as the contributions of talented post-graduate doctoral researchers and external associates.

**ADEMU has been guided by an advisory committee, whose members are:**

- ▶ **Thomas F. Cooley** (Stern School of Business, New York University), *Advisory Committee Chair*
- ▶ **Sir Charles Bean** (London School of Economics)
- ▶ **José Manuel Campa** (IESE and Grupo Santander)
- ▶ **Jean-Pierre Danthine** (Swiss National Bank)
- ▶ **Lars Peter Feld** (Walter Eucken Institut and University of Freiburg)
- ▶ **Lucrezia Reichlin** (London Business School)
- ▶ **Thomas J. Sargent** (New York University)
- ▶ **René Smits** (University of Amsterdam)

**The executive and steering committee includes:**

- ▶ **Ramon Marimon** (European University Institute and Barcelona GSE), *Steering Committee Chair*
- ▶ **Radim Boháček** (CERGE, Charles University in Prague)
- ▶ **Giancarlo Corsetti** (University of Cambridge)
- ▶ **Hugo Rodríguez Mendizábal** (Barcelona GSE)
- ▶ **Christian Hellwig** (Toulouse School of Economics)
- ▶ **Thomas Hintermaier** (BGSE, University of Bonn)
- ▶ **Morten Ravn** (University College London)
- ▶ **Pedro Teles** (Universidade Católica Portuguesa)

You can find a complete list of all the researchers, associated researchers and associate PhD and post-doctoral researchers who have contributed to the project on our website, which will be archived for future reference:

[www.ademu-project.eu/partners/researchers](http://www.ademu-project.eu/partners/researchers)  
[www.ademu-project.eu/associated-researchers](http://www.ademu-project.eu/associated-researchers)  
[www.ademu-project.eu/associate-phd-researchers](http://www.ademu-project.eu/associate-phd-researchers)

\*see <https://ec.europa.eu/research/participants/portal/desktop/en/opportunities/h2020/topics/euro2014-1-.html>.

\*\*Barcelona Graduate School of Economics, Católica Lisbon School of Business & Economics, CERGE-EI, European University Institute, Toulouse School of Economics, Universität Bonn, University College London and the University of Cambridge



ADEMU steering committee member José Manuel Campa, left, (IESE, Grupo Santander and ADEMU advisory committee member), speaking at an ADEMU conference at Banco de España with former EC Vice President Joaquín Almunia.

## ADEMU RESEARCH

The ADEMU team has spent three years examining the legal and institutional framework of the European Economic and Monetary Union (EMU). Together, these experts have conducted a rigorous investigation of risks to the long-term sustainability of the EMU, and developed detailed institutional proposals aimed at mitigating these risks.

Experts from global institutions including the International Monetary Fund, the European Commission, the Federal Reserve of the United States, the European Stability Mechanism, the European Central Bank, the European Fiscal Board, national governments and central banks have attended conferences, workshops and seminars across Europe to discuss this research and move forward proposals for a stable Eurozone.

The result is a series of implementable proposals that aim to allow the EMU to learn lessons from the euro crisis and present solutions that will help prevent further economic and financial crises.

## WORKING PAPERS

ADEMU researchers and associates have produced more than 100 working papers, all of which are archived in an open access repository managed by the Barcelona Graduate School of Economics, Universitat Pompeu Fabra and Universitat Autònoma de Barcelona.

In order to further extend the scope of the research carried out in the framework of the ADEMU project, and with the additional aim of contributing to a relevant dissemination of its objectives and outcomes, a number of economics scholars and policy makers have been invited to join the project as associated researchers. As such, associated researchers are regularly informed about ADEMU events and can publish their research related to ADEMU in the working paper series.

[www.ademu-project.eu/working-papers](http://www.ademu-project.eu/working-papers)



Jean Pierre Danthine (Swiss National Bank and ADEMU Advisory Committee member), left, speaking at the 'A Fiscal Union for the EMU' conference



# ADEMU EVENTS

*ADEMU's research has been discussed, analysed and refined at a series of events around Europe in collaboration with organisations including Banco de España, Deutsche Bundesbank, International Monetary Fund, and the European Stability Mechanism. These events have included presentations from some of the world's leading economists, who have actively contributed to ADEMU's research.*



Waltraud Schelkle, Associate Professor of Political Economy, London School of Economics, with ADEMU PhD researcher Johannes Fleck, European University Institute



Nobel prize-winning economist Edward C Prescott with ADEMU Scientific Coordinator Ramon Marimon at an ADEMU workshop in Barcelona

Rolf Strauch, Chief Economist, European Stability Mechanism, speaking to ADEMU during the 'How Much of a Fiscal Union for the EMU' conference



ADEMU at Banco de España







Former EC Vice President Joaquín Almunia (left) with Martin Sandbu, economics commentator at the Financial Times



Federico Fabbrini, Full Professor of European Law, School of Law and Government, Dublin City University







# THE EMU AFTER THE EURO CRISIS: LESSONS AND POSSIBILITIES

*Findings and proposals from the Horizon 2020 ADEMU project*

*The three-year Horizon 2020-funded ADEMU project was established in 2015 to reassess the fiscal and monetary framework of the European Monetary Union (EMU).*

The research has used, and further developed, the tools and theories of modern economics and finance, as well as of modern legal research, with three aims:

- ▶ To gain a better understanding on how economies behave and react to policies in times of crisis and recession
- ▶ In light of this enhanced understanding, to reassess the current EMU framework and existing proposals for reform
- ▶ To establish new proposals to strengthen the resilience and competitiveness of the EMU, potentially implementable with consensus in the current heterogeneous euro area.

Addressing these issues has required covering a large number of related topics: sovereign debt crisis, risk sharing and economic stabilisation policies, fiscal stimulus and consolidation policies, fiscal multipliers, optimal tax policies, financial stability, macroprudential and unconventional monetary policies, among others.

ADEMU has also focused on the design of the EMU architecture yet to be finished; namely, the incomplete Banking Union and the not-yet fully functioning Economic and Fiscal Union.

All this research has resulted in two new proposals to strengthen the EMU:

- ▶ Risk-sharing and economic stabilisation capacity - the European Stability Fund (ESF)
- ▶ A European Unemployment Insurance System (EUIS)





## *Our main research conclusions and policy proposals are presented in our VoxEU.org ebook. They are:*

### *Lessons from the euro's first 20 years*

- ▶ The euro crisis and dealing with the debt overhang (see page 10)

### *The EMU's capacity for risk sharing and economic stabilisation*

- ▶ A European Stability Fund for the EMU
- ▶ A European Unemployment Insurance System (EUIS)

### *New models for understanding recessions, and optimal policy responses*

- ▶ Macroeconomic stabilisation in heterogeneous societies
- ▶ Recessions following expansions: the instability of market economies

### *Resilience through fiscal policy*

- ▶ Persistent stimulus packages
- ▶ Reassessing tax policies and tax coordination: The case for a tax on automation

### *Financial markets and stability*

- ▶ Banking Union and the European Central Bank
- ▶ Financial stability: The role of macroprudential policies

### *EMU reforms from a legal and political economy perspective*

- ▶ European Stability Mechanism: the path to reform
- ▶ The political economy of policy implementation

### *The EMU's fiscal and monetary framework*

- ▶ A new fiscal and monetary framework for the EMU? The EU Presidents' Roadmap in 2018 (see page 11)

## *See the recommendations in full at:*

**<https://voxeu.org/content/emu-after-euro-crisis-lessons-and-possibilities-findings-and-proposals-horizon-2020-ademu-project>**

# LESSONS FROM THE EURO'S FIRST 20 YEARS

*In the aftermath of the global financial crisis, the long and slow recovery of the euro area coincided with a strong economic and financial divergence of member states. Activity, unemployment, fiscal and financial stability varied massively from country to country.*

The benefits of the Union were many. But it became clear that the risks involved in implementing a single currency had been vastly underestimated. Key functions of monetary policy were overlooked when it was transferred from national capitals to Frankfurt, and these functions contributed to the polarisation and imbalance between member states.

One such function was the role that a central bank plays in ensuring the stability of government debt. During the crisis, central banks such as the Federal Reserve System in the United States and the Bank of England in the United Kingdom were ready and able to take the necessary steps to ensure stability of the markets for national government bonds.

It wasn't until 2012 that the European Central Bank was able to play a comparable role, through the outright monetary transactions (OMTs) programme. This was possible after long political negotiations, creating a consensus to establish the European Stability Mechanism (ESM) (and its predecessor).

A key complement of the OMTs is that the ECB can intervene and buy public debt, provided that the country requesting assistance enters an ESM programme and accepts the conditions that come with it.

Within the European Union, there are countries with a heavy debt burden, and others which benefit from a low-risk status in the assessment of investors. This polarisation conditions the ability of the Union to emerge from persistent financial and economic stagnation, exacerbating the debt overhang problem.

By lending over long periods at very low rates, interventions by the ESM have given countries with high debt the space and time to reform economic policy and implement measures to speed up recovery.

There is no doubt that the initial ESM interventions, complementing the ECB programmes, have been successful in curtailing adverse consequences that could have escalated into a euro crisis between 2011 and 2012.

Yet, to consolidate these gains and achieve full recovery, many reforms are needed at both country level and Union level. Europe is still exposed to risk of financial and economic involution.

*ADEMU's research in this area has focused on creating a sustainable, meaningful way to trade-off between two conflicting objectives: to reduce debt as fast and efficiently as possible, and to avoid the risks that reduction may create.*

This is a challenging task that requires, first and foremost, well-designed policies that have consistent political agreement and support. What is important now, and what ADEMU's research has illustrated, is that we need to consolidate, clarify and develop a permanent structure that will allow Europeans to reduce debt today while minimising future risk.

*"What is important now, and what ADEMU's research has illustrated, is that we need to consolidate, clarify and develop a permanent structure that will allow Europeans to reduce debt today while minimising future risk."*



# TWO PROPOSALS TO STRENGTHEN THE EMU

*The euro crisis has been a major stress test for the European Economic and Monetary Union (EMU).*

Among other things, the crisis turned into a recession for euro area 'stressed countries' (with the exception of Ireland). For the EA15 (excluding Portugal, Italy, Greece, and Spain), the recovery has followed a similar pattern to (or slightly better than) the US and Japan.

*In view of the changing political environment and the challenges faced by the Monetary Union, it is more important than ever to be clear about the lessons one should extract from the euro crisis, in order to provide proper research to assess the framework of the EMU and propose new ways to strengthen the Union.*

ADEMU started in June 2015, when the most critical moments of the crisis had already unfolded and just before the EU Five Presidents' Report was released, providing a roadmap to 'forge Europe from the euro crisis'.

It was not just a declaration of intentions. Following the Four Presidents' Report of 2012, important steps had already been taken: the European Banking Union was taking shape and the ECB and the new European Stability Mechanism (ESM) were beginning to play a role in resolving the euro crisis.

Nevertheless, viewing the euro crisis in light of the Presidents' Roadmap raises many questions, some of which can be addressed with modern macroeconomics and finance. Definitive answers will be slow to emerge, but using the tools of modern economics and finance can improve our understanding of the weak points in the EMU as it exists today.

Our research helps us to better understand the euro crisis and recession, and, most importantly, to make a reassessment of EMU in 2018. It allows us to conclude with two proposals that can help to strengthen it.

## **The European Stability Fund (ESF) as a constrained efficient mechanism**

It is possible to substantially, and voluntarily, improve the risk-sharing capacity across heterogeneous European countries without incurring undesired transfers or moral hazard problems. In doing so, we can enhance the resilience of EMU to new crises and better confront the 'debt overhang' problem and the need for 'safe assets'. ADEMU provides the theory and software showing how things would have been very different (indeed, better) if a European Stability Fund – which can be built out of the ESM – had been in place during the euro crisis.

## **A European Unemployment Insurance System (EUIS)**

We show just how different labour markets, and unemployment insurance policies, across Europe are. We also show, however, that in spite of these differences, there can be unanimity among euro area countries – and among the employed, the unemployed and the inactive within countries – with regards to a common EUIS with undefined coverage and a low replacement rate (around 15% of wages), provided that stable labour taxes to cover unemployment benefits vary across countries in order to avoid permanent transfers. However, reaping the gains of such reform would require coordinated action.

The ADEMU research project has contributed to the current policy debate on the future of the EMU, based on basic research. This, in turn, makes contributions to the modern macroeconomics and finance literature from which it has built. It has also benefited from a fruitful collaboration with an EUI Law research group. In sum, it is an example of what EU (UK included) funded social research can provide.

**Our detailed findings and proposals can be seen in our eBook produced in collaboration with VoxEU at <https://voxeu.org/content/emu-after-euro-crisis-lessons-and-possibilities-findings-and-proposals-horizon-2020-ADEMU-project>**

*Reassessing the fiscal and monetary framework of the EMU also raises important and interesting legal issues and political economy concerns. Addressing these questions, and providing answers, has formed the research agenda of ADEMU.*

# ADEMU FOR POST-GRADUATE STUDENTS

*The contribution of PhD and post-doctoral researchers to ADEMU has been invaluable to the project.*

ADEMU working groups met regularly to discuss students' work on related topics. This work has been presented at our events - including our final conference - where students also acted as discussants for papers by ADEMU researchers and participants.

PhD and post-doctoral research papers are included in the ADEMU working paper series at [www.ADEMU-project.eu/working-papers](http://www.ADEMU-project.eu/working-papers)

## Johannes Fleck PhD researcher

*Johannes Fleck is a PhD researcher at the European University Institute (EUI). Under the supervision of ADEMU scientific co-ordinator Ramon Marimon, Johannes has been responsible for directing the ADEMU working group at the EUI, which includes setting topics and dates of meetings, inviting external speakers and keeping group members up-to-date with project activities. He has also been a valued contributor to ADEMU conferences, presenting his work and acting as discussant.*

"Being part of the ADEMU project has helped me to get a comprehensive and detailed picture of the current research frontier in several fields of economics. Starting from this basis, I was able to develop ideas for genuine research projects, discuss them with leading academics and receive feedback on my work. By supporting the project coordinator in some administrative tasks, I also gained hands-on experience regarding practical aspects related to managing a large scientific project, such as communicating with participants and organising academic conferences.

Most importantly, I became closely familiar with published and on-going research projects of high-calibre economists. Specifically, I learned what questions they are working on and what methods they apply to answer them. Beyond this, I was able to talk with them in person about their work and to ask their advice on some of my own projects. In this way, I have also become part of an academic network which connects academics and policy makers across several countries, institutions and fields of specialisations.

Two more opportunities given to me by the ADEMU project were financial support to attend events organised by other participating departments and the experience of directing the ADEMU working group at the EUI.

My aim is to contribute to economic research on macroeconomics and fiscal policy, which includes topics related to European affairs. For the immediate future, this means that I aim to finish my PhD studies with a strong job market paper as well as a portfolio of high-profile working papers.

To this end, the ADEMU project has made substantial contributions as it gave me the opportunity to present my work and to receive comments and suggestions on how to improve it. In other words, it made me familiar with the process of defining research questions, using state of the art methods to answer them and transforming my findings into publications."





### *ADEMU PhD and post-doctoral researchers*

- ▶ Lian Allub
- ▶ Nicolas Aragon
- ▶ Ivo Bakota
- ▶ Guillerme Bandera
- ▶ Rafael Barbosa
- ▶ Kizkitza Biguri
- ▶ Alica Ida Bonk
- ▶ João Brogueira De Sousa
- ▶ Silvia Calò
- ▶ Andrea Camilli
- ▶ Felix Corell
- ▶ Constance de Soyres
- ▶ Alessandro Ferrari
- ▶ Alexandra Fotiou
- ▶ Johannes Fleck
- ▶ Carlo Galli
- ▶ Matteo Gatti
- ▶ Henrike Groeger
- ▶ Philipp Grübener
- ▶ David Koll
- ▶ Carolina López-Quiles Centeno
- ▶ Georgios Manalis
- ▶ Viktor Marinkov
- ▶ Lukas Mayr
- ▶ Guarava Meta
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- ▶ Ana Moreno Maldonado
- ▶ Gergo Motyovszki
- ▶ Vladimir Novák
- ▶ Joonseok Oh
- ▶ Matic Petricek
- ▶ David Rivero
- ▶ Anna Rogantini Picco
- ▶ Laure Simon
- ▶ Chima Simpson-Bell
- ▶ Agnieszka Smolenska
- ▶ Albert Soto
- ▶ Jan Teresinski
- ▶ Milena Wittwer
- ▶ Martin Wolf
- ▶ Tomasz Wozniakowski



# THANK YOU

*ADEMU is grateful to all researchers, speakers, participants, associates, students, event attendees and everyone who has contributed to the project over the last three years.*

**We thank you for your  
valuable contributions.**





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