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European Monetary Union: The Great Presumption

With a scandalous ruling, the German Constitutional Court not only calls into question the legal system of the EU, but also proves that it is totally incapable of understanding a multilateral economic order.

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The German Constitutional Court regards the Public Sector Purchase Programme (PSPP) launched by the European Central Bank (ECB) in 2015 as exceeding the powers of the central bank. It calls on the German Government and the Bundestag "to work towards a proportionality test by the ECB. The court grants the ECB a three-month period for this purpose. If this period expires without "the Governing Council of the ECB clearly stating in a new evaluation that the monetary policy objectives pursued with the PSPP are not disproportionate to the economic and fiscal policy implications associated with it", the Deutsche Bundesbank may no longer participate in the implementation and enforcement of the programme.

The judgment is scandalous because it is written without any knowledge of macro-economic interrelationships, because it demands the consideration of interrelationships (but only for Germany), which are of course part of the ECB's assessment (but for Europe). The German Court has also triggered an earthquake in legal and political terms, because it disregards a judgment of the European Court of Justice, which is clearly superior to it in these matters.

In 2015, the ECB wanted to stimulate consumption and investment with the purchase of government bonds and similar marketable debt instruments made possible by the PSPP in order to raise the inflation rate in the euro zone back to just below 2 percent. This was because the rate of price increases had been below 1 per cent in 2014 and continued to slide in early 2015 (this was also the case, incidentally, even without taking into account the sharp fall in energy prices). Without a European recovery, there could be no return to an appropriate level of inflation.

Proportionality?

The Court considers that this action by the ECB does not respect proportionality. In its press release on the ruling, it writes: "The unconditional pursuit of the monetary policy objective pursued by the PSPP to achieve an inflation rate below but close to 2%, while ignoring the economic policy implications of the programme, therefore manifestly disregards the principle of proportionality."

This is an assertion that can only be called absurd: the Court is accusing the actors in the ECB of not having considered the economic policy implications of their own programme. Apparently the judges in Germany believe that they understand more about economics than the economists in Frankfurt. In the opinion of the court, the ECB ignores in its measures relationships which have such major economic policy consequences that the court believes it can qualify the measures as disproportionate. The judges have probably not noticed that the court's examples of the consequences all come from the well-

worn ideology of the German conservatives. They could and should have known that the ECB is responsible for the whole euro zone, not just Germany; but this fact was not taken into account in the judgment.

Similarly superior in their economic expertise in comparison to the ECB, the German judges also feel superior to the legal expertise of their colleagues at the European Court of Justice (ECJ), which ruled in December 2018 that the ECB's measures were in keeping with its mandate. The press release of the Federal Constitutional Court states the following with regard to the judgment of the ECJ: "The view of the Court of Justice that the decision of the Governing Council of the ECB on the PSPP and its amendments still fall within the scope of its competence obviously fails to recognise the significance and scope of the principle of proportionality (Article 5 (1) sentence 2 and (4) TEU), which must also be observed in the allocation of competences, and is methodologically simply no longer justifiable because the actual effects of the programme on economic policy are completely excluded.

Here, too, the German Constitutional Court suggests that it knows the real effects of the bond purchase programme on economic policy, or at least is better placed than the judges of the ECJ to assess them. What the German court considers to be the "real" effects of the programme, which the rest of the world has apparently overlooked or at least failed to appreciate properly, is, however, revealing. It writes:

"The PSPP improves the refinancing conditions of the Member States because they can obtain loans on the capital market on much more favourable terms; it therefore has a considerable impact on the fiscal policy framework in the Member States. ... The PSPP also has an impact on the banking sector by transferring large amounts of risky government bonds to the Eurosystem's balance sheets, thereby improving the economic situation of banks and increasing their creditworthiness".

These are certainly both effects of the programme that the ECB is seeking to achieve in exactly the same way, and it is therefore natural that the Governing Council of the ECB should have considered these effects when it chose the

PSPP. The German Court should have taken note of the fact that, in a world in which private households are saving as usual, and in which the corporate sector has also become a net saver in most countries for years, growth can only be stimulated, and an inflation rate close to 2 percent only be achieved, if the state makes credit-financed expenditures. It is precisely for this purpose that favourable financing conditions for these states and a stable banking sector are needed. But such considerations are certainly not written down by the Association of German Banks, which is the mentor for the constitutional judges.

Economic illiteracy

The ECB Governing Council uses a medicine which the German court rejects because, in its view, it causes undesirable side effects. A court cannot judge economic interrelationships if it is given solely unilateral advice, and consequently it should not judge the effects of the ECB's policy. It seems to believe that the ECB's desired effect on the inflation rate should simply happen by magic, but it should not be achieved by means of public spending or by stabilising the banks of other euro countries. The fact that the court does not name any other remedy which it believes the ECB could have better implemented shows that the German judges are calling on the ECB to square the circle. That cannot be a sensible ruling!

The court's press release goes on to say: "The consequences of the PSPP also include economic and social effects on almost all citizens, who are at least indirectly affected as shareholders, tenants, property owners, savers and policyholders. Savings, for example, are subject to significant risks of loss."

This is curious: risks of loss for savings arise above all when the euro zone fails in macroeconomic terms. And this is exactly what the ECB is desperately trying to prevent by attempting to ease the financing conditions of the EMU member states. These states have been struggling for economic survival under the yoke of German wage dumping since the start of EMU and the austerity policy that the German government has imposed for years on the German state. Once again, the judges do not get the big picture: the consequences of Germany's

aggressive policy are deflationary efforts of the debtor countries to adjust to German wages and prices. And this inevitably leads to a downward adjustment of interest rates – where else should they go? Lawyers may find it incomprehensible that interest rates are not a detached variable that a central bank can somehow set without regard to the overall economic situation of the area for which it is responsible. But the ECB cannot be held responsible for such “economic illiteracy” on the part of German judges, as the *Financial Times* has rightly termed it.

The fact that the court, in listing the effects of the PSPP, also notes that “companies that are no longer economically viable per se ... remain in the market because of the general interest rate level, which has also been reduced by the PSPP”, shows the judges' complete incompetence in economic matters. The fact that the euro zone is stuck at zero percent interest rates is largely due to the misguided European economic policy emanating from Germany. One can imagine what a euro zone would look like without PSPP, where there would only be “viable” German companies, where unemployment in Southern Europe would be 20 percent and in Germany a comparatively mild 10 percent, and where all German claims on the rest of the EMU would be devalued accordingly.

Ignorance at the highest level

The judges' demand, that the ECB should weigh up its actions, forecast the effects, and document everything, is an egregious display of ignorance. The decisions of the central bank are precisely documented session after session, commented on and openly questioned by media representatives. Forecasts are produced regularly and long reports are written by the ECB. Anyone interested can read this. To state that it is “not evident that the Governing Council has recorded and weighed up the consequences that have been created in the PSPP and are directly connected with it” is sheer impudence.

Finally, to set the central bank a three-month deadline by which it must carry out the weighing up and documentation is arrogant. One can only advise the ECB to write a letter to the court expressing its doubt that it could succeed in

rectifying so much legal ignorance in economic matters within three months. It is impossible to gauge the political damage that this judgment will cause.

Incidentally, the principle now upheld by the German Constitutional Court, according to which consideration must be given to collateral damage to monetary policy, is to be warmly welcomed. So far, this has been rejected almost exclusively by German stability fanatics. Who in Europe has enforced the rule that the central bank – without any consideration for losses – must always and everywhere enforce the objective of price stability? Germany, because it is mentally guided by stability fanatics, has succeeded in getting the Maastricht Treaty to make the ECB far more committed than before to the objective of price stability and to make it completely independent.

And now the highest German court is saying: there are things outside price stability and the ECB must not ignore them; and that the government and the Bundestag should monitor the actions of the ECB, which is actually completely independent. Bravo, then most of the rest of Europe will rightly declare Germany to be schizophrenic. If the German government does not quickly and completely distance itself from the ruling of the Federal Constitutional Court by declaring the court to have no jurisdiction over the ECB, Europe is lost. Otherwise there can be no question of trust in the willingness of Germany and the EU to lead the European economy out of its biggest crisis since the Second World War..