

Author:

IGNAZIO VISCO

Governor Emeritus – Bank of Italy, Rome

ON EUROPEAN FRAGMENTATION AND THE SINGLE CURRENCY IN AN UNCERTAIN WORLD*

ABSTRACT

Europe faces growing strategic and economic challenges arising from the policies of the second Trump administration, extending beyond trade to energy, defence, digital services, and cross-border payments. Heightened uncertainty over US policy has raised concerns about the stability of the international monetary system and the future role of the dollar. In this context, some observers argue that the European Union could strengthen its geopolitical position and that the euro could assume a more prominent role as an international reserve currency. However, market fragmentation, political divisions and heterogeneous legal frameworks continue to constrain this prospect. Sustaining Europe's economic and geopolitical standing in the face of demographic, technological, and market pressures requires a coherent reform agenda aimed at deepening integration, improving policy coordination and communication, preserving economic openness, and managing the social consequences of economic transformation.

Keywords European Economy; Single Currency; International Monetary System

JEL Classification: E02; F02; F15

RIASSUNTO

La frammentazione europea e la moneta unica alla luce dell'incertezza globale

Crescenti sfide strategiche ed economiche per l'Europa derivano dalle politiche della seconda amministrazione Trump e non riguardano solo il commercio ma anche l'energia, la difesa, i servizi digitali e i pagamenti transfrontalieri. La maggiore incertezza generata dalle politiche

* This article originates from a talk given at the LSE European Institute, London, 29 September 2025. I would like to thank Iain Begg and David Marsch for the invitation to the event, co-sponsored by Omfif, and for useful comments and suggestions Fabrizio Balassone, Piero Cipollone, Alessio De Vincenzo, Antonella Foglia, Giuseppe Parigi and Stefania Zotteri, while remaining solely responsible for the views presented here.

statunitensi solleva preoccupazioni circa la stabilità del sistema monetario internazionale e il futuro ruolo del dollaro. In questo contesto, alcuni osservatori sostengono che l'Unione europea potrebbe rafforzare la sua posizione geopolitica e l'euro assumere un ruolo più importante come valuta di riserva internazionale. Tuttavia, frammentazione economica, divergenze politiche e differenze normative e istituzionali limitano fortemente queste prospettive. Per sostenere la posizione economica e geopolitica europea di fronte alle pressioni demografiche, tecnologiche e di mercato è necessario un programma di riforme coerente volto ad accrescere l'integrazione, migliorare il coordinamento e la comunicazione delle politiche, preservare l'apertura dell'economia e gestire le conseguenze sociali delle trasformazioni economiche.

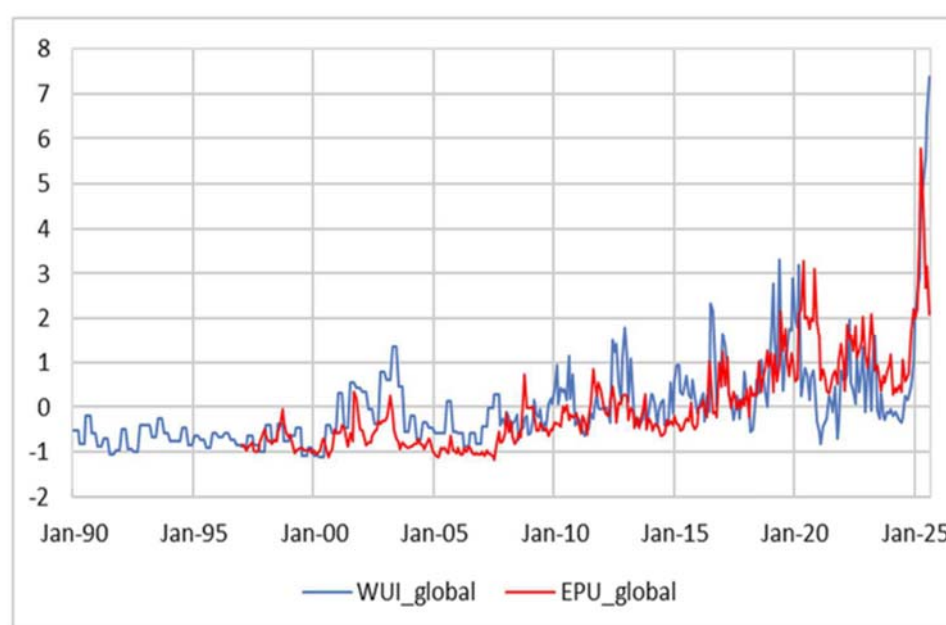
1. WORLD UNCERTAINTY AND THE UNFAVOURABLE GEOPOLITICAL LANDSCAPE

The rise in global uncertainty less than a year into Donald Trump's second term as President of the United States is, at the very least, startling. Both international and domestic policy decisions have led some commentators to argue that the European Union could benefit from this situation, as it might prompt the EU to finally get its act together on institutional and policy reforms, and fulfil its geopolitical potential. According to some, the euro could profit from a (supposed) weakening of the dollar and become a fully-fledged reserve currency and international payment instrument. Like others, I remain sceptical of this last claim, given the absence of a sufficiently large and liquid market for euro-denominated safe assets, the fact that the euro remains a "currency without a state" (Padoa-Schioppa, 2004), and the persistent, perhaps growing, political, economic, and financial fragmentation in Europe.

In such a divided Europe, despite the ambitions expressed in last year's Reports by Enrico Letta and Mario Draghi, a higher degree of integration is unlikely to materialize within this decade due to several political and institutional obstacles that are difficult to overcome. When it comes to currencies, their strength reflects the strength and integration of the economy – and its legal, political, and security systems – that underpin them, not the other way around. This explains the dominance of the British pound during the Empire (De Cecco, 1974), the emergence of the US dollar-centric system under the Bretton Woods agreements in 1944, and the persistence of a dollar-centric "non-system" after their collapse in 1971.

This may also explain current scepticism about the US dollar's continued "exorbitant privilege", which has allowed the United States to finance large deficits at relatively low cost, thanks to low-risk premiums on long-term US Treasuries. In fact, as I have noted, Trump's second term has driven global uncertainty to levels not seen since the end of the Cold War (Fig. 1). The geopolitical landscape is indeed dramatic: ongoing wars and aggressions, rising protectionism, nationalist and populist upheavals, the decline of multilateralism, and the extreme weakness of international cooperation.

FIGURE 1 – *Uncertainty Indicators (Standardized Indices)*



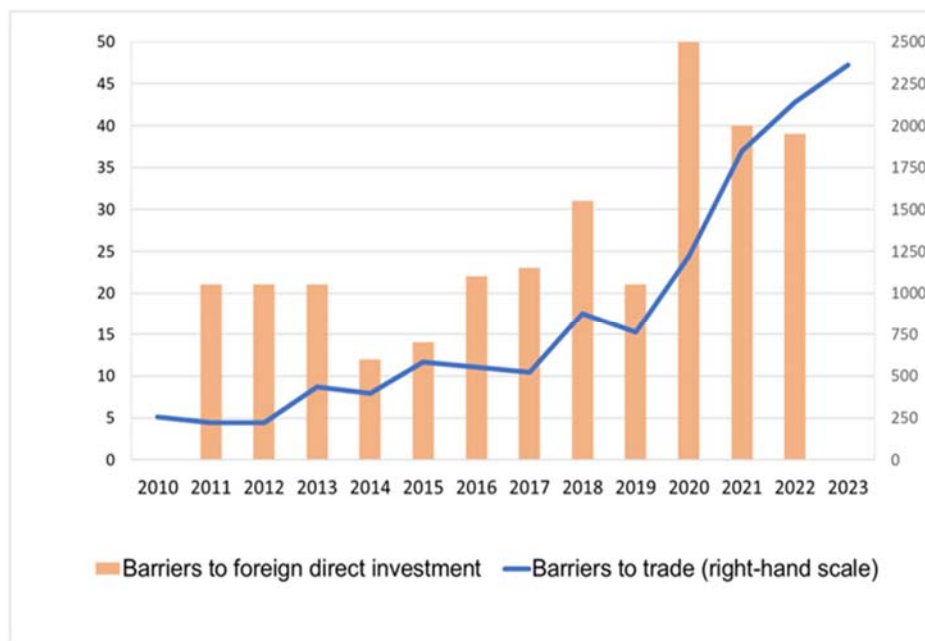
Sources: <https://www.policyuncertainty.com>

Note: the World Uncertainty Index (WUI) is based on Ahir *et al.* (2022); the Economic Policy Uncertainty Index (EPU) is based on Davis (2016).

On the economic front, and more broadly regarding common global challenges and possible responses, the current situation is truly appalling, whether we consider climate change and energy sources (i.e. fossil fuels versus renewables) or pandemic risks and vaccines. As well, digital threats, the risks related to the persistence of extreme poverty in LDCs and the consequences of demographic trends are minimised, if not outright denied, by the current US administration.

Without delving into the rationale behind Mr. Trump's tariff campaign – which seems poorly grounded from a purely economic perspective, even though the political use of trade policy has a long history (Hirschman, 1945) – it must be acknowledged that protectionist trends did not begin with Trump's second term (Fig. 2). While the US administration's declarations and actions have certainly intensified global uncertainty, the policies accompanying the extraordinary opening of global markets and the ICT/digital revolution have failed to produce more equitable and balanced economic conditions. Hundreds of millions have escaped extreme poverty in the so-called Third World, yet inequality and anxiety have steadily increased in advanced economies. Improvements in emerging markets have also been uneven. The inadequate recognition of their growing economic importance in the governance of international financial institutions has led to mounting dissatisfaction.

FIGURE 2 – *New Barriers to Trade and to Foreign Direct Investment*
(number of new barriers)

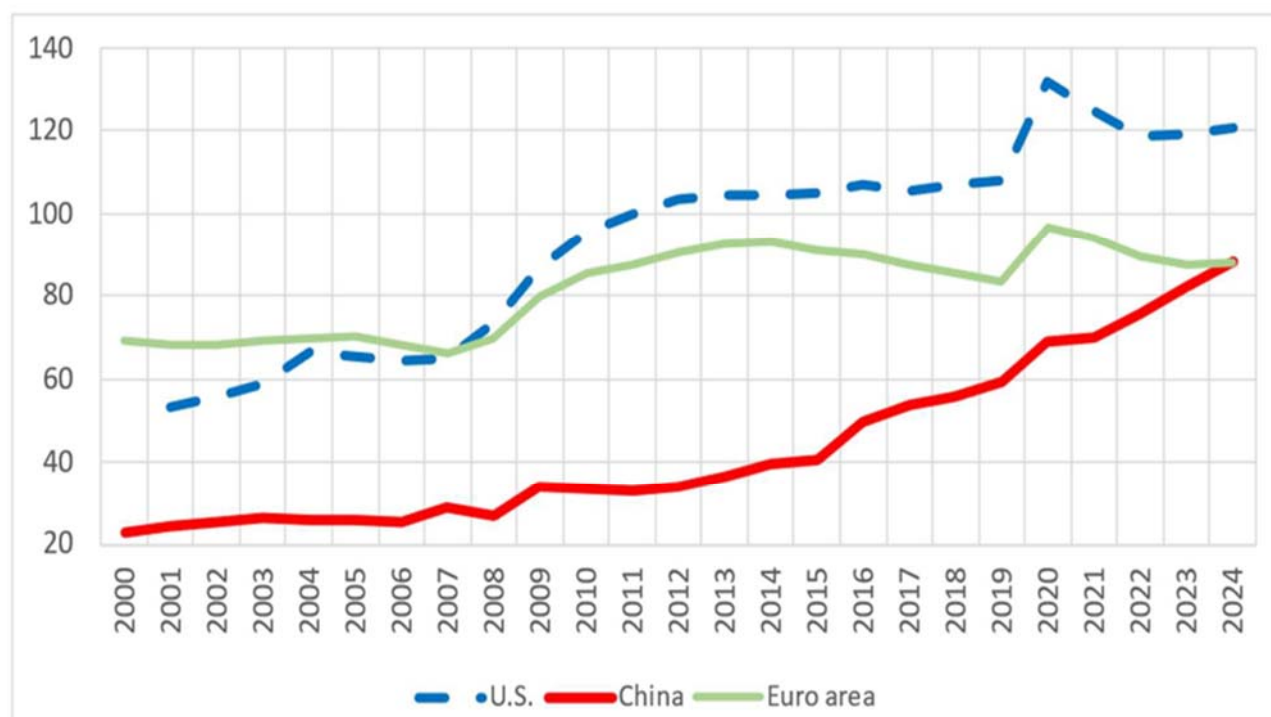


Sources: Global Trade Alert and UNCTAD.

2. IMBALANCES AND VALUATION EFFECTS

At the same time, it is a fact that US internal and external imbalances have been rising well before the current administration took office, and they are very significant today. Domestically, public debt is now around 120% of GDP (USD 36 trillion) and rising (Fig. 3). This is occurring alongside rising debt levels in China and other emerging economies, including private (banking- and non-banking) debt. Overall, excluding financial intermediaries' liabilities, global debt totals approximately USD 250 trillion – split roughly into USD 100 trillion in public debt, USD 90 trillion in corporate debt, and USD 60 trillion in household debt – while global GDP stands at about USD 100 trillion. While in the euro area the public debt-to-GDP ratio has been fluctuating around 90% since the Global Financial Crisis (GFC), it is particularly worrisome that for both the United States and China projections are pointing to a prolonged continuation of the rising trends.

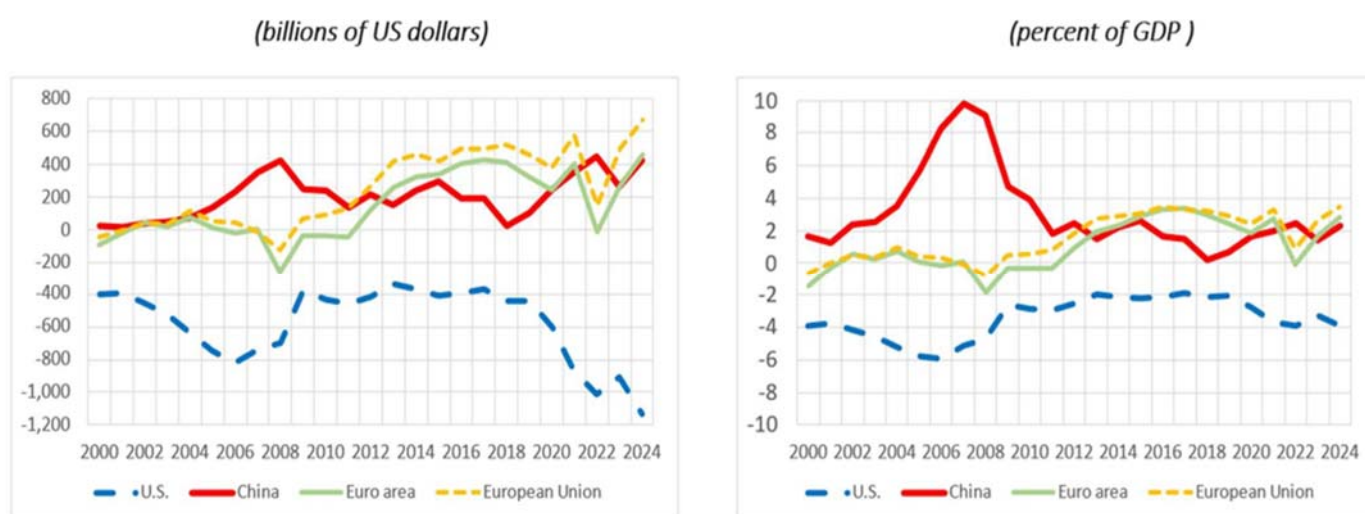
FIGURE 3 – *General Government Gross Debt (percent of GDP)*



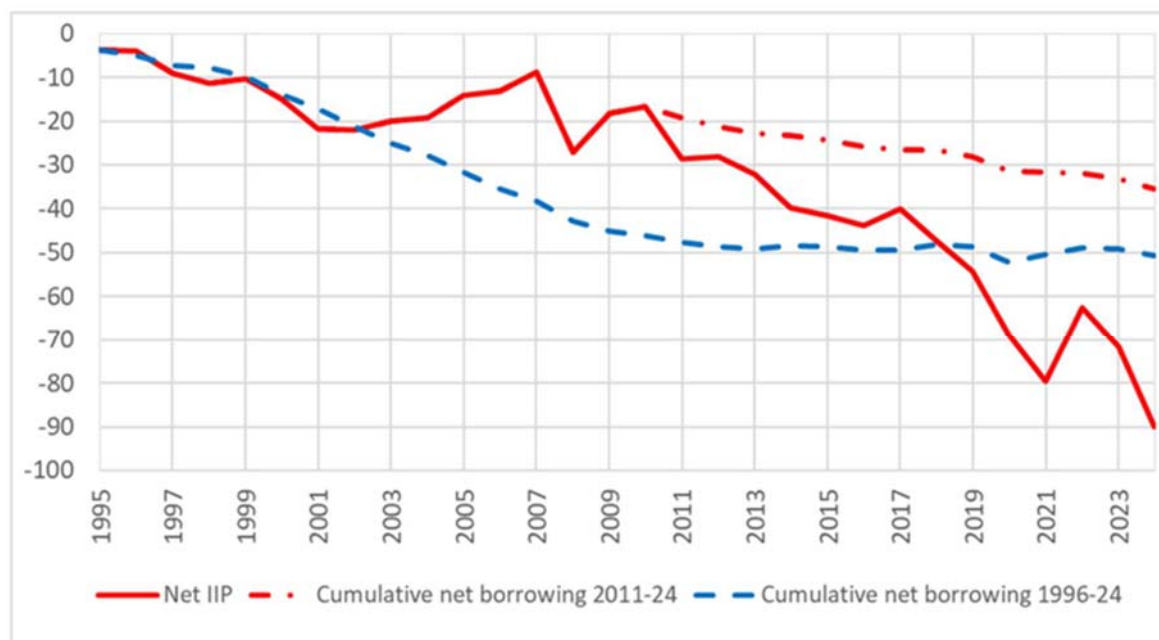
Source: IMF (2025a).

Externally, the US current account deficit, which hovered around 2% of GDP since the GFC, reached approximately 4% (USD 1.1 trillion) in 2024 (Fig. 4), while the net international investment position (NIIP), slightly negative already at the start of century, closed the year at a record low of USD 26 trillion (negative 90% of GDP; Fig. 5). As aptly observed, today's global landscape is characterized by numerous (relatively small) creditors and a single (very large) debtor (Milesi-Ferretti, 2023a; Fig. 6). That said, it is undoubtedly true that, since the turn of the century and its participation in the WTO, China has not only registered a continuously large current account surplus but has also become the United States' most important economic partner. Between 2000 and 2024 its bilateral cumulative surplus in net exports of goods was around USD 7 trillion.

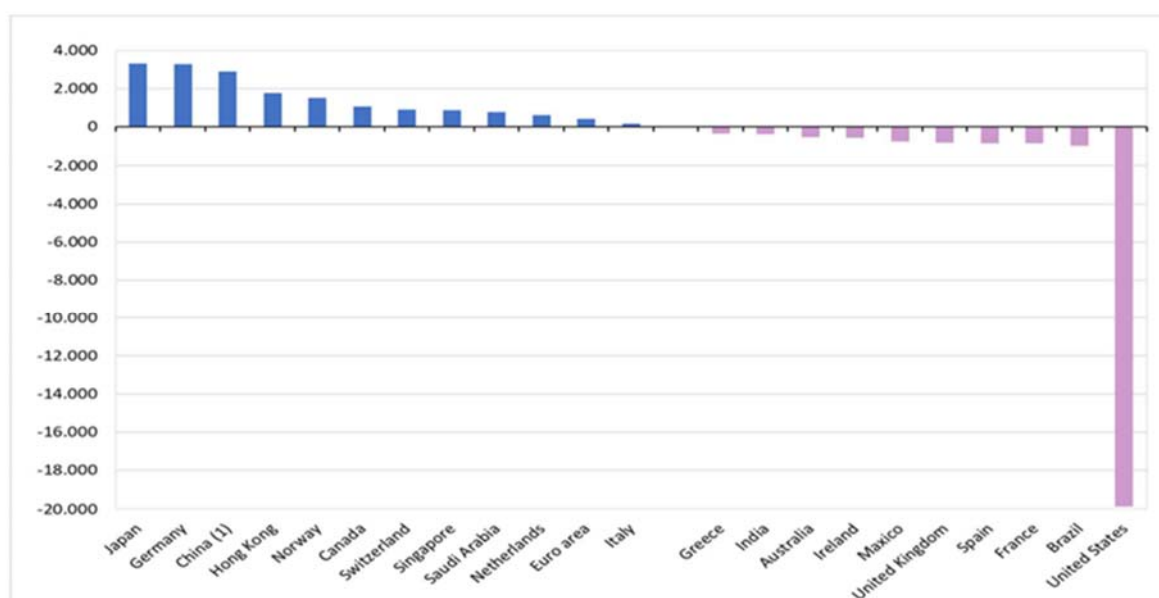
FIGURE 4 – *Current Account Balance*



Source: IMF (2025a).

FIGURE 5 – *International Investment Position of the United States (percent of GDP)*

Source: Milesi-Ferretti (2023a), updated by the author.

FIGURE 6 – *Net International Investment Positions (2023, billions of US dollars)*

Note: (1) China (excl. Hong Kong).

Source: Milesi-Ferretti (2023b).

This is certainly a significant factor in the United States' overall net financial position. However, it should be noted that this does not make China a major US "creditor". In fact, evidence shows negligible correlation between merchandise trade and financial exposure between the United States and its major trading partners. Clearly, by diversifying its financial activities abroad, China has distanced itself from the US by investing mainly in loans and direct investments in emerging and less developed economies. Therefore, China's substantial bilateral trade surplus is only reflected in a modest proportion of US net financial liabilities.

The case for the European Union (as well as for other countries such as Japan, the UK and Canada) is clearly different. Considering the Union as a whole, its current account only turned to surplus after the GFC. In the immediate aftermath of the crisis and during the sovereign debt crisis imports were somewhat limited due to low domestic demand. Later, exports performed relatively well, reflecting the strength of the manufacturing sector (first and foremost in Germany).

Two points are worth emphasising. First, of the United States' current account deficit of USD 1.1 trillion in 2024, only around EUR 50 billion stems from the bilateral trade imbalance with the European Union, which is made up of a goods surplus of EUR 200 billion and a services deficit of EUR 150 billion. Taking the income accounts into consideration, the euro area's overall bilateral current account with the United States is essentially balanced, reflecting negative net income from foreign direct investment.

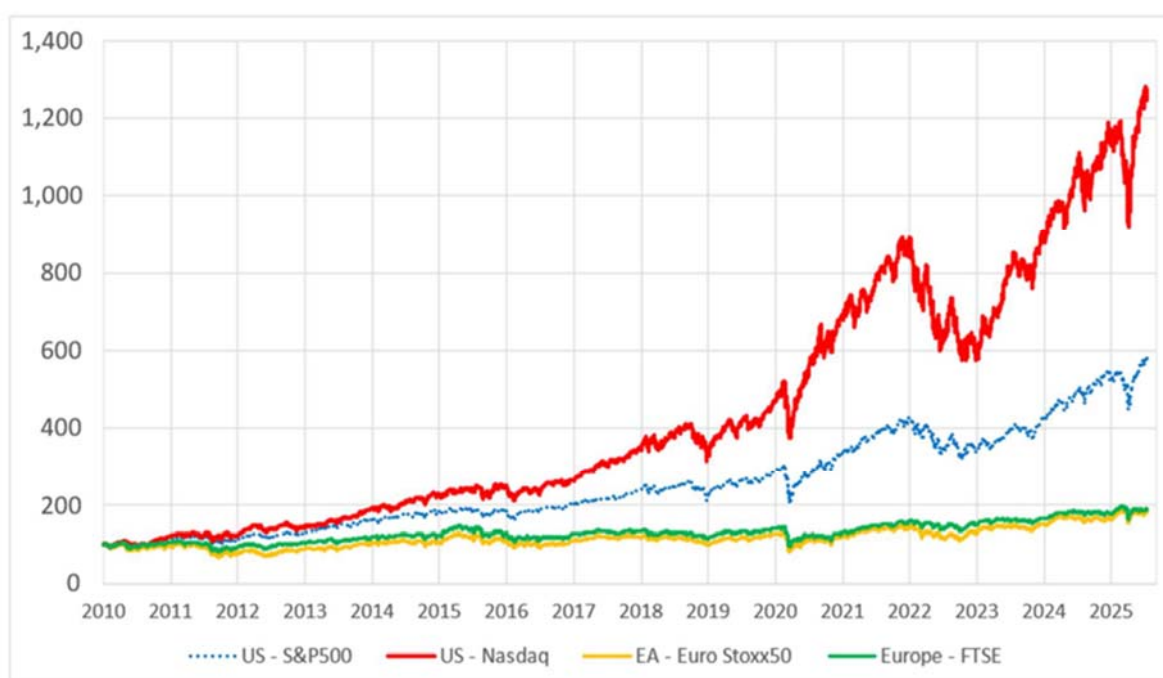
As we know, imports of services from the United States are highly significant for Europe. According to Eurostat, the bilateral services deficit has increased substantially over the past five years, a fact that is largely ignored by the corresponding US BEA statistics. ECB estimates (Emter *et al.*, 2025) attribute this mainly to the activity of US multinational affiliates in the euro area (especially in Ireland), which account for around 90% of the services deficit and 30% of the goods surplus. This largely results from charges for the use of intellectual property, such as patents and copyrights.

Second, the negative US NIIP stems from cumulative net borrowing due to the current account deficit, which had deteriorated to around 50% of GDP by the time of the GFC. Until then, extremely favourable valuation effects had masked an already unsustainable underlying trend (Visco, 2009). While cumulative net borrowing has remained high at around 50% of GDP since

2010, the dramatic increases in net value adjustments to the stock of assets and liabilities have accounted for most of the subsequent increase in the NIIP (in absolute terms).

Since 2011, about one-sixth of its deterioration, from 20% to 90% of GDP, is due to dollar appreciation. The remaining five-sixths are attributable to the extraordinary rise in the value of US corporate capital (equity and foreign direct investment), around 30% of which is held by non-residents, primarily in Europe and Commonwealth countries (Milesi-Ferretti, 2023a). From the end of 2010 to the end of 2024 US prices have increased by around 370%, compared to less than 25% in the rest of the world (Fig. 7). This is largely due to the exceptional performance of the US technology sector. Considering the so-called “Magnificent Seven”, the annual rate of return since 2015 has been an astonishing 38% (Tab. 1).

FIGURE 7 – *Stock Prices (end 2009=100)*



Source: Based on LSEG data.

TABLE 1 – *US Equity Returns: Magnificent Seven (M7) vs the Other*

	ALL	M7	Other
Cumulative			
31.03.2015-29.08.2025	216%	2,753%	131%
31.03.2015-31.12.2021	135%	1,286%	89%
31.12.2021-29.08.2025	35%	106%	22%
Annual			
31.03.2015-29.08.2025	11.6%	37.6%	8.3%
31.03.2015-31.12.2021	13.5%	47.6%	9.9%
31.12.2021-29.08.2025	8.5%	21.8%	5.5%

Source: Bloomberg US Large Cap.

M7 = Alphabet/Google, Amazon, Apple, Meta/Facebook, Microsoft, Nvidia, Tesla.

This is an indication of the strength, rather than the weakness, of the US economy, reflecting the significant innovation and capital investment that has occurred since the GFC, and continues to occur. However, the resulting exuberance in stock prices suggests a considerable rise in the market power and monopoly profits of these companies in the United States and beyond. This could lead to a reduction in social welfare (Atkeson *et al.*, 2025) and, in the long term, have negative consequences due to the weakening of innovative investment alongside an increase in monopoly rents, as foreseen by some (Acemoglu, 2025). Not to mention its current and prospective distributional effects.

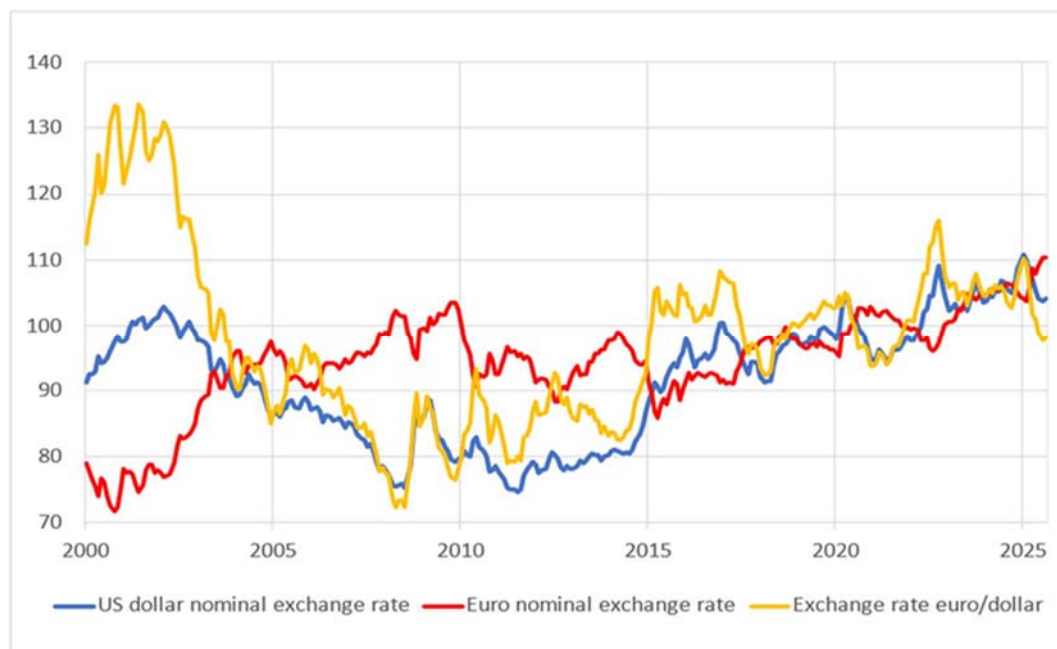
Anyway, the magnitude of these companies' actual and expected returns largely explains the flow and size of the capital they can attract, both domestically and internationally. The new US administration seems largely unconcerned by the extraordinary market power of the technological mega-corporations. In fact, it is vehemently complaining about the restrictions they are currently "forced" to face in their foreign operations. The objective of reducing trade imbalances through the imposition of "reciprocal tariffs", however defined, is discussed without ever mentioning the US balance of payments surplus for services (especially financial and technological) and the knowledge monopoly that largely underlies it. While the

confrontation between “open” science and the defence of intellectual property is certainly complex, the consequences in terms of market power could be significant and long-lasting and should not be ignored.

3. TRADE, TARIFFS AND DOMESTIC FACTORS

At the same time, the extremely low revaluation of the assets of US residents held in other economies reflects both the appreciation of the US dollar over the last fifteen years or so (Fig. 8) and the somewhat dismal performance of their equity markets. This may be an indication of the relative prospective weakness of those economies. In this respect I would highlight two considerations. First, regardless of the reasons behind the US administrations’ tariff policy, external imbalances are simply too large and will inevitably be reduced. This could potentially occur in a disorderly fashion, involving a reversal of the valuation effects, and a weaker US dollar. To some extent, and perhaps counterintuitively, the rise in tariffs has led to some depreciation of the dollar rather than the appreciation that economic theory and historical experience would suggest. This may be the result of the uncertainty and fears generated by the US domestic and international action, even if by historical standards the effective exchange rate depreciation is still limited. At the same time, the stock market remains bullish.

As far as trade imbalances are concerned, it is highly unlikely that they will be permanently resolved with tariffs, since they depend primarily on domestic policies. As has been repeatedly observed, the United States simply has an excess of investment over savings related to its fiscal stance (Obstfeld, 2025), and containing this does not appear to be among Mr Trump’s immediate objectives. Conversely, China has a substantial surplus of savings over investment due to its prolonged reliance on export-led growth. In the euro area and the European Union as a whole, the situation is perhaps less clear. Based on demographic and other considerations, the IMF currently estimates that overall, domestic demand in Europe should be higher (IMF, 2025b). However, the situation varies considerably across countries, and the figures are much smaller.

FIGURE 8 – *Effective Exchange Rates (2020=100)*

Sources: Bank for International Settlements and ECB.

In fact, the weakness so often attributed to Europe appears to reflect the low return on prospective investment channelled through capital markets more than the actual relative past performance of GDP *per capita*. As is clear from the Draghi and Letta reports (Draghi, 2024; Letta, 2024), and as I have discussed in more detail elsewhere (Visco, 2024, 2025a, 2025b), the economic and financial prospects of the European Union and its member states are unlikely to improve in the absence of a proper response to demographic, economic and financial challenges.

Starting with the demographics, the European population is ageing rapidly due to increased longevity and a dramatic reduction in births. While the world population has grown from approximately 5 billion to 8 billion over the past thirty years and is projected to reach 10 billion within the next thirty years, the EU population is expected to remain relatively stable at under 450 million (declining from 9% to 4% of the global population between 1990 and 2050). However, the working- age population (15–64) is set to shrink dramatically, with the old-age dependency ratio set to rise from one-third to around three-fifths. *Ceteris paribus*, this would have a substantial negative effect on *per capita* incomes.

Labour shortages can only be overcome through policies that raise the retirement age, increase labour market participation, and design immigration programmes to compensate for population decline. However, these policies will only be effective if they are accompanied by substantial improvements in the quality of human capital, which will require increased investment in education and knowledge from both the private and public sectors. Nevertheless, all this may still be insufficient to ensure the sustainability of public debt and the maintenance of the European welfare state – much valued in Europe and in need of improvement in many respects – without a significant increase in productivity levels. This calls into question the level and quality of R&D expenditure, and the efforts needed to close the European technological gap.

These efforts are clearly at the heart of Draghi's report. While the gap with the USA is not new and has been an issue throughout the decades of the European Union's development from the early days of the Common Market, its nature is different today. Over time, Europe has successfully imported, applied and developed US innovations at a sectoral level, as well as profitably exchanged manufactured goods and related services. However, innovations such as the internet, cloud computing and artificial intelligence are now general-purpose technologies affecting economies and societies, and none of them originates in Europe. There is a risk that much of the world, including Europe, will be left behind or face significant limitations on productivity growth and material well-being because of their dependency.

In fact, R&D trends in the European Union are not encouraging. Overall, the European Union spends more than one percentage point less of its GDP on R&D than the United States (2.3% vs. 3.4%), while China has already overtaken Europe (starting from below 1% at the beginning of the century). Moreover, where R&D expenditure is higher, it is mostly in traditional manufacturing sectors. Furthermore, the trend among companies with higher R&D expenditure is also negative. Of the 2,500 companies with the highest R&D investment (accounting for almost 90 per cent of the world's total expenditure), Europe's share is relatively low and decreasing: it is less than 18 per cent, compared to 40 per cent in the United States and over 18 per cent in China, which was still below 2 per cent in 2010.

4. EUROPE'S CHALLENGES AND THE ROLE OF THE EURO

In Enrico Letta's report, *Much More Than a Market*, the addition of a "fifth freedom" – the free movement of knowledge, research, and innovation – to complement the free movement of persons, goods, services and capital, is a very significant suggestion. Mario Draghi's *Report on European Competitiveness* takes it further, emphasising the need to overcome the twin deficits of investment and productivity. Together, the two reports present a compelling argument for a radical restructuring of Europe's institutional framework, which appears to be a very challenging undertaking. Indeed, the political feasibility of this is demanding, as it would involve removing fragmentation in key sectors such as energy, telecoms, defence and financial services, developing deeper capital markets, and establishing a fiscal framework oriented towards public investment and long-term growth.

Despite declarations of principle, the current divided Europe is the result of well-defined political choices supported by deep-rooted, albeit short-sighted, national interests. Moreover, and especially today, it is not obvious that the European Union and its member states should follow the same path as that which has underpinned the success of the American economy over the last quarter of a century. Nor would the process behind China's rapid progress and overtaking in several sectors offer much guidance to European democracies. In fact, current global developments suggest that attention to the need to preserving social cohesion mechanisms and addressing the distributional consequences of economic policy decisions must not be lost.

However, the truth is that, to maintain social stability and sustainability, the forces reducing the scope and size of our real economy must be counteracted. This cannot be achieved without the member states agreeing to drastically reduce fragmentation, particularly in capital markets, and to harmonise crucial legislation, such as that relating to commerce, company and insolvency laws, securities, banking and financial markets, intellectual property, employment and taxation. Adopting a code of business law incorporating a 28th regime would be a pragmatic – albeit perhaps questionable – way of overcoming the resistance to harmonisation. Member states should also reduce risk aversion in financial markets while maintaining safeguards to prevent fraud and improve transparency. At the same time, they must commit to providing more European public goods, which are considered crucial in sectors such as energy and defence, but which may also be required in other areas.

From this point of view, the reports may already have proved useful. The adoption of the *Competitiveness Compass* and the Communication on *A Simpler and Faster Europe*, as well as the publication of *The Single Market Strategy* and the *EU Startup and Scaleup Strategy*, seem to be moving in the right direction. The *State of the Union* address by the President of the European Commission to the EU Parliament on the 10th of September 2025 also appears to contain all the relevant messages and proposals. However, we must be realistic. Not only is there entrenched resistance to fiscal solidarity, deeper risk-sharing and treaty change, but there is also a renewed emphasis on domestic protection and economic security for individual member countries in Europe.

Indeed, projects and policies should be aligned with clear, well-communicated and feasible objectives. The dismal outcome of the “strategic goal for the new decade” set out by the 2000 Lisbon European Council’s should be born in mind. The objective was for Europe “to become the most competitive and dynamic knowledge-based economy in the world, capable of sustained growth with more and better jobs and greater social cohesion”: an overly ambitious and unattainable goal.

Perhaps too much attention has been given to the size of the investment needed to address Europe’s “competitiveness gap”, as suggested in the Draghi Report. However, it is not just a matter of investing more. In fact, total investment as a ratio to GDP in the European Union is no lower than in the United States. What is very different is its composition, with a substantial bias towards construction investment. While Europe’s energy and defence needs are undeniably pressing, higher investment in these sectors will not necessarily enhance growth.

From this perspective, where Europe’s shortcomings are particularly evident is in areas that matter most today, such as investment in intangibles (Gros *et al.*, 2024). When discussing imbalances, we have seen that imports of services are largely related to charges for the use of intellectual property. This is clearly the result of insufficient investment in R&D and, especially, an inability to encourage innovation and positive risk-taking in the private sector.

This raises the issue of fragmentation in the capital market and the obstacles that have impeded so far the establishment of an effective Capital Markets Union (CMU), despite the efforts of the past ten years. The objective to create a single market for capital and banking is now that of the Savings and Investment Union launched in May 2025, building on the CMU

and following the recommendations of the Letta and Draghi Reports, as well as those of the report written in the Spring 2024 by a committee of French experts chaired by Christian Noyer (Noyer *et al.*, 2024). However, it must be underlined that, while market fragmentation is high, there is a uniform tendency among Member States towards extremely limited retail participation. In the European Union, more than half of household savings are invested in real estate, compared to less than one third in the United States (Tab. 2). Not only is the share of financial wealth held as bank deposits and other liquid assets more than 30%, double that of US households, but the limited investment in capital markets is also mostly held in guaranteed products, such as life insurance. The assets managed by private non-bank intermediaries are also particularly low, perhaps suggesting that the wealthiest in the European Union are more risk averse than their American counterparts (Fig. 9).

TABLE 2 – *Household Asset Allocation (Q4 2024, percentage of total assets)*

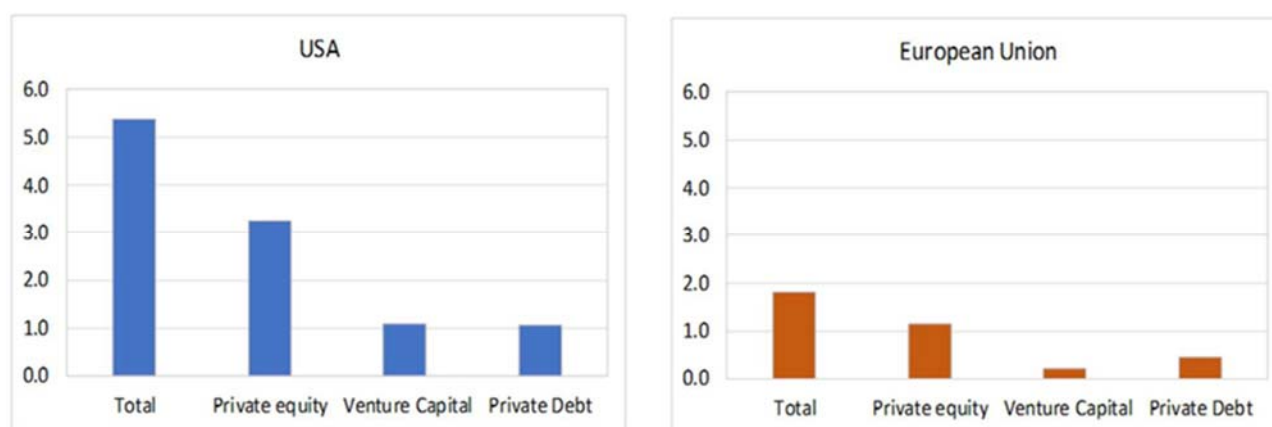
	USA	Euro Area
Real estate	31.0	54.9
Deposits+MMF	10.6	14.4
Capital markets + NLE (*)	55.8	27.7
Other (**)	2.6	3.1

Sources: ECB and FRB.

Notes: (*) It includes debt securities, listed shares, mutual funds, life insurance, pension funds and non-listed equity. For the European Union, non-corporate business wealth is not included.

(**) It includes other assets, derivatives, commercial credit and loans.

FIGURE 9 - *Assets Managed by Private Market Intermediaries*
(H1 2023 – trillions of US dollars)



Source: Preqin.

Not only is venture capital investment in Europe only one-sixth of that in the United States, but it also mostly originates from outside the region and is directed at established companies rather than new, innovative start-ups. Furthermore, despite much-improved transparency and regulation, the securitisation market still seems a long way from recovery following the GFC. The volume of US securitisations placed on the market is six times higher than that of the European Union.

The limited participation of retail investors in Europe's capital markets may be partly due to ageing and attitudes, as well as to the modest turnover of the distribution of wealth across generations. There seems to be fewer opportunities for new innovative and successful enterprises. Consequently, most of the financing is left to the banking sector, which, by its nature, cannot lend as freely or take as many risks as market participants can. The reality is that this market is too small and fragmented across national boundaries in Europe, and there is an urgent need to revise excessively cumbersome legislation that is possibly counterproductive. The establishment of an effective savings and investments union aimed at unifying European capital markets is an urgent endeavour.

The stalemate on institutional reforms that would allow progress to be made at a faster pace along the "long and winding" road to financial, fiscal and, eventually, political union is

hindering the acceptance of the results of recent academic exercises that suggest the possibility of a shift to a “euro-centric monetary system” (Hassan *et al.*, 2025). Even though the euro is still “a currency without state”, it is the linchpin of Europe’s sovereignty in the current union of national countries, as well as in the uncertain but possible future of progressive political unity. However, the euro remains institutionally vulnerable today, lacking a stronger real economy, a fully integrated financial system, and a fiscal union to support it. To this, we must add the difficulty to reform the EU decision-making process, which is largely entrenched in the requirement for unanimous voting.

Indeed, even if the US administration’s tariff campaign and other domestic and international initiatives were to erode the US dollar’s safety premium, it is unlikely that the euro’s role would change significantly until Europe develops a comparable safe asset market. The absence of such a market again reflects the incomplete nature of the European project and existing political divisions regarding the promotion of greater economic integration. It is preposterous to think that this will change within the timeframe of the expected US currency weakening.

5. PAYMENTS AND CURRENCIES

As suggested, perhaps the international monetary architecture will change in response to the rapidly changing global geopolitical landscape. This may lead to a period of higher financial instability, some shift away from the dollar as a safe asset and substantial changes to the rules of the game relating to the exchange of goods and services, capital movements and technology. What appears certain is that digitalisation will be a driving force behind this change.

One area in which this prospect is already becoming a reality is payments, both domestic and international. This is a complex field, outside the scope of these pages. It involves cryptocurrencies and stablecoins, central bank digital currencies, and digital platforms. It also involves what is happening at a regulatory level, where, on the other side of the Atlantic, the pendulum seems to be swinging back towards a less regulated financial system, which could lead to new liquidity and financial stability risks.

For the purposes of the discussion here, it should be emphasised that the weakening of the dollar as a reserve asset may not necessarily coincide with its weakening as a payment instrument. This is particularly pertinent in the context of the new international digital

payment system that could emerge from the developments following the *Genius Act* signed by President Trump in July 2025. Aside from the well-established risks of liquidity and financial stability associated with private currencies competing outside the control of monetary authorities, volatile in terms of both quantity and price, there are possible outcomes at the international level that still need to be well understood.

There are questions that need answering and which should prompt a European response, as recommended by the central banking community (Lagarde, 2025; Cipollone, 2024, 2025; Scotti, 2025). These questions are closely related to security, stability and monetary sovereignty. I will just advance a few queries: What implications might there be for liquidity in European markets if US stablecoins gain popularity among European consumers? What could the consequences be of deep interactions between US stablecoin issuers, digital platforms, technology firms and the US large banking intermediaries (who, incidentally, seem silent about the competition they will face on bank deposits)? Might there be risks to the placement of other countries' public debt if US stablecoins were to be backed by US Treasuries on a massive scale?

It is uncertain how a depreciation of the US currency, due to its weakened role as a safe asset, would affect the wider use of USD tokens on the global stage. Over time, new financial stability risks may have to be addressed by central banks in some way, as we have learned from the history of money, credit and finance. In the meantime, however, as previously mentioned, if the US currency loses traction due to tariffs and withdrawal from the international stage, the lack of safe assets for the euro and the absence of an established institutional framework for the renminbi (yuan) make it unlikely that a new "non-system" centred on currencies other than the dollar will be established. While the dollar's exorbitant privilege may be coming to an end under the Trump administration, it is not obvious that it would be a "privilege" for some single other currency to replace it, while we risk a lengthy period of international monetary disorder. There are no obvious global alternatives to this, other than ones based on renewed but unlikely international cooperation.

Does this mean that efforts in Europe to create a genuinely shared safe asset should not be stepped up? There are indeed good reasons to work in this direction. One reason is the need to reduce overall financing costs and increase the availability of private funds for investment

projects currently being discussed in Europe. These costs are kept high by the fragmentation of the single market, which especially affects sectors, such as financial and IT services, where economies of scale are particularly important. Further research is needed to determine the potential level of the benefits that could be obtained, but there are already indications that they could be significant (Panetta, 2025). The next issue would then be how to proceed.

One proposed solution is to create a market for true European public debt by transferring part of domestic debts to a common fund totalling a substantial amount (Blanchard and Ubide, 2025). This would establish a deep, liquid and permanent euro market of, say, around EUR 5 trillion (the difference between the current level of debt in the euro area and the amount corresponding to 60% of euro area GDP). This idea has recently received significant media attention. Building on similar proposals put forward in the aftermath of the GFC, it has somehow disappeared from policy discussions. A detailed analysis of a proposal identical to the one just advanced can be found in a paper written by Bank of Italy economists prior to the Covid-19 crisis (Cioffi *et al.*, 2019). Moral hazard risks can be adequately managed, and the proposal could be implemented within the legal framework of the EU Treaties (Maiocchi, 2025).

In essence, to repeat what was said a few years ago, building upon considerations related to the financing of the NGEU, “it would make a significant contribution to strengthening the stability of the euro area as a whole and to creating a supranational public sector bond market of adequate depth and liquidity, with positive effects also for the completion of the banking union and the capital market union. The activity of this kind of European fund would be structured in such a way as to avoid the systematic transfer of resources from one country to another and to maintain the incentives to conduct fiscal policy responsibly” (Visco, 2022).

6. EUROPE’S RESPONSE

The economic and financial implications of the new global landscape are too significant to ignore. These are closely linked to political developments, and Europe cannot afford to be a marginal player. Of course, there are actions to take that appear to be unrelated to what is taking place on the international front, even though it will be impossible to ignore this. I believe the issue is not what should be done based on the groundwork set out in the Draghi and

Letta reports, but what could be done today with a reasonable chance of success, provided it is presented well to the political audience and the public at large.

Substantial progress could be made in terms of the internal market, domestic research, and technological innovation. This could also serve as a response to the aggressive commercial and political threats posed by the US administration. However, regardless of this, the single market should be simplified and streamlined in many respects, and new, improved channels for financing innovation should be established.

There is an urgent need to find common responses to common challenges. For instance, in view of the risks associated with fragmented payment systems, proposals for the creation of a digital capital markets union should be given careful consideration. Above all, it must be recognised that the functioning of the single market is a collective responsibility and that member countries should be active proponents, rather than passive – and often *a priori* critical – recipients, of the European Commission's proposals.

One costly solution for the Union would be to close itself off. A better approach would be to seek more reasonable and friendly trade partners than its main North Atlantic ally. However, the chosen response of negotiating to limit the damage resulting from the threats on tariffs is subject to uncertainties linked to the ambiguities of the American counterpart's requests and decisions. The situation is still fluid, and it cannot be ruled out that the European Union will reciprocate by raising tariffs on specific American goods.

It is debatable whether this could also involve EU imports of US services, particularly from major technology companies. Essentially, higher taxes on these services would lead to higher consumer prices, and there would be no obvious alternatives in EU countries. Nevertheless, direct dialogue with these companies should be encouraged, as should joint ventures. However, one thing that must be ruled out is abandoning regulations aimed at safeguarding individual and collective security, reducing excessive market power, and promoting transparency and consumer protection.

At the same time, thorough discussions should aim to reach an agreement on the "common goods" on which the European Union should invest directly to reduce its major external dependencies. Alongside energy, my list would include satellites, telecommunications, the

cloud and improved public–private coordination on artificial intelligence and quantum computing. There is much to be gained, and it is probably not too costly to define new programmes aimed at financing basic research centres and attracting scholars and researchers who are currently looking for better locations with the financing of specific new programmes.

Finally, global challenges are not going to disappear. They cannot be ignored because some are unwilling to cooperate. The short-sightedness of a few cannot become the norm for everyone, because all would suffer. While severe trade impediments, such as tariffs and non-tariff barriers, and a return to a fragmented world would be costly for advanced economies, they would be disastrous for the developing world. In fact, most of the two billion people expected to be added to the current world population in the next thirty years will reside there. Rather than containing migration flows, a less open world might see an increase in their numbers, and an increase that would be completely unmanageable.

The coming years will therefore be turbulent. Global uncertainty is likely to remain high, and volatile markets could reduce growth and well-being. The international trade system and the international monetary system should not be left in a permanent state of disorder. Other than one based on renewed, reasonable and pragmatic international cooperation – perhaps in the form of “coalitions of the willing”, as some are suggesting – I can’t see any obvious global alternatives. We should probably start addressing individual issues while respecting existing national sovereignty, with the only unavoidable condition being fundamental respect for the founding principles and values of peaceful coexistence between nations.

In these challenging times, establishing a dialogue between distant and different political and social systems will be difficult. However, there are also common global challenges, such as climate change, pandemics, demographic pressures, extreme poverty, digital risks and disruptive conflicts, which cannot be overcome in isolation. Although Europe is still developing its institutional setup in many respects, it cannot be denied that it has a special interest and an inevitable responsibility in maintaining an open dialogue and keeping the flame of international cooperation alive.

REFERENCES

- Acemoglu, D. (2025), “After the American Century”, *Financial Times, Life and Arts*, February 9, <https://www.ft.com/content/4e3f1731-3d63-4b31-88ce-c3f5157d8170>
- Ahir, H., N. Bloom and D. Furceri (2022), “The World Uncertainty Index”, NBER Working Paper Series No. 29763, <https://doi.org/10.3386/w29763>
- Atkeson, A., J. Heathcote and F. Perri (2025), “The End of Privilege: A Reexamination of the Net Foreign Position of the United States”, *American Economic Review*, 115(7), 2151-2206, <https://doi.org/10.1257/aer.20230732>
- Blanchard, O. and Á. Ubide (2025), “Now is the Time for Eurobonds: A Specific Proposal”, *Realtime Economics*, Peterson Institute for International Economics, 30 May, <https://www.piie.com/blogs/realtime-economics/2025/now-time-eurobonds-specific-proposal>
- Cioffi, M., P. Rizza, M. Romanelli and P. Tommasino (2019), “Outline of a Redistribution-Free Debt Redemption Fund for the Euro Area”, Banca d'Italia, Questioni di economia e finanza (Occasional Papers) No. 479, <https://doi.org/10.2139/ssrn.3432516>
- Cipollone, P. (2024), “Towards a Digital Capital Markets Union”, Keynote speech at the Bundesbank Symposium on the Future of Payments, Frankfurt, 7 October, <https://www.ecb.europa.eu/press/key/date/2024/html/ecb.sp241007-cc903db51d.en.html>
- Cipollone, P. (2025), “Preparing the Future of Payments and Money: The Role of Research and Innovation”, Keynote speech at the conference “The Future of Payments: CBDC, Digital Assets and Capital Markets”, Bocconi University, Milan, 26 September, <https://www.ecb.europa.eu/press/key/date/2025/html/ecb.sp250926-e856d2e386.en.html>
- Davis, S.J. (2016), “An Index of Global Economic Policy Uncertainty”, NBER Working Paper Series No. 22740, <https://doi.org/10.3386/w22740>
- De Cecco, M. (1974), *Money and Empire: The International Gold Standard, 1890-1914*, Basil Blackwell: Oxford.
- Draghi, M. (2024), *The Future of European Competitiveness*, European Commission, Brussels, September, https://commission.europa.eu/topics/competitiveness/draghi-report_en
- Emter, L., M. Fidora, F. Pastoris, M. Schmitz and T. Schuler (2025), “US Trade Policies and the

- Activity of US Multinational Enterprises in the Euro Area”, *ECB Economic Bulletin*, 4, https://www.ecb.europa.eu/press/economic-bulletin/focus/2025/html/ecb.ebbox202504_02-b993bf44eb.en.html
- Gros, D., P-L. Mengel and G. Presidente (2024), “What Investment Gap? Quality Instead of Quantity”, Institute for European Policymaking@Bocconi University Policy Brief No. 22, <https://iep.unibocconi.eu/publications/policy-briefs/policy-brief-n22-what-investment-gap-quality-instead-quantity>
- Hassan, T.A., T.M. Mertens, J. Wang, and T. Zhang (2025), “Trade War and the Dollar Anchor”, *Brookings Papers on Economic Activity*, Fall, <https://doi.org/10.3386/w34332>
- Hirschman, A. (1945), *National Power and the Structure of Foreign Trade*, University of California Press: Berkeley and Los Angeles, <https://doi.org/10.2307/jj.15976659>
- IMF (2025a), *World Economic Outlook Database*, International Monetary Fund, April, <https://www.imf.org/en/publications/weo/weo-database/2025/april>
- IMF (2025b), *External Sector Report. Global Imbalances in a Shifting World*, International Monetary Fund: Washington, DC, Imf (2025): <https://www.imf.org/en/publications/esr/issues/2025/07/22/external-sector-report-2025>
- Lagarde, C. (2025), “Speech at the Hearing of the Committee on Economic and Monetary Affairs of the European Parliament”, Brussels, 23 June, <https://www.ecb.europa.eu/press/key/date/2025/html/ecb.sp250623-fd501a6cab.en.html>
- Letta, E. (2024), *Much More than a Market. Speed, Security, Solidarity*, European Commission, Brussels, April, <https://www.consilium.europa.eu/media/ny3j24sm/much-more-than-a-market-report-by-enrico-letta.pdf>
- Maiocchi, A. (2025), “Financing European Expenditures with the Issuance of Union Bonds”, *Fondazione CSF, Policy Papers, New Series N. 002*, June, https://www.fondazionecsf.it/images/2025/PP2025/PPNS002EN_AM.pdf
- Milesi-Ferretti G.M. (2023a), “Many Creditors, One Large Debtor: Understanding the Buildup of Global Stock Imbalances after the Global Financial Crisis”, *The Brookings Institutions, Hutchins Center Working Paper No. 90*, December, <https://doi.org/10.1057/s41308-023-00229-4>

- Milesi-Ferretti, G.M. (2023b), “External Wealth of Nations Complete Update”, Brookings, 13 January, <https://www.brookings.edu/articles/external-wealth-of-nations-complete-update-2023/>
- Noyer, C., D. d’Amazrit, N. Calcoen, F. de Coutrois, M. Kallala, B de Mazières, R. Ophèle, A. Pointet (2024), Developing European Capital Markets to Finance the Future. Proposals for a Savings and Investments Union, Economy and Finance Ministry, Paris, April, <https://www.tresor.economie.gouv.fr/Articles/2024/04/25/developing-european-capital-markets-to-finance-the-future>
- Obstfeld M. (2025), “The U.S. Trade Deficit: Myths and Realities”, Brookings Papers on Economic Activity, Spring, <https://doi.org/10.1353/eca.2025.a978548>
- Padoa-Schioppa, T. (2004), The Euro and its Central Bank. Getting United after the Union, MIT Press: Cambridge, MA, <https://doi.org/10.7551/mitpress/2846.001.0001>
- Panetta, F. (2025), “Finance and Innovation for the Future of the Economy”, Keynote speech, Annual Meeting, Italian Banking Association, Milan, July 11, <https://www.bancaditalia.it/pubblicazioni/interventi-governatore/integov2025/20250711-panetta/index.html>
- Scotti, C. (2025), “Stablecoins in the Payment Ecosystem: Reflections on Responsible Innovations”, Welcome address, Economic of Payments XIV Conference, Banca d’Italia, Rome, 18 September, <https://www.bancaditalia.it/pubblicazioni/interventi-direttorio/int-dir-2025/20250918-scotti/index.html>
- Visco, I. (2009) “The Global Crisis – the Role of Policies and The International Monetary System”, in G20 Workshop on the Global Economy, *Macroeconomic Causes of the Crisis: Key Lessons*, Co-hosted by the Reserve Bank of India and the Bank of England, Mumbai, 24-26 May, <https://www.bis.org/review/r090715e.pdf>
- Visco, I. (2022), “The Governor’s Concluding Remarks”, Bank of Italy, Annual Report for 2021, Rome, 31 May, https://www.bancaditalia.it/pubblicazioni/interventi-governatore/integov2022/en-cf_2021.pdf?language_id=1
- Visco, I. (2024), “Un futuro per l’Europa. Demografia, tecnologia, mercato”, *il Mulino*, 2/24, <https://www.rivistailmulino.it/isbn/9788815423191>
- Visco, I. (2025a), “On Economic and Financial Imbalances in the New Geopolitical Framework”, *PSL Quarterly Review*, 78(313), 161-179, <https://doi.org/10.13133/2037-3643/18997>

Visco, I. (2025b), “Europe’s New Challenges in an Unbalanced World”, *Bancaria*, 9/2025, <https://bancaria.it/en/livello-2/archive-2/last-summary/september-2025/europes-new-challenges-in-an-unbalanced-world/>