Review of Social Economy

ISSN: (Print) (Online) Journal homepage: https://www.tandfonline.com/loi/rrse20

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To cite this article: Stefano Merlo (2023) Self-fulfilling crises in the Eurozone and the institutional preconditions of republican sovereignty, Review of Social Economy, 81:1, 130-153, DOI: 10.1080/00346764.2022.2117401

To link to this article: https://doi.org/10.1080/00346764.2022.2117401

REVIEW OF SOCIAL ECONOMY
2023, VOL. 81, NO. 1, 130–153
https://doi.org/10.1080/00346764.2022.2117401

Self-fulfilling crises in the Eurozone and the institutional preconditions of republican sovereignty

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ABSTRACT
The normative vocabulary of republican political theory can be fruitfully applied to evaluate the phases of market turbulence in sovereign debt markets witnessed during the Eurozone crisis. A view of justice that requires the minimisation of dominating relationships between agents highlights how the institutional preconditions of undominated sovereignty were lacking in the Eurozone. The agreed-upon structure within which countries operated fuelled self-fulfilling market movements in sovereign bond markets, which bear the hallmark of unjust domination as weaker Member States formed a social relationship with investors over which they did not have meaningful control. In motivating the thesis, the paper touches upon the recent debates on the sources and site of domination and on the stance, republican scholars should take toward competitive markets. Given this diagnosis, Eurozone countries have an obligation to establish supranational institutions that increase private and public channels of risk-sharing.

ARTICLE HISTORY Received 17 February 2021; Accepted 17 August 2022

KEYWORDS Republicanism; Eurozone crisis; financial markets; non-domination; sovereignty

Introduction

What does it mean to be sovereign in a monetary union and, more in general, in a globalised world? To better grasp what an answer to this question involves, this article proposes to zoom in on the Eurozone crisis, its institutional causes and some of its most visible repercussions, namely the phases of market turbulence experienced by periphery countries. My claim is that republican theory – specifically a view of justice that requires the minimisation of dominating relationships between agents (Pettit, 2014, xxii) – helps us to attain a precise appreciation of the normative problems involved when market movements display the kind of self-fulfilling characteristics seen during the Eurozone

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crisis. In turn, this analysis suggests that sovereignty, understood in a republican sense, cannot be sustained in a monetary union without appropriate risk-sharing institutions.

More precisely, the main argument is that the institutional framework within which Eurozone countries operated before the crisis has led to the decoupling of public authority from citizens' control. Domination, being structurally embedded in the incomplete construction of the monetary union, has been activated under conditions of crisis via sovereign bond markets, who thus act as a vehicle of this injustice. In practice, domination was inherent in the agreed structure of the monetary union, as it facilitated a self-fulfilling liquidity crisis, in which weaker member states found themselves part of a social relationship vis-à-vis investors over which they had no meaningful control. Weaker countries' position of disempowerment towards financial markets can be traced back to the coexistence of three institutional characteristics, namely, the lack of a lender-of-last-resort in the sovereign bond market, the lack of a banking union and the absence of co-responsibility for public debt. In turn, it will be claimed that the sovereign debt crisis exposed a level of collective responsibility in the set-up of EMU that is not appropriately met by corresponding institutional duties.

Given republican scholars' belief in the usefulness and feasibility of implementing the republican institutional program at the international level (Laborde & Ronzoni, 2016; Pettit, 2015), this analysis attempts to flesh out more precisely how republican principles can be used to evaluate current events. While this conception of unfreedom and injustice (Pettit, 2014, xxii) is epitomised by the relationship between a master and his slave, it is probably harder to appreciate how it materialises at the international level and in the world of finance (Herzog, 2019; Preiss, 2018 offer interesting applications of the republican vocabulary to global finance). Nevertheless, in analysing the position of Eurozone countries, the argument builds on the characteristically republican intuition that freedom corresponds to the capacity to control the terms of the social relationships one is part of, rather than to the availability of options to choose from. In turn, the focus is on the institutions that structure social relationships and, in this case, on the uneven construction of the Eurozone.

The analysis deviates from the classic slave-master case, since it considers the non-intentional behaviour of a multitude of agents, in this case, investors in sovereign bond markets, as dominating. At the same time, by focusing on a specific social relationship, the diagnosis remains distinctly republican and falls short of adopting the normative vocabulary of theories of structural injustice (Young, 2006). Indeed, the claim is that Eurozone countries formed a problematic relationship with sovereign bond markets, one which can be labelled as a socially constituted and systemically arbitrary form of domination (Blunt, 2015).

In turn, the attitude republican scholars should have with regard to competitive markets in general (Taylor, 2013) and international finance in particular (Preiss, 2018) should be reconsidered. Political theorists in this tradition have focused too narrowly on individual market power as evidence of domination and too little on how markets are structured and which institutions sustain them. In other terms, if domination can be socially constituted and systemically arbitrary, then certain market phenomena that can be described as collective action problems deserve the attention of republican scholars.

Crucially, the way goods and financial markets are structured and the institutional framework that sustains them is the result of political decisions that result in different distributions of power between consumers and producers, investors and savers. Therefore, in line with the republican suggestion that abolishing slavery, rather than punishing masters, is the right response in the face of problematic power asymmetries, the argument concludes by claiming that member states have a duty to reform the EMU. Responding to this injustice is not about sanctioning investors in sovereign bond markets or blaming other member states, but about building the institutional preconditions of undominated sovereignty. This means the establishment of supranational risk-sharing institutions that prevent self-fulfilling capital market flows from arising in the first place.

The article is organised as follows. Section 2 briefly outlines the theory of non-domination, as put forward by Philip Pettit and suggests that a republican justification of the EU can pivot around its promise to make markets more competitive while preserving the collective freedom of its member states. Adapting Ingham and Lovett's (2019) argument, I then respond to a potential objection to the idea that eliminating the capacity for arbitrary domination in a market setting may be too demanding and even unfeasible.

Despite this defence of the republican institutional program, the subsequent sections aim to show that republicans' support of competitive markets rests on shaky foundations. To this end, Section 3 describes the Eurozone sudden-stop crisis as an example of domination. Even if investors do not have individual market power, nor are they to blame for their actions, they were able to collectively impose a dominating relationship over EU governments. This shows that domination can be systemic and not depend on the will of a single agent (Section 4). In section 5, I defend this argument, partially with the help of a game theoretical model of domination, against two objections: the first is that if investors can dominate a government then republican freedom is too demanding a conception; the second is that even if domination occurred Member States have entered in this institutional arrangement in an undominated way. This last objection leads to the issue of responsibility for injustice. I conclude by arguing that there is a level of co-responsibility for upholding this system that is not met by appropriate institutional duties and that grounds a political obligation to create new channels for sharing risk between members of the Economic and Monetary Union (EMU).

Republicanism: robust freedom at the international level

Republican political theory distinguishes itself from liberalism by contesting the idea that freedom is the absence of interference. The difference between the two schools of thought is made clear by the oft-cited example of the slave and the master. A liberal would not define a slave who has a benevolent master as unfree, since this kind of master would not interfere with her choices. Republicans argue instead that the master still has the capacity to arbitrarily interfere with the slave as she sees fit, thus making her unfree (Pettit, 1999a, 1999b, p. 165).

Republican freedom is a 'robust' conception, in the sense that the possibility of agent A arbitrarily interfering with agent B is enough to make B unfree. An arbitrary power is then one that fails to track the interests of those subject to it (Pettit, 1999a, 1999b). This happens when individuals do not have a say in the terms of the social relationship they are in and they lack meaningful control over the choices they can make as a result of their position of disempowerment. Crucially, what is problematic about domination is not the restriction of choice *per se* but the denial of status that this lack of control over social relationships implies. Simply put, the slave suffers an injustice, not because his options are limited, but because the institution of slavery strips him away of any social standing. Republicanism's insistence that the possibilities for arbitrary interference are created and supported by formal and informal institutions, which may be complex in their construction and involve the active and passive actions of many agents, thus places the theory close to Young's account of structural injustice.[1] The intimate link between the status of free and equal people, the ideal of non-domination and its institutional preconditions has allowed republicans not only to define what unfreedom is, but also to ground a conception of justice (Laborde & Ronzoni, 2016; Pettit, 2014; Lovett, 2010a, 2010b). Indeed, a just society and a just state should aim at minimising domination as a matter of right (Lovett, 2010a, 2010b).

Republican theorists also argue that the eradication of domination can be a plausible and implementable (Pettit, 2015) guiding idea to structure global institutional arrangements. The ultimate goal is often summarised using Pettit's slogan: 'the state ought to be internationally undominated, domestically undominating defender of its citizens' freedom as non-domination' (Pettit, 2012a, 2012b, 2012c, p. 19). This three-dimensional picture thus has at its core

[1] Some republican scholars have recently argued that domination can actually be described as a form of structural injustice (Gädeke, 2021). In this article, I stick to the republican notion of domination as it underlines that (even if it may come to be embodied in institutions) domination can eventually be reduced to concrete social relationships.

the concern for individual freedom, which can only take place if citizens enjoy status equality through the democratic control of their state. In turn, the state requires, not only institutions that are non-dominating towards its citizens, but that is itself not dominated by external actors, such as other more powerful states, transnational corporations, but also global monetary and trade institutions. In short, citizens' free status vis-à-vis each other can only be guaranteed if they collectively, and therefore as a people, also enjoy a similar kind of status as part of the international community.

But what does the objective of providing 'each people with a collective version of individual freedom' (Pettit, 2015, p. 38) actually imply for the design of international institutions? This can be a hard question in the case of a complex governance system like the EMU, in which members' cooperation over multiple policy areas creates deep interdependencies as well as externalities. In principle, a republican justification (see Bellamy, 2019; Zimmermann, 2019; Collignon, 2017 for more complete applications of the republican paradigm to the EU) of the over-arching economic rationale of the EMU – namely the smooth functioning of a common European market for goods and services – can be made with reference to the idea that a level-playing-field and sufficiently strong competitive forces help reduce the potential sources of domination associated with market concentration and countries' trade policies. Indeed, the EU's market friendly ethos squares well with the argument proposed by Taylor (2013) in support of competitive markets. He writes that

> the right republican attitude toward competitive markets is celebratory rather than acquiescent and that republicanism demands such market for the same reason that it demands the rule of law: because both are essential institutions for protecting individuals from arbitrary interference. (Taylor, 2013, p. 593)[2]

Borrowing Taylor's terminology, one can say that the arbitrary interferences that the EU's founding fathers were trying to limit were, for instance, the beggar-thy-neighbour trade policies used to favour specific industries at the expense of consumers, both national and foreign.

From a republican perspective, competitive markets promise to represent a sort of agentless mechanism to deal with situations of scarcity; they guarantee the dispersion of power between consumers and producers, so that no one can be said to meaningfully control the outcomes of the impersonal forces of supply and demand. The market can thus perform the same function as constitutional provisions – what Lovett and Pettit called 'an empire of law' (12) – since it guarantees that authority does 'not rest with a single unlimited center of power' (Lovett & Pettit, 2009, p. 22). Republicans' endorsement of competitive markets can be best explained by reference to the distinction between what Pettit (2012a, 2012b, 2012c, p. 38) calls a 'vitiative' hindrance and an 'invasive'

[2] For a different republican view on markets, see Anderson (2015), Arnold (2017), Gourevitch (2015) and MacGilvray (2011)

hindrance. The latter entails domination since it describes a kind of interference exercised by an agent over another which limits the choices available or their expected payoff. The former is instead the kind of restriction for which no person is directly responsible and is therefore more similar in nature to the result of a natural process. Pettit further maintains that only invasive hindrances on freedom should be a matter of public concern since they reflect an agential abuse of power that is fundamentally inimical to republican's supreme value. In theory then a perfectly competitive market, by making both consumers and producers price-takers, guarantees that the kind of forces shaping individual decisions and economic outcomes will be similar in kind to those exercised by natural phenomena, for which we do not feel resentment and gratitude.[3]

Once again, a crucial element is that the claim to non-domination of both states and citizens must be robust, in the sense that the enjoyment of republican freedom must be possible, not just 'in the actual world, but also in a range of nearby possible worlds' (List & Valentini, 2016, p. 1048). Yet one might rightly ask, how expansive an interpretation should we give to this robustness condition? In other terms, when are the powers of potential dominators sufficiently constrained? The risk is that a broad interpretation of this requirement would make a theory of institutional design inspired by republican principles hopelessly demanding and, therefore, impossible to attain in practice. Indeed, if the mere capacity for arbitrary interference is normatively problematic, then most states that take part in the tariff-free area that the EMU supports seem to be at the mercy of other powerful external forces and redressing this may be far too burdensome. For instance, a large company (or group of companies) that fully exploits the advantages of the Single Market has the possibility of arbitrarily interfering with a government by threatening to halt its production (thereby causing severe economic damage to the local economy) if the same government does not put in place some business-friendly measures. While competitive markets should normally ensure that such a strategy is not economically viable in the long run, it is possible to imagine that certain types of CEOs at the top of the corporation would be so committed to this course of action and so devious to try to strong-arm the government into doing as it wishes. If this is a real possibility, so the argument goes, then domination seems to be ubiquitous so that minimising it becomes too burdensome and international interdependence appears to inherently incompatible with republican principles.

An interesting reply (which will be useful for this argument as well) to this objection has been provided by Ingham and Lovett (2019) by borrowing some ideas and concepts from game theory. They show how the existence of a particularly deranged (or bullish) type of agents willing to interfere with the lives of

[3] Highlighting the republican justification of this ideal state should not detract from the more important point that in practice the existence of domination is not a yes/no proposition. Hence, the goal of minimising, rather than eliminating it. I thank the anonymous reviewer for highlighting this.

others – or, in our case, of large companies threatening governments to relocate or else – does not pose a problem for the theory as a whole. Under this 'Moderate Republicanism' and if markets are perfectly competitive, these types of company CEOs should be 'justifiably ignorable', in the sense that if a government knew that they do not have such deranged type (that would be willing to bear the cost of intervention), it would not try to ingratiate itself with the Company. The idea behind this is that if it became common knowledge that this CEO is of a type that would want to intervene, the government would modify its behaviour in order to convince him/her not to intervene (the representation of this game three is in the Appendix).

Conversely, if markets were not fully competitive (and the cost of interference was low), the types of CEOs that would want to interfere could not be regarded as 'justifiably ignorable', because the Government would act differently if it became known that the CEO is not of that type. The Government would not try to ingratiate itself with the Board of Directors of the Company.

We can thus conclude this section by noting that, republicanism need not be seen as hopelessly demanding. Even if some companies may – thanks to the benefits offered by the EU Single Market – have the possibility to arbitrarily interfere with democratically elected governments, these types should be regarded as justifiably ignorable, as long as markets are perfectly competitive. In other terms, the basic republican argument for competitive markets and its prima facie support of the EMU's rationale seems to be holding its ground: if individual market power is minimised then competitive markets deliver their promise of eliminating domination (Taylor, 2013).

In the next sections, I aim to show that this thesis is incomplete. In contrast to the analysis put forward by Taylor, I will identify a form of domination in market processes that does not display any abuse of market power and in which no individual market participant can impose her preferred price. What this thesis is missing is a proper consideration of the institutional embeddedness of markets and the way in which this institutional embeddedness can give rise to seemingly agentless mechanisms that nevertheless impose dominating relationships.

Self-fulfilling crises and republican sovereignty

The ideal of non-domination and republican sovereignty imposes quite important demands on the institutions (national and supranational) that shape and structure social relationships. At the national level, this ideal suggests that citizens should be equal controllers of the actions and policies of their state, as this is the only way for them not to see the necessary interferences that the state's authority imposes as a form of alien power (Pettit, 2012a, 2012b, 2012c). In turn, only democratic procedures and the dispersion of powers they imply can fulfil the republican desiderata.

Unfortunately, at the international level, the nexus between individuals' status as free citizens and their capacity to control public authority can be weakened, especially when – as in the case of the EMU – some of the traditional powers of states come to be shared with other polities. The creation of a common market for goods and services put an end to the power of states to set tariffs and quota and empowered supranational institutions to set the rules for a level-playing-field. The promise (and desire) of an efficient common market then paved the way for monetary integration and the attempt to create a stable currency that could fulfil the same functions as national currencies did, but also foster the creation of a European capital market. Much like in the goods market's case, the policy area became a supranational competence and countries relinquished the control of monetary aggregates to a highly independent Central bank tasked with a narrow mandate to fight inflation.

As a result, not only has European citizens' control over (monetary) executives' decisions been weakened, but this institutional framework has also proved dysfunctional, since it fuelled highly asymmetric credit flows from the centre to the periphery of the Union. The integration of monetary functions (in particular, the function of money as a store of value and means of deferred payment, see Zimmermann, 2019, ch.8) allowed periphery countries to access a larger pool of liquidity to finance higher levels of investment. Crucially, the adjustment mechanisms that before the advent of the euro would have led to a devaluation of periphery countries' currency and an increase in their exports, were not present, nor did these flows lead to high enough inflation in core countries to reduce their momentum. By 2008 core countries had financed dangerously high levels of investment in the periphery. The stage was set for the upcoming sovereign debt crisis.

The incompleteness of the EMU institutional framework was put on display as the 2008 financial crisis spread to Europe and the current account deficits that periphery countries had accumulated since the introduction of the Euro appeared harder to finance through inter-bank lending (see Zimmermann, 2019, chapter 9). Between March 2008 and March 2009, Ireland and Greece saw an abrupt outflow of capital that quickly translated into pressures in the bond market (Baldwin et. al, 2015). The spring of 2010 marked the beginning of a second sudden-stop crisis, following the agreement between the EU and the IMF on the Greek programme. Greece and Ireland were caught up in the spiral again and market turbulence spread to Portugal, while at the end of 2011, it was Spain and Italy's turn to witness the power of a change in market confidence in the third and final episode (Merler & Pisani-Ferry, 2012).

Investors perceived periphery countries as being unable to repay their obligations, or obtain help from supranational institutions, since the ECB's statue (Article 123(1) FFEU) prohibited it from buying member states' government bonds. This meant that investors knew that no one was there to repay them if the situation worsened. For most countries, the existence of a lender of last resort in the sovereign bond market prevents the self-fulfilling prophecy from happening in the first place.[4] In the EMU, the lack of a banking union and common resolution framework suggested that national governments were ultimately responsible for any future bailout of their banks, so that as financial institutions started experiencing problems, the prospect of them being bailed out by the government increased doubts about the future solvency of the latter (Pisani-Ferry, 2013). On top of this, at the intergovernmental level, no common fund was set aside in case a Member State had problems refinancing its public debt. The coexistence of these three institutional features reinforced and coordinated investors' negative expectations until they became self-fulfilling.

Critically, these sudden-stop crises bear the hallmark of domination as was enshrined in the set-up (or at least in its deficiencies) that was agreed among the EMU members. As such, these events should not be seen as acceptable interferences nor factored in as part of the costs of a country's membership in the Monetary Union. EMU created a single market in which individual member states surrendered their traditional capacities to control and address hostile capital flows. In the absence of democratically constituted capital market controls at the EU level, member states were left exposed to the possibility of capital markets domination. Since the institutional preconditions for the enjoyment of undominated sovereignty were lacking in the EMU, investors' decisions to sell or buy more government bonds had the capacity to instantiate a social relationship with weaker member states without them being able to revise its terms. In turn, public authority was decoupled from citizens' control and, relatedly, from their capacity to decide how to weather the impact of the crisis. Much like in the case of the slave not having any form of control over the political system that determines his rights, this lack of control over the terms under which pricing decisions are conducted is symptomatic of a lack of status.

With the benefit of hindsight, one can now see how the phase turbulence in sovereign bond markets was nearly inevitable and, in this sense, financial markets were a mere vehicle that reproduced the institutional weaknesses of the single currency. To appreciate this point, it is important to zoom in on the self-fulfilling nature of these capital movements and their dominating features. As investors in the sovereign bond market start questioning the capacity of a Member State's government to service its debt, perhaps because its public finances deteriorated as a result of banks bailouts, some will start selling government bonds in order to avoid future losses. In turn, this pushes interest rates

[4] De Grauwe and Ji (2013a), (2013b) have thus concluded that ' (…) financial markets do not punish standalone countries for public debt accumulation that appear to be equally unsustainable as in the Eurozone countries' (p.31). Countries with their own central bank cannot be easily pushed from a liquidity crisis to a solvency crisis, simply because the cash will always be there for investors, as their debt is denominated in their own currency. At the same time, this does not mean that the Central Bank alone can ensure stability in financial markets, as the experience of Latin American countries suggests.

further up, making it harder for the government to rollover its stock of debt at the new rates. Noticing such funding problems, investors demand even higher interest rates, and the vicious loop repeats itself. What may start as a liquidity crisis, can quickly turn into a solvency crisis. Market participants' expectations play a key role here. Holding the size of the initial shock constant, if market participants are confident about the future, they will not expect the government to default on its debt and will thus ask for a normal return on its treasury bills, which will allow the country to weather the shock. However, if investors are pessimistic, they will ask for a higher return and a 'bad' equilibrium will arise, in which investor's initial expectations become reality (Baldwin et al., 2015). In short, it is the self-fulfilling nature of expectations (for a formal model of the dynamic see Calvo, 1998;; Flood & Marion, 1996; Gros, 2012 Obstfeld, 1986 and Corsetti & Dedola, 2011), not fundamentals, that determines whether a state will be able to weather the crisis or whether it will be pushed into illiquidity and possibly insolvency (Arghyrou & Kontonikas, 2012).[5]

All in all, weaker states lost a sufficient degree of control in the social relationship they formed with their lenders, since the self-reinforcing coordination of investors' expectations takes away their capacity to have a say in the terms of the exchange. Once the self-fulfilling run has started, the fundamentals over which governments have control stop being strong determinants of bond prices, which means that the agonistic relationship between borrowers and lenders is now supplanted by the prisoner's dilemma type of game investors play among themselves (see Obstfeld, 1996), in order to avoid being the last one selling the bonds.[6] This reflexivity means that investors' expectations of each other's choices influence directly the bond's valuation, thus taking away agency from the borrower's control over its asset. This lack of control on the part of borrowers is in need for moral justification.

As often happens in dominating relationships, the options left for periphery countries were less than appealing and trying to reassure investors by cutting spending seemed like the best thing to do. In the Eurozone, Member States cannot devalue or inflate within the common currency, but they could, in principle, leave the euro and regain monetary sovereignty. However, leaving the euro in times of scarce liquidity is an incredibly painful process that is expected to have long-term and incalculable economic and political costs. A second option for Member States facing liquidity (and eventually solvency) problems, would then be to remain in the euro, but default on their debt. This would still be uncharted territory for policy-makers, since the Eurozone lacks a legally and

[5] De Grauwe and Ji (2013a, 2013b), Favero and Missale (2012) and Bocola and Dovis (2016) have shown how a major share of the Eurozone bond spreads cannot be explained by changes in fundamental variables as the debt-to-GDP level, fiscal space and current account position

[6] Of course, this does not mean that if the price of a financial asset is very low, some form of domination is necessarily taking place. On the contrary, a low price may actually reflect the underlying capacity to repay. What is important is that the valuation was not driven by borrowers' self-fulfilling expectations, but by an evaluation of the prospective growth of the country's economy

politically recognised framework to deal with a sovereign bankruptcy. While in theory, this option may sound more appealing than leaving the currency union, the lesson from the crisis has been so far that there are significant spill-overs between countries (see for instance Candelon et al., 2011). In turn, it is doubtful that a country deciding to default on its debt would find cooperating partners in the Council.

While, from a republican perspective, this lack of meaningful choices is not *per se* what is normatively problematic, it highlights how Member States' fiscal sovereignty was temporarily suspended. Indeed, given the lack of other policy options, the governments that were caught up in the liquidity crisis were not responsive to their citizens' needs but to investors' and rating agencies' reactions. In times of crisis, financial markets in the Eurozone enjoy the sort of 'editorial control' described by Pettit (2006), in the sense that governments' reform and spending plans are to be drafted with an eye to what investors at the Treasury's bond auction, rather than citizens, will think. This undermines the values and function of political institutions as citizens are governed without justification. Citizens' collective status as a free polity and, in particular, the country's right to fiscal self-determination has been eroded.

To summarise the argument so far, the collective design of the EMU incentivised significant capital movements in the run-up to the crisis and took away the capacity of member states to control monetary aggregates. At the same time, key supranational institutions were missing, namely: a common banking union, a supranational central bank that could backstop sovereign bond markets and some form of collective fund that could rescue individual governments. Under conditions of crisis, this institutional framework casted doubts on the capacity of periphery countries to finance their public and private debt and motivated investors to collectively sell those sovereign bonds that appeared too risky. The self-fulfilling liquidity crisis that ensued depleted member states of their autonomy and status, as they entered into a relationship with their lenders whose terms they could not meaningfully control.

While investors in financial markets have unearthed these institutional weaknesses, they can still be labelled as dominators, albeit of an unwitting kind, in the sense that they do not intend to dominate nor are their actions 'unjustified. Moreover, it is not them that should be blamed for this injustice. These last two points in the argumentation require careful elaboration, which is what the next sections are devoted to.

Aggregate pricing decisions and systemic domination

I have argued that the self-fulfilling run on periphery countries' government debt represents a form of dominating power, since governments became part of a social relationship over which they have no meaningful degree of control. Given the republican reasons for endorsing competitive markets, we seem to be left with a problem though. How can such a market process be dominating? After all, Pettit understands domination to be an agential concept, meaning that someone must be limiting your republican freedom, while the self-fulfilling crisis is caused by (and consists of) investors fire-selling government bonds. However, it is clearly not them to be morally responsible for the constraint placed on governments actions. They are risking their own resources by signing a debt contract with a country's government that allows them to sell the bond as they see fit. Moreover, once the run on the asset has started, it is even rational from the point of view of the singular investor to sell, so as to avoid future losses.

In republican terms, interferences that are the product of 'the aggregate consequences of independently motivated actions by others' (Pettit, 2012a, 2012b, 2012c, p. 37) are not granted the same normative significance as invasive hindrances. Indeed, most republican scholars conceive domination as being a fundamentally agential (Pettit, 1997, p. 52; Lovett, 2010a, 2010b, p. 48; Laborde, 2010, p. 57) – or, using Blunt's (2015) terminology, interactional – conception in the sense that the source of domination must be an agent, as is the case of the master in the famous thought experiment. It could thus be objected that no domination occurred as no investor could unilaterally impose its preferred price on the bond sold by governments. In other terms, the invisible hand of the market which prevents intentional attempts on the part of investors or of the government at exerting market power is still there.

In order to respond to this argument, we need to briefly venture into the discussion on the sources and sites of domination (see Blunt, 2015 for a great summary of the various positions) and recognise that this conception fundamentally entails the power to impose a social relationship on some agents. In turn, the source of this power can be socially or personally constituted: personal power is power that is 'determined by the personal attributes of the dominating agent' (8), while social power is determined by the rules and norms of behaviour of an institution. Blunt (2015) asks us to compare the case of a gunman that forces a passer-by to hand in her wallet, with the usual one of the slave and the master. In the gunman case, the source of power is personal, in that his personal characteristics (i.e. being armed) allow him to establish a situation of dependency, while in the slave-master case it is social, since it is the institution of slavery that allows the master to command his slave. In both cases, it seems proper to speak of arbitrary interference.

Moreover, the way in which domination materialises can be interactional or systemic. The two terms describe the site of domination, namely how power is administered. In the gunman case power is interactionally arbitrary: whether the gunman will stick to his word and shoot if he does not get what he wants or whether he will let the passer-by go depends entirely on his will (Blunt, 2015, p. 13). But we can imagine also a case in which some discriminatory rules, as in an apartheid regime, become codified in law and are impartially administered by judges. Citizens living under these laws would be certain that these laws will be applied, since their application does not depend on anyone's will, yet they would rightly claim to lack sufficient status, since they lack the ability to challenge and change them.

In our case of self-fulfilling liquidity crises, the source of domination is socially constituted in the sense that the power of financial markets derives from the social practice of international lending to eurozone sovereign states that together have decided to share the same currency and a single central bank. The interference is systemically arbitrary (rather than interactionally arbitrary), in that the self-fulfilling crisis does not depend on the will of any individual investor, but on the spontaneous and impartial market movements (a sort of unwritten rules). Investors are mere enablers of domination in the sense that they are only in a position to follow these movements. Yet, in the aggregate, these pricing decisions have the power to institute a relationship with the borrowers that assigns them a lower status as states cannot contest or to have a say on the terms of this relationship, since the bond pricing stops being related to what states can control (i.e. their fundamentals). Using Pettit's terminology, debtor states are not able to 'command non-interference' (Pettit, 1996, p. 589) and thus cannot resist the market forces that arbitrarily determine the value of their debt.

This is a peculiar case of a system that dominates without people consciously enforcing it, or an instance of 'pure' systemic domination. Blunt (2015, p. 17) tries to offer an example of this by imagining a situation in which a legislator imposes the laws that compose the apartheid regime, which are in turn impartially enforced by a series of automatons that have been programmed for that function. Both the privileged and discriminated group have no influence on this system (they do not have either systemic or interactional power). In this case, 'The automatons cannot be said to dominate, since they are not agents, but only machines with no will of their own. The legislator cannot be said to dominate after laying down the law, since he is dead and has no agency' (p. 18). In our case, the laws (i.e. the self-fulfilling characteristic of the market phenomenon) have been given by the automatons (i.e. the investors) themselves and they arise because of a specific set of institutional features of the Eurozone. So conceived, this form of domination shares some important features of the Youngian approach to structural injustice in that the sources of empowerment and disempowerment are institutionally constituted and wrongdoers do not necessarily intend to harm (nor can they do otherwise) .[7] It is also important to highlight that, while in the case of Young's structural injustice the harm cannot be reduced to an individual relationship between agents (think of the famous Sandy thought experiment), in our case the focus is on a specific kind

[7] One key difference is ingratiation: weaker EU countries would try and infer the market valuation, change the market mood by promising further cuts in spending. In Italy, for instance, a care-taker government was elected to appease investors and effectively change their expectations.

of interaction, namely the one between states and sovereign bond markets. Indeed – and to summarise the argument so far – the incomplete construction of the Eurozone allows financial markets to establish market rules and norms (i.e. the self-fulfilling nature of the crisis) that are arbitrary because they create a social relationship between member states and investors that the former cannot revise or contest.

Siding with Blunt has further implications for republicanism's support of market mechanisms. If we allow for domination to be systemically arbitrary, then it is not enough to look at the market power of individuals (or corporations) as preliminary evidence of potential domination, but it is necessary to also assess whether the interests of market participants are met. This further information can shed light on whether one party is losing out with respect to the other and, in turn, whether the institutions that shape market outcomes play a dominating role. By focusing on individual market power alone, instead, one only takes into account personally constituted and interactionally arbitrary forms of domination, which is only one way in which domination can manifest (Blunt, 2015, p. 19). In other terms, individual market power is not a necessary condition for identifying domination in a market setting.

This reasoning also makes clear that economists and republicans support competitive markets for different reasons. Pettit's and Taylor's support of competitive markets has so far been stacked upon its capacity to disperse individual power and thus prevent discretionary price setting on the side of producers or employers, while for economists, the exercise of market power is associated with the sub-optimal satisfaction of individual preferences. Such wider focus allows economists to also question those institutions that allow markets to function (or not) and that shape the outcomes these markets produce. The self-fulfilling run described here is a case in which investors' valuations are a key driver of price movements themselves. In other terms, they affect the value of the good they are meant to price and this happens without any of them exercising market power individually. The institutional characteristics of the single currency allow this to happen, yet Taylor would not see anything objectionable in this, since no singular agent is exercising interactional arbitrary power. The problem with relying on interactional power, which underpins the distinction between vitiating and invasive hindrances, as the main conceptual tool to assess real-world market institutions, is that one loses sight of the institutions in which markets are embedded and that are instead the product of political action (Preiss, 2018). Importantly, these institutions shape market players' expectations and incentives, which in turn limit the amount of control states enjoy over their relationship with financial markets.

To summarise the argument above, I have argued – in line with Blunt's (2015) analysis – that the sudden-stop crisis witnessed by periphery countries in the Eurozone is an instance of socially constituted and systemically arbitrary form of domination.

The 'Voluntariness' objection and the 'Ubiquitousness' objection

Two objections can be raised to the argument so far. First, if it is the case that any sufficiently large group of investors can, through its simple decisions to accept of refuse the offer of buying sovereign bonds, push a country in a situation of illiquidity and even insolvency, then any country borrowing from financial markets should be considered vulnerable to domination. In other terms, if the freedom countries enjoy in financial markets cannot be considered robust, then republican freedom in this setting is simply impossible or too demanding to reach in practice.

The second objection relates to the voluntary nature of supranational institutions like the EU and the Eurozone. Since European countries entered these institutional arrangements after a process of consensus-building, it seems wrong to claim that that anything unjust has occurred. Nobody forced countries to form a monetary union with the characteristics described above.

The first objection can be answered using the same model developed by Ingham and Lovett (2019) described in Section 2 and the exposition should also help clarify the strategic interaction between a government and investors during a sudden-stop crisis.

The game is set as follows (the game tree is in Figure 1). A European government G has to decide whether to increase or reduce public spending in the midst of an economic crisis. Before this decision is taken, two investors Inv_{1} and Inv_{2}, who are holding the government bond of the said country, simultaneously decide whether to sell the asset or keep it in their portfolio. To make notation easier, the game has two investors, but the conclusions that are drawn would apply if the number of potentially dominating agents is increased.

If all investors sell the bond, the government is forced to cut spending because the negative valuation puts pressure on public finances. If instead investors do not coordinate and take opposite decisions, the government will not be subject to market pressure and will be able to carry out its preferred strategy, namely to spend public resources to fight the recession.

The game shows that when both investors sell the government bond and the self-fulfilling run has started, it does not matter what the government does, they will both get v_i as a payoff. In other terms, the government does not have a say in the bond valuation. Instead, when investors do not expect each other to sell the bond and cannot coordinate, their payoff will depend on what B decides to do.

Investors have different types v_i, some may be more risk averse than others; this influences their payoffs and, consequently, their decisions whether to sell the bond or hold it. If, for instance, Inv_{1} has a high type, he/she will be less risk averse and more likely to risk her money and sell the bond. Indeed, selling the bond carries a cost if the other investor does not do the same. The idea is that selling the bond is like betting on the future fall of the price of the asset, yet

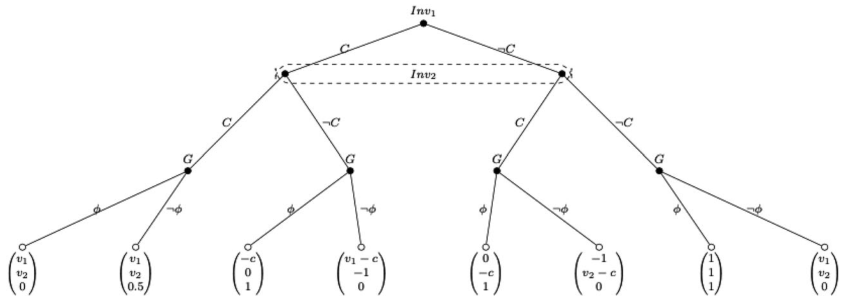

Figure 1. There are two Investors in this game that move simultaneously. Each can decide to either sell the bond (C) of country G or to keep it (– C). If both investors expect each other to sell and decide to do so (if v_{1, v_{2} is higher than the cost of intervention c), then the government G will be pushed in a dominating relationship, in which it is forced to renounce to its democratic mandate – Φ and in which it has no say over the bond valuation. This is the second payoff matrix from the left and one of the two perfect Bayesian equilibria that are discussed, as in Ingham and Lovett (2019). The other equilibrium is at the far right and in this case even though both investors would want to sell, they both expect the other not to, so they both end up keeping the bond.

if the other investor keeps it, the country will not be subject to high pressure and selling the bond will turn out to be a bad decision.

Two equilibria of this game are worth discussing. In both the government chooses to spend, unless both investors sell the bond. In one, however, nobody sells the bond even though their type would make it rational for them to do so (v_i, > 1). This equilibrium results from both Inv_{1} and Inv_{2} expecting each other not to sell. Conversely, in the other equilibrium both decide to sell since v_i, > 1 and both believe the other will take the same decision.

Given the potential for investors to push a country in this second equilibrium, it is reasonable to ask the following question: when are the powers of financial markets appropriately constrained? In Lovett and Ingham's setting, powers are constrained if the combination of types that would want to coordinate is 'justifiably ignorable'. The set of types of potentially dominating agents is ignorable if it is ignorable if its becoming common knowledge that the actual types of Inv_{1} … Inv_{n} do not lie in this set would have no practical consequences for G.

It would be too demanding to require that no investor were ever of a type that would sell the bond and indeed some combination of types would rationally prefer to so. However, in the sovereign bond markets of most countries (at least of those that are not part of an incomplete currency union) these types would be ignorable. Even though most investors were to be of a high type, such that they would have the possibility of pushing countries in a dominating relationship, they would generally lack the *ability* to do so since everyone would expect the others not to sell. In turn, knowing that the investors who happen to be lending at that point in time are not of that type, would have no practical consequences from the government's perspective. In other terms, the government would not feel pressured to try and please the investors in order to prevent them from selling its bonds.

Contrast this with the case of EMU periphery countries. Lenders to troubled Member States know that the system of rules that shape the monetary union does not guarantee that they will get their money back, when the bond reaches maturity. In turn, investors of a high type (more scared ones) will expect each other to sell the bond, thus making 'sell' also their own preferred strategy. Given that these expectations are common knowledge, if each investor preferred to sell the bond, the country would be pushed in a negative equilibrium where no matter what the country does investors will get the same payoff. In this situation, government officials would, out of fear of repercussions, feel pressured to draw some policy packages that reassure them or announce future spending cuts. Imagine then that it somehow became common knowledge that the kind of investors the government face is not of a type that would want to sell the bond. Even if this was the case, we should still say that the country is dominated, since these types are not ignorable. They are not ignorable because knowing that they are not of that type would have practical consequences for the government, namely: it would spare the government the task of ingratiating itself with them.

To summarise, it is not enough that investors are of a particular type for the self-fulfilling run to start. It must also be the case that the expectations they hold of each other's behaviour are consistent with that equilibrium. In the previous section, it was argued that investor's expectations are driven by the logic of the 'uncomfortable trinity'. The system of rules that shapes the common currency plays a key role in steering investors' beliefs which allow them to successfully push countries into a dominating relationship.

The 'Voluntariness' objection suggests that even if we project moral responsibility on the system of rules of the single currency, it still seems like Member States entered this currency arrangements in a non-dominated way. If the decision to join the euro and to create that kind of institutions and procedures is a free choice, then the whole claim that the power exercised by the financial market is arbitrary seems misplaced. After all, nobody forced periphery countries to give up their monetary sovereignty, to accept the no-bailout rule and the prohibition of monetary financing.

The strength of this objection pivots around the nexus between consent and non-domination. However, one's consent to a specific contract (or institutional relation) does in no way preclude the possibility that the distribution of powers it creates in the future will lead to domination. Moreover, on a philosophical level, it seems wrong to argue, as this counterargument implicitly does, that justice claims, like the demand to not be arbitrarily interfered with by financial markets, cannot find their place in voluntary associations (see Sangiovanni, 2012). No member state could consent to be externally dominated in order to enter an international institution, as much as no person would subject herself to an arbitrary power, like in the slave-master thought experiment. Eurozone countries have instead consented to pool (rather that relinquish) sovereignty through supranational and intergovernmental political structures that channel their justice claims and allow them to collectively decide how to shape the common market(s) they created.

A variant of the 'voluntariness objection' goes as follows. If periphery countries' government overspending and over-regulated labour markets caused the sovereign debt crisis, by reducing the countries' export competitiveness, then a limitation of their autonomy is the price to pay for fiscal profligacy and wrong policies (see for instance Chen et al., 2012; Dadusch, 2010; Sinn, 2013). Moreover, excessive government spending in the form of deficits among periphery countries is a negative externality as it raises interest rates for all other Eurozone Members, so why should irresponsible governments, who misuse the common good (i.e. a hard currency) and impose costs on others be bailed out or helped in any way? This objection is factually wrong in its claim that the culprit of the crisis is periphery's fiscal profligacy. The only country that fits this diagnosis is Greece, whose government misreported its liabilities and whose competitiveness was severely compromised even before the crisis started (Sinn, 2013). Even in that case, though, the objection does not challenge the idea that periphery countries lost control of the relationship they formed with their lenders, nor that this amounted to domination, but rather it questions what exactly should follow from this harm to their status. By claiming that weaker member states 'brought it on themselves' this reply, casts doubts on the kind of duties to remedy this injustice that fall upon EMU members. The next and last section elaborates on this point after summarising the main turning points of the overall argument.

Co-responsibility against arbitrary interference

The article has so far claimed that the conception of freedom as non-domination can be fruitfully employed to single out a specific kind of injustice that materialised during the Eurozone crisis. Weaker Eurozone Member States could not control the terms of their relationship vis-à-vis sovereign bond markets, as no matter what their capacity to repay was, the bond valuation was determined by investors' self-fulfilling expectations. Even though investors have the ability to impose this sort of relationship over governments – thus making freedom in sovereign bond markets not robust – this does not mean that domination is ubiquitous and therefore too burdensome to attain in practice. In a well-functioning monetary union, those types of investors that do not have confidence in a country's capacity to repay (or that try to bet on its default) should be justifiably ignorable. In other terms, knowing that some investors may be of such type should not force the government to change its policies, in order to ingratiate itself with them. Unfortunately, the lack of a common backstop in the banking sector, the lack of a lender of last resort and the no-bailout rule created an institutional environment in which those types of investors could not be ignored, since they could – unwittingly, yet successfully – coordinate and push countries in a downward spiral of higher interest payment and cuts to public spending.

Highlighting how the institutional conditions for undominated sovereignty were lacking during the Eurozone crisis leads us ask what should be done to guarantee the collective freedom of EMU Members.

The three-dimensional picture republicanism offers, namely that citizens are free only if their state is externally free as well, points toward the need to regulate the sources of arbitrary power that constrain democratic self-rule. Much like the republican state is meant to maximise citizens' freedom as non-domination, so should a supranational institution shield countries from the external sources of domination. Laborde (2010) warns us against the use of arbitrary interactional power by transnational corporations and powerful states, yet the way financial markets function and the constraints on sovereignty that they impose do not only depend on individual market participants' decisions. Moreover, stopping market participants from establishing dominating relationships misses the point of the republican institutional program. As the case of slavery shows, the eradication of unjust power asymmetries cannot be exhausted by simply sanctioning dominators (i.e. the masters), but requires the guarantee that agents really enjoy status equality (i.e. the abolishment of slavery).

In line with this intuition, an account of responsibility that is sensitive to cases of systemic domination means recognising first, that financial markets and their expansion 'are not natural phenomena, but are the result of the specific structure of a financial system' (Pistor, 2017, p. 186). In turn, the goal of making states free from market domination imposes certain duties on the supranational structure in which they are embedded.

More precisely, avoiding self-fulfilling sudden-stop crisis in the future requires, at a minimum, providing a supranational level of insurance either in the private sector – through a common back stop in the banking sector – or in the public one – through public debt mutualisation. These measures increase the level of co-responsibility among Eurozone members and signal to investors that states are not alone when facing asymmetric shocks to their economies. Securing member states non-domination would arguably only be the first step along a more ambitious reform plan that could lead to the establishment of a full-fledged republican union, in which EU citizens truly control supranational institutions (see Zimmermann, 2019).

These duties to create risk-sharing institutions do not arise because of an injustice inflicted by one country on another. These are duties of solidarity generated by the countries' membership in the Euro area and thus respond to the demands of a political conception of justice. Political obligations are different from legal and moral duties, in that they require us to create new institutions and to fix the ones we have. Nowhere in the EU Treaties is it written that a more extensive form of co-responsibility between states is needed as a matter of right. Yet, in virtue of their membership in the Euro area, member states should recognise that the common rules have had consequences on the autonomy and standing of periphery countries vis-a-vis other members. In turn, this realisation grounds a duty to create new institutions, which are meant to secure countries' non-domination.

Simply put, there is a shared responsibility in upholding common rules that requires us to fix what is wrong about them. Borrowing Young's words: 'The point is not to blame, punish, or seek redress from those who did it, but rather to enjoin those who participate by their actions in the process of collective action to change it' (Young, 2006, p. 122).

Acknowledgements

I would like to thank Professor Ben Crum for the support and his excellent supervision. Thanks also to Hannah McHugh, Cosmin Vraciu, Kasim Khorasanee and Bjoern Brugemann, as well as the researchers at the UCL's Political Theory Workshop and those at the VU PPE PhD Club for feedback on earlier drafts.

Data availability statement

The theoretical model that supports the findings of this study is available from the corresponding author, SM, upon request.

Disclosure statement

No potential conflict of interest was reported by the author(s).

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Appendix. The Basic Model from Ingham and Lovett (2019)

This appendix presents the general game used in the paper and first introduced by Ingham and Lovett (2019). This game (Figure A1) is played by two agents, one potential dominator and one victim, while the one presented in the paper is played by three agents: two investors and a government.

In this game, a Company CEO C has to decide whether to intervene or not in the business of a democratic Government G, for instance, by halting its production in that country in order to extort some favourable tax treatment. Nature here represents all the possible types of CEOs that may come to govern the Company C. C then decides to Interfere or not based on the payoff it will get (which depends on the type of CEO and the cost $-c$) after the Government G has decided what to do based on its payoff. If C intervenes, because its CEO has a particularly reckless type (a high value of v), G is forced to choose not to phi (not abide by its democratic mandate), which is not its most favoured strategy.

As Ingham and Lovett (2019) explain, it would be too demanding to ask that the CEOs of this company were never of a type that would want to interfere. Instead, they

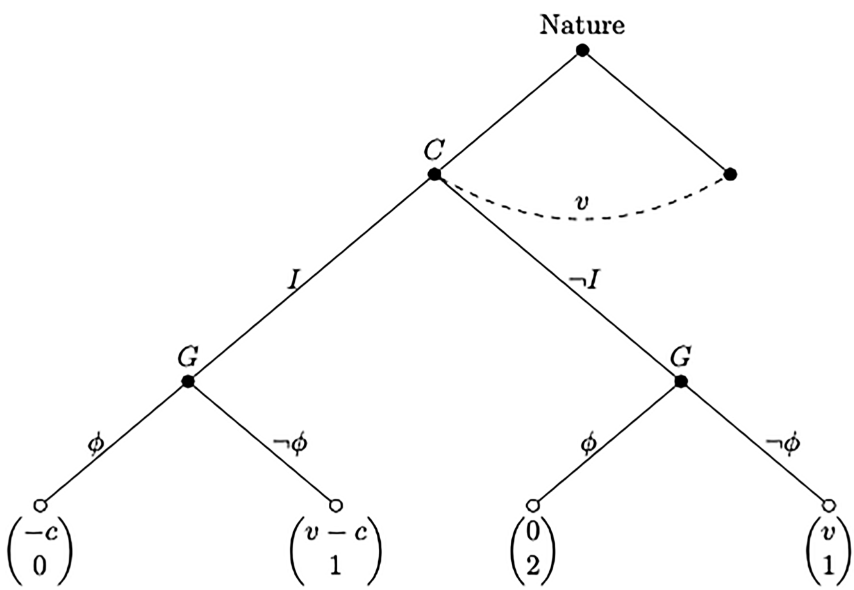

Figure A1. The basic model from Ingham and Lovett (2019).

show how, given that the right republican institutions are present, the types of CEOs that would want to interfere should be regarded as 'justifiably ignorable'.

Imagine, for instance, that the CEO of the company knows that the cost of intervention will be very high, for instance, because a competitor will steal his market share if he devotes resources to bully the government. In turn, the types of CEOs that would want to interfere should be regarded as justifiably ignorable, in the sense that if it became common knowledge that a specific CEO is not from that group, it would not have any practical consequences for the Government. In other terms, if the government knew that the specific type of CEO is not so deranged as to risk his business in order to interfere, it would change what the government does.

Compare this to the situation in which the cost of intervention is very low, so that the CEO would know that it is not costly to bully the government (maybe because markets are not competitive at all). In this case, the types of CEO that would want to interfere could not be regarded as 'justifiably ignorable', since, if it became common knowledge that this CEO is not of a type would want to interfere, this would have practical consequences for the Government. For instance, it would not create an incentive to ingratiate itself with the CEO.