Reform of the ESM - speech by Klaus Regling

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Klaus Regling, ESM Managing Director
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(*Please check against delivery*)

Ladies and Gentlemen,

It is a pleasure for me to speak to members of parliament from euro area countries.

In my short statement, I will describe the new set of tasks assigned to the institution that I manage in the revised ESM Treaty. I will also show how ESM reform is part of a wider process of strengthening Economic and Monetary Union.

The euro area today is stronger and more resilient than it was ten years ago. However, economically it would be wise to continue the process of deepening monetary union and bringing the reform agenda to an end. Especially as economic and political risks are increasing in Europe.

Last December, the EU Heads of State and Government endorsed a package of reforms. This involves the completion of banking union, the further development of the ESM, and a new fiscal capacity. In June this year, the Eurogroup broadly agreed on the detailed proposals to enhance the ESM's role.

Let me describe what this will mean in practice for the ESM.

First, the ESM will provide the backstop to the Single Resolution Fund (SRF). This is a fund established by the EU for resolving failing banks in the context of the banking union. It is financed by contributions from the banking sector. In the event that the resources of the SRF are depleted, the ESM can act as a backstop and lend the necessary funds to the SRF to finance a resolution.

The backstop will be "fiscally neutral", which means that there will be no burden on taxpayers. If the backstop is needed, repayments will come from the banking industry. By 2024 at the latest, the backstop should be fully operational with a volume of around €55 billion.

Second, the ESM will play a stronger role in future economic adjustment programmes. In collaboration with the European Commission, the ESM will design, negotiate and monitor future assistance programmes. The prerogatives assigned to the Commission by the EU Treaty in economic policy coordination will be fully respected, but the ESM will be fully involved in future programmes.

Third, the ESM's financial assistance toolbox was reviewed to make the use of precautionary credit lines more effective. They will be easier to use, which should help to prevent small problems from becoming big problems.

Fourth, the ESM could facilitate the dialogue between a euro area country and private investors when a debt restructuring may be needed.

These new tasks are included in a revised draft of the ESM Treaty. The revised Treaty will come into force when it has been ratified by parliaments in all 19 ESM Member States.

That process will start when all key documents related to the ESM reform are politically agreed by the governments of all ESM Members. This is expected to happen in December 2019, and then ratification will take around 12-18 months.

Since 2010, Europe has accomplished a great deal in terms of strengthening Economic and Monetary Union. However, I share the view that there are still a few more steps needed to make the euro area permanently crisis-proof.

The Euro Summit in June this year mandated the Eurogroup to work in two areas: a common European deposit insurance scheme, and a euro area budgetary capacity called Budgetary Instrument for Convergence and Competitiveness (BICC).

It is clear that the ESM’s role would be much easier with a complete banking union and a pan-European deposit insurance. With an identical level of depositor protection across the euro area and a weaker link between banks and sovereigns (i.e. sovereign-bank nexus), financial fragmentation would decrease and so would the risk of bank runs in a crisis. The volume of the past ESM programmes would have been much lower had a common deposit insurance already been in place.

These are strong reasons to create a European deposit insurance. But for this to happen, euro countries need to agree on a mutually acceptable balance between risk-reduction and risk-sharing. This implies that legacy problems in some countries must be tackled - meaning a further reduction in non-performing loans and a re-balancing of banks’ exposure to government bonds in their balance sheets.

As for a euro area budgetary instrument, the current focus is on improving convergence and competitiveness in euro area countries. It is positive to allocate budgetary resources to an improvement of convergence and competitiveness.

But in my view, it would also be useful to think about a tool for macroeconomic stabilisation. I know such an idea is controversial. I will be happy to explain the reason for such a tool in our discussion later. But I can say already now that such a tool could be designed without creating additional transfers.

Thank you very much.

Author

[Klaus Regling](#)

Managing Director

Contacts

Cédric Crelo

Head of Communications and Chief Spokesperson

+352 260 962 205

c.crelo@esm.europa.eu

Anabela Reis

Deputy Head of Communications and Deputy Chief Spokesperson

+352 260 962 551

a.reis@esm.europa.eu

Juliana Dahl

Principal Speechwriter and Principal Spokesperson

+352 260 962 654

j.dahl@esm.europa.eu