“Safeguarding the Euro – the inside story of the ESM” - speech by Klaus Regling

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“Safeguarding the Euro – the inside story of the ESM”
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(*Please check against delivery*)

Welcome everyone.

Thank you, Valdis, for taking the time to be here today.

And thank you to the colleagues from the Commission who were involved in the preparation of this event.

As you mentioned, Valdis, this is indeed a happy event. It is a particular pleasure for me come to the Commission to present the ESM history book “*Safeguarding the euro in times of crisis – The inside story of the ESM*”.

When you read the book, you will see that one person played a particularly important role in the history of the ESM: Jean-Claude Juncker. Without him, the ESM would not exist in its current form and I would probably not be its Managing Director.

Valdis, we have worked together for many years; in all-nighters side by side to keep Greece in the euro area. Initially, the ESM helped in the troika, then we became a quartet.

We all are convinced that the euro, our single currency, is good for Europe, economically and politically. In our careers we have prepared monetary union, introduced the euro and safeguarded it in times of crisis.

The ESM - Safeguarding the euro in times of crisis

Let me now turn to the ESM.

The ESM was not part of the initial setup of the euro area or the EU. The Maastricht Treaty does not mention the ESM. There was no lender of last resort for sovereigns. With the ESM, the euro area now has a lender of last resort for sovereigns.

The ESM has established itself as a permanent institution with sufficient firepower and it has worked well. Like the IMF, it disburses loans only against conditionality. That means extensive reforms, as this helps countries to overcome the problems that led to a loss in market access and to return to long-term financial stability.

During the last eight years, both rescue funds disbursed €295 billion to five countries: Ireland, Greece, Spain, Cyprus, and Portugal. This provided essential financing to governments, without which some of the countries would probably have been forced to leave the euro area.

Countries benefit from budgetary savings due to our loans with very long maturities and very low interest rates. The Greek budget, for example, saved €13 billion in 2018, representing 7% of Greek GDP. Greece will enjoy these savings for many years to come, and this is an essential contribution to Greece’s return to debt sustainability.

Today, the euro area is better equipped to deal with a future crisis than ten years ago. But as many policymakers noted, more can and should be done to further strengthen the euro area’s financial architecture, to make it more resilient. And more is being done.

The current reform debate

The EU Heads of State and Government endorsed a package of reforms last December. This involves another step towards the completion of banking union, the further development of the ESM, and more work on a European deposit insurance and a fiscal capacity.
In June, the Eurogroup broadly agreed on the detailed proposals to enhance the ESM's role. This decision will imply the following steps for the ESM.

As Valdis mentioned already, the ESM will provide the backstop to the Single Resolution Fund (SRF).

Second, the ESM will play a stronger role in future economic adjustment programmes. Together with the Commission, the ESM will design, negotiate and monitor future programmes. This means the prerogatives assigned to the Commission by the EU Treaty with respect to economic policy coordination will be respected.

Third, the ESM's has reviewed its financial instruments, in particular its precautionary credit lines, to make it more useable.

Fourth, the ESM could facilitate the dialogue between a euro area country and private investors if a debt restructuring is needed.

Future vision

It is evident that since 2010, Europe has accomplished a great deal in strengthening EMU. However, I think there are still a few more steps needed to make the euro area crisis-proof in the future.

In my view, we need progress in four areas:

First, **a common deposit insurance**. With an identical level of depositor protection across the euro area and a weaker link between banks and sovereigns, financial fragmentation would decrease, and so would the risk of bank runs in a crisis. If we had had a European deposit insurance in the last ten years, all ESM programmes could have been substantially smaller. Obviously, legacy problems in the balance sheets of some banks need to be sorted out before a common deposit insurance becomes possible.

The second issue to be resolved is **liquidity in resolution**. The completion of banking union also requires addressing the remaining risks of a liquidity gap after a resolution. Different proposals to address the possible liquidity shortfall are currently being discussed. Some of these include liquidity provided by the Single Resolution Board (SRB) or the ESM. This will be difficult for the ESM given the potential financial magnitude. Other proposals suggest a stronger role for the ECB as a provider of a special liquidity facility. There is no agreement yet on how to proceed.

Third, a **fiscal capacity for macroeconomic stabilisation** is needed in my view and in the view of all European and international institutions. I know this is a controversial topic. But in my view this is a key element missing in the architecture of our monetary union. This would be useful because countries that are members of a monetary union have given up two key macroeconomic policy instruments: monetary policy and exchange rate policy. Moreover, monetary policy can often be pro-cyclical for individual countries. Such a tool could be designed without creating additional transfers. We do not need an annual budget for macroeconomic stabilisation but a revolving fund would be sufficient.

Progress in these three areas and in creating a capital markets union – one of Valdis top priorities for the next five year, I believe – would improve risk-sharing within the monetary union significantly. That can be done without creating permanent transfers and would really help to avoid small problems from becoming big problems where an ESM programme would be needed. I want to avoid that.

Fourth, and finally, we should begin to think about a **European safe asset**, even though this is highly controversial. A safe asset would increase the volume of highly rated assets, which is now limited to a few sovereign and supranational issuers, and is actually shrinking. It would provide a common benchmark that could be used to price debt throughout the euro area. A safe asset would also allow Europe’s banks to reduce their holdings of national debt, and to attract international capital to Europe. Safe assets would be a crucial step to integrate markets, and to make the euro more attractive for international investors, thus strengthening the international role of the euro.

Conclusion

The euro area today is stronger and more resilient than it was ten years ago.

However, I hope we will see progress in the mentioned four areas. That would continue and complete the process of deepening monetary union. Not next year, but over time as the preconditions are put in place. And it would certainly strengthen the role of the euro in the international monetary system.

I will conclude here and I am sure the panel with Marco, Pervenche and Guntram will pick up some of the issues I mentioned.

Thank you.

Author

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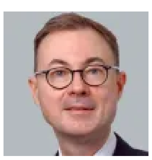

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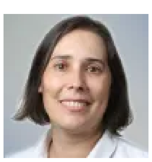

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