EMU: what next and what else?

Pierre Gramegna
Minister of Finance, Luxembourg

Focussing on the big picture: the way forward for Europe's success

The euro has come a long way since its introduction 20 years ago. Its early childhood was marked by euphoria as Europe entered a new stage of development through a higher level of integration. After a promising first decade, the euro met its teenage crisis, laying bare the underlying weaknesses in the European monetary architecture. In its wake, trust in the common project appeared to lose ground but those days are now certainly behind us.

I have myself experienced first-hand the bold steps taken to create a stronger Economic and Monetary Union (EMU). Major achievements certainly include the reforms of the fiscal framework, the creation of the European Stability Mechanism (ESM) or the Banking Union. One cannot underline enough the historic progress made in recent years.

Sometimes taking a step back also allows to better appreciate what has been achieved, to develop a better understanding of remaining issues and to get the fundamentals right before taking the next step forward. It is crucial to remember that our common currency is a true European success story and public support for the euro is at a record high.

Looking forward, it will be essential to continue our efforts to foster the combination of structural reforms, sound fiscal policies and quality investments, which build the foundation for a more resilient and competitive EMU. This is all the more important given the softening economic momentum and such a targeted focus will be more conducive to the long-term success of our economies than yet another academic discussion on the perceived institutional deficiencies of the European construction.

Given the current economic outlook, raising potential growth needs to be at the top of the agenda. Targeted structural measures will be key to ensure higher productivity and to improve the competitiveness of the European economy. It will be crucial to step up efforts by concentrating on areas with high potential such as digitalization and knowledge-intensive sectors.

As regards public finances, policies should be encouraged that leave sufficient fiscal leeway and put debt ratios on a sustained downward path so as to ensure preparedness for a possible downturn. At the same time, sufficient consideration should be paid to the growth-friendliness and inclusiveness of public finances, as well as to the impact of fiscal policy on climate change.

Promoting and sustaining quality investment in key areas, such as education, skills, infrastructure and innovation, will support the growth potential of our economies. The aim should be to encourage higher levels of private and public investment, which nurtures a sustainable economic model and long-term well-being, without compromising resources for future generations.

In this context, the new budgetary instrument recently endorsed by the Eurogroup can play a role to increase both the euro area's competitiveness and convergence. At the same time, the Eurogroup also agreed to set up the common backstop to the Single Resolution Fund at the level of the ESM and, more generally, to further strengthen the ESM and its toolkit. These ambitious initiatives will significantly upgrade the resilience of euro area to adverse economic shocks.

By finding a broad agreement on these important elements of reform, we have sent a positive signal to the world that the EU's single currency continues to move forward. This unique capability to find compromises to complex issues makes Europe stand out in the world and it is on that basis that I remain fully confident about the continued success of our Economic and Monetary Union.

Vilius Šapoka

Minister of Finance of the Republic of Lithuania

Financial fragmentation in the EMU: what has been done and what remains to be done

We live in challenging times - Brexit, trade wars, weakening global demand. Sometimes it is easy to get caught in the news of the hour, in largely exogenous issues and miss the bigger picture - that there are endogenous structural challenges that are more relevant than ever.

The global financial crisis revealed several structural weaknesses in the Economic and Monetary Union (EMU). Most of them can be boiled down to a lack of financial unity in the EMU, in other words, the financial system is too fragmented. At the time of global financial crisis the member states were often cut off from the single market and had to face challenges in the banking sector singlehandedly, which made the burden very heavy to carry. The capital market, which was supposed to “step in” and fill in the void created by the banking sector, thus alleviating the credit crunch, failed to do so as it was also fragmented and, to a large extent, confined to the single member states.

Much has been done since then. We raised the confidence in our banking system by introducing and implementing the Single Supervisory Mechanism, which reduced fragmentation in terms of rules and regulations. Then the Single Resolution Mechanism followed; a member state no longer had to carry the burden of its banking sector issues on its own, which greatly increased the banking sector stability and issue resolution predictability in the whole EMU. The fragmentation in capital markets has not been forgotten as well. A significant amount of work has been done with substantial progress that we can be proud of. The agreement has been made on legislative initiatives ranging from harmonisation of rules and supervision to offering better options for retirement savings and improving SME’s access to capital. These milestones brought much needed unity in capital markets by reducing the fragmentation further and further. At the end of the day, can we say that the EMU financial system has significantly improved? Yes. However, have we done enough? No.

With the global financial crisis behind us, it is tempting to relax and gloat over the success achieved. However, as I have already mentioned, there is an ample amount of other issues, which despite their exogenous nature can be a substantial challenge to the EMU financial system and this time we need to be not mostly, but fully ready to face it. That is why I have always supported and called for a full completion of the Banking Union (BU) and Capital Markets Union (CMU).

The European Deposit Insurance Scheme (EDIS) is a still missing element of the Banking Union, which, I believe, will be setup one day. This would be a final nail in the coffin of instability and fragmentation of the banking sector. I understand political difficulties in risk sharing when the risks are not evenly distributed. However, I believe that a mutually agreeable balance could be found. On the other hand, the progress on risk reduction is evident. As a result, there is some reason to be optimistic regarding the eventual adoption and implementation of EDIS.

I firmly believe that in the long term every member of the EMU will benefit from stability, resilience and confidence a fully-fledged BU will bring. We should not forget that the EMU is not a zero-sum game. One member’s gain is not offset by another’s loss, despite the fact that it may sometimes seem so in the short-term - the EMU is a positive- sum game.

With regard to the CMU, the progress on remaining policies should be sped up. Nevertheless, I am glad that in addition to more traditional capital market aspects important sustainable finance issues are also being tackled. The initiatives on low carbon benchmarks and disclosure are agreed upon and only some taxonomy issues remain, which I believe will be tackled in the near future with full support from the Lithuanian side.

In addition to the aforementioned structural weaknesses of the EMU, I feel the need to touch upon one more issue which is crucial for the sustainability of the euro area - sustainability of public finances. It is vital that the Stability and Growth Pact rules are respected.

I understand the political and economic hardship this brings. However, the only way to address the sustainability of public finances is to focus on structural reforms inside the country, as, unfortunately, these reforms cannot be done from the outside. I wholeheartedly wish that these issues, wherever they may occur, are successfully resolved all across the EMU, as this will benefit us all.