“Unfinished business in the new EU political constellation” - Klaus Regling speaks in Berlin

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Ladies and gentlemen,

We’ve arrived at the final panel, and the last two hours of this conference. This panel will deal with “unfinished business in the new EU political constellation”. You have talked a lot about regulation and supervision today. So let me broaden the discussion, and focus on the topic that lent this conference its name: financial stability.

In my view, financial stability in Europe is closely linked to the euro. One of the goals of the Economic and Monetary Union was – and remains to this day – to have a large area of financial and monetary stability. Having such an area is conducive for growth, and creates a true competitor for the other large economic regions of the world, the United States and China. Some would say that we have failed miserably, given the euro debt crisis, which was a serious set-back. But let's not forget that Europe also had major crises before the single currency. And without the euro, the global financial crisis would equally have caused tremendous currency volatility in Europe, at a large economic and possibly political cost.

With the significant steps taken in response to the crisis during the last decade, the euro area is now more robust. Its institutional architecture is also much stronger, with a range of new institutions. We now have a single supervisor for the 130 largest systemically important banks, and a single resolution mechanism to wind them down when they are a gone concern. And with the ESM, we have created a new function to provide assistance loans to countries that land in trouble during a crisis. As a result of these programmes, countries that needed emergency financing have tackled their problems, through fiscal adjustments, improvements in competitiveness and repairs of their banking systems. At the European level, we have tighter and broader economic surveillance, and better policy coordination. All these steps have made monetary union more robust, and will help financial stability in the future.

As you know, politicians are currently talking about reforms to further strengthen the euro area. The debate focuses on the completion of Banking Union, fiscal arrangements and developing the mandate of the ESM, including possibly a greater focus on crisis prevention. All these steps will bring more financial stability, and are therefore part of the "unfinished business" this panel is about.

So, what is currently under discussion? Let me first look at Banking Union. A backstop for the Single Resolution Fund is required to make it more credible in the eyes of financial markets. There is a growing consensus that this is a role the ESM could fulfil. A European Deposit Insurance Scheme is the second important step to complete Banking Union. If depositors know that their money in the bank is protected by the whole euro area, and not just their own government, the chances of a sector-wide bank run in one country are slim. Therefore, setting up such a deposit insurance is the best guarantee it will never be needed in any major way.

But this can only happen if legacy problems with banks in some countries are tackled first. Healthy banks in one country cannot be expected to have to pay for mistakes made in the past by banks in another country.

Another reform that is needed is the broad harmonization in the European Union of corporate, bankruptcy and tax laws known as Capital Markets Union. This would boost cross-border investment and open up new financing channels for companies. It would have the added benefit of reducing Europe’s heavy reliance on bank funding, and would greatly enhance economic risk-sharing through private markets. Completing the Banking Union, and creating a Capital Markets Union would certainly strengthen financial integration in the euro area and thus increase risk sharing.

Secondly, let me turn to fiscal issues. The EU does not need a full fiscal union, with larger transfers between countries. The existing EU budget already allows for significant transfers to poorer countries, which can amount to up to 4% of their economy. We also do not need a large additional budget to counter a deep crisis hitting the region. The simultaneous increase in fiscal deficits during the global financial crisis of 2008/09 showed that Europe can successfully fight a crisis in truly exceptional cases under the existing rules.

However, there is room in the monetary union in my view for a facility that deals with economic shocks hitting one individual country, a so-called asymmetric economic shock. For instance, think of Ireland if it were hit by a particularly hard Brexit. Different ways to establish such a facility are possible: rainy day funds or a complementary unemployment insurance – which exist in most U.S. states – could be attractive options. This is because they do not lead to permanent transfers or debt mutualisation between the participants. Rainy day funds, for instance, pay out during a crisis, but states have to reimburse the money when they recover.

Such a fiscal capacity could be combined with a more predictable and transparent system for burden-sharing with private creditors in case of a sovereign debt restructuring. Until now, this has happened on an ad-hoc basis, as was the case with the Greek Private Sector Involvement, or PSI. In my view, this should be done by including stricter collective action clauses in euro area bond documentation. The ESM could take on the role of organising so-called London Club-type restructurings, to assure a fair outcome for all parties involved. There are suggestions for automatic maturity extensions whenever a country requires an ESM programme. This is a risky option, in my view, as such automaticity would be pro-cyclical, and make problems worse rather than solve them.

Thirdly, and finally, the development of the ESM in the way I described it would also help to make monetary union more resilient, and thus contribute to financial stability.

Ladies and gentlemen, I hope I have made clear that there is enough "unfinished business" in Europe. In bank regulation and financial market supervision, and, more broadly, in deepening monetary union. Fortunately, the political impetus for further euro area integration is now as good as ever. In recent elections, Europe's citizens have shown their commitment to a tradition of multilateralism. The popularity of the euro is at record heights, and this gives politicians a clear mandate to pursue the reforms that will, among others, bring greater financial stability to the euro area.

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