

The role of the ESM in a deeper monetary union - speech by Klaus Regling

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04/07/2018

Speeches

Frankfurt, Germany

Klaus Regling, ESM Managing Director
“The role of the ESM in a deeper monetary union”
ECB Fiscal Workshop
Frankfurt, 4 July 2018

(Please check against delivery)

Last week, the European Council issued a statement on deepening the monetary union. It is a good sign that the political will exists to strengthen the currency union now that the economy is doing well, and there is no crisis that forces us to act.

When talking about deepening monetary union, we should not ask if Europe needs new institutions, or if existing institutions need new tasks. That is of secondary importance. We should analyse what is needed to make Economic and Monetary Union (EMU) more robust, more resilient. Now that the crisis is behind us, what weaknesses remain, and what can Europe do to fix them?

The broadest answer to that question, in my view, is that the euro area needs more economic risk sharing. Risk sharing between countries of the euro area is underdeveloped, compared for instance to the U.S. More cross-border banking in Europe would be one way to increase risk sharing through the private sector. More integrated capital markets facilitating investments from one country into the other are another. That is why it is so important to complete the Banking Union, and to put in place the Capital Markets Union.

These two policy packages will help reduce financial fragmentation. In addition, there is a controversial discussion whether Europe needs also new fiscal tools, to complement private sector risk sharing. I would talk about that briefly at the end.

Concerning the Banking Union, it is good that the decision to set up a backstop for the Single Resolution Fund (SRF) has been taken. A common deposit insurance is the other crucial measure but this requires that legacy problems are dealt with first.

Friday's statement made clear that the ESM will play a more prominent role in the future. This is a recognition of our successful work, of the growing analytical capability of the ESM - for instance in the area of debt sustainability - and of our expertise as an institution operating in financial markets every day.

The backstop to the SRF will be provided by the ESM. The debate about other new mandates, which reached an interim conclusion at the June Eurogroup, will continue until December, at least.

But it is already clear that our member states support a greater role of the ESM in future assistance programmes, together with the Commission and the ECB. How will this affect the working relations between the ESM, the IMF and the Commission? By establishing the ESM, Europe built up the financial expertise and firepower it did not have before the crisis. Over the years, this meant the IMF's role became smaller. The Fund did not financially contribute to the third Greek programme at all. Still, the IMF will remain involved in Europe in the future - every member state of the monetary union is also a member of the IMF - although to a smaller degree than was the case during the euro debt crisis.

Cooperation with the IMF will also benefit from the increasingly close dialogue between the Fund and the world's regional financing arrangements - like the ESM -

which we set in motion.

Our working relation with the Commission was laid down in a Memorandum of Understanding this year. This will be revised depending on the summit conclusions in December. But there is no tension here – each of us has their own perspective. This is clearly visible when we visit together former programme countries, as part of our Early Warning System. The ESM looks at repayment capability, debt sustainability and market access, the Commission at a much broader set of topics. This will remain the case even if the ESM gets a bigger role in monitoring euro area countries. In any case, the future distribution of labour will fully respect the role of the Commission laid down in the Treaty.

The Eurogroup is also looking at the toolkit of the ESM. This is because while we have six instruments at our disposal, only two have ever been used. There is a debate, for example, about how to make it easier to use the precautionary arrangements, by revising their eligibility criteria. The ESM could also provide additional facilities with shorter maturities than our traditional 20 to 30 year lending.

That is part of a wider debate about fiscal risk sharing, including fiscal facilities for macroeconomic stabilization. A number of euro area fiscal tools, such as a reinsurance of national unemployment systems, a rainy day fund, or a budget for investment, convergence and stabilisation, are under discussion. This is still a very controversial debate among our member states. And it is linked to the question of sovereign debt restructurings. It would make sense in my view to have a framework in place to make such restructurings more transparent and more predictable, without tightening the rules. In my view, we don't need to have a more rigid approach but a more transparent one. And the ESM can play a role in such a framework.

Let me finish with a few thoughts about the future governance of the ESM. I am in favour of incorporating the ESM in the EU Treaty, when the EU Treaty is changed. The Commission proposal to incorporate the ESM into the EU framework through secondary law is questionable and not supported by most member states. The model I prefer is that of the European Investment Bank, which is part of the EU Treaty, has its own statute, its own capital and its own governing bodies, which lends it the independence and the flexibility to operate in markets like us.

The intergovernmental set-up chosen for the ESM requires unanimity for important decisions. This can be cumbersome, but it is not something I expect countries to give up anytime soon. And frankly, this set-up has worked quite well. The ESM has been able to act fast and decisively, handling large amounts of money.

One could consider establishing closer links between the ESM and other EU institutions, even while the current legal situation persists. The MoU with the Commission offers one possibility for that. Similar arrangements with the Single Supervisory Mechanism (SSM), the Single Resolution Board (SRB) and the SRF would be helpful, to assess financing needs in future programmes and to manage the backstop.

One could also consider a more formal relationship with the European Parliament. I visit the European Parliament a number of times each year, for an informal exchange of views. The accountability of the ESM is, ultimately, to national parliaments through the finance ministers of the euro area countries, who are also our Governors. This does not preclude a more formal dialogue between the ESM and the EP based on an inter-institutional arrangement.

Thank you. I am now ready to discuss these topics with you.

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