Informal Exchange of Views with the Economic and Monetary Affairs Committee (ECON) of the European Parliament

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(Please check against delivery)

Introduction

- I would like to thank Chairwoman Bowles and the Economic and Monetary Affairs Committee for inviting me to this informal exchange of views.
- The ECON Committee is a central platform of debate on euro area economic policy matters. This is illustrated by the regular appearances of Eurogroup President Dijsselbloem, who is also the Chairman of the ESM Board of Governors, of ECB President Draghi and of Commission Vice President Rehn.
- The ESM was founded almost year ago. I am grateful for the opportunity to discuss with you the ESM – and the EFSF - and how they fight the crisis together with the euro member states, the European Commission and the ECB.

The ESM's institutional design

- In order to frame our debate I would like to underline the ESM's institutional set-up which is different from EU institutions.
- When the temporary EFSF and the permanent ESM were founded, the 17 euro Member States chose an intergovernmental setup outside the EU treaty framework. That was the only way to become operational quickly.
- The money for the ESM capital comes from the Member States' national budgets. The ESM's decisions for an assistance programme and individual loan disbursements are under tight political control as Member States decide unanimously. There is also strong democratic legitimacy as several governments have to seek a mandate for these decisions from their national parliaments.
- This set-up implies that the relationship between the ESM and the European Parliament needs to be ad hoc and informal.
- Our relationship could change in the longer term, should the euro Member States decide to integrate the ESM into the EU treaty framework.

How crisis resolution works in the euro area

- The 17 ESM members contribute a total subscribed capital of €700bn with €80bn in paid-in capital, the highest of any International Financial Institution.

- The ESM has a maximum effective lending capacity of €500bn. Together with the EFSF – which continues to manage the programmes for Ireland, Portugal and Greece - the lending capacity is €700bn.
- Since early 2011, the EFSF has provided €168.5 bn in loans to Ireland, Portugal and Greece. €19.8 bn remains to be disbursed. Since July the EFSF can no longer enter into new programmes.
  The ESM is now the sole mechanism for responding to new requests for financial assistance.
- Currently the ESM has a financial sector assistance programme for Spain, for which €41.3bn has been disbursed; no further disbursements are expected.
- The ESM also has a macroeconomic adjustment programme for Cyprus. By the end of the week €4.5bn out of a programme volume of €9bn will have been disbursed.
- This means that about €450bn remains unused. This corresponds to 90% of the ESM's lending capacity.
- Together EFSF and ESM have disbursed €212bn since operations started in early 2011.

ESM's strategy has been successfully used by the IMF for decades

- The basic idea is one that the IMF has successfully used for decades in many countries: providing temporary loans for countries in a crisis when markets refuse to lend. IMF loans provide two critical advantages at times of stress: time to undertake reforms and reasonable costs of financing. These loans are granted in exchange for conditionality.
- The ESM operates according to this model. We provide temporary financial assistance in the form of loans, bond purchases or credit lines at very favourable conditions. The interest rate we charge is the interest rate we pay when we raise funds in the markets. We only add a very small fee to cover operating costs.
- The ESM financial assistance buys time. During this time the conditions attached should enable the countries to reform their economies and regain investors' confidence.

The ESM is part of coherent euro area strategy

- The ESM is part of a coherent economic policy strategy that involves the 17 euro area Member States, the Commission, the ECB and, where appropriate, the IMF.
- Under conditionality there have been significant fiscal consolidation and structural reforms in beneficiary countries.
- Unit labour costs in Ireland, Portugal, Greece and Spain have fallen. As a consequence these countries have improved their competitiveness and current account deficits are disappearing. These results show that conditionality works.
- In parallel, budget deficits have decreased in beneficiary countries. Greece is even showing a primary surplus.
- Markets are rewarding these efforts. Ireland and Portugal were able to return to the market with 10-year bonds this spring at acceptable rates. Spain has been able to keep market access.
- I am convinced: without our assistance some of the beneficiary countries would have been forced to leave monetary union.

The efforts are beginning to affect the real economy

- However, people in borrowing countries do not see this progress yet. Many are enduring hardship. Salaries and pensions have been cut, many have lost their jobs. At the ESM we are aware of the pain the adjustment has caused.
- A key question is when will these efforts be rewarded, when will growth and jobs return.
- IMF experience shows that structural reforms and improvements in competiveness do lead to growth and employment – but with a time lag.
- In the second quarter we saw the encouraging signs in the real economy. Unemployment has finally stabilized in beneficiary countries, albeit at an unacceptably high level, and the macroeconomic disequilibria are improving.
- In Portugal, the economy grew for the first time in two and a half years by 1.1 %, which is the highest increase in all EU countries. Exports in Spain are growing at a healthy rate. In Greece, the situation is stabilizing.

The euro area as a whole is improving its economic governance

- The strategy of addressing the acute economic and fiscal problems in the beneficiary countries is reinforced by improvements in the euro area economic governance.
- The enhanced economic policy coordination with the "Six-pack", the "Two-pack", the "European Semester" and other new rules are essential in this context. It is now indispensable that these new rules be scrupulously applied.
- The European Parliament's responsibility as the co-legislator is crucial and I would like to pay tribute to role of the ECON committee in crafting these new rules.
- As the ESM Managing Director I meet global investors and economic policy makers all the time. They are scrutinizing how the euro area reforms its economies and its governance. For our credibility it is crucial that the decisions for the improved euro governance are lived up to and the plans on Banking Union are implemented without delay.

The necessity of completing Banking Union

- Very recently the Trilogue on the Single Supervisory Mechanism (SSM) was successfully concluded. This is without any doubt a major step that will define the European banking landscape in years to come and a cornerstone for the so-called Banking Union.
- As you know the euro finance ministers also reached a political agreement in June on the main features of the direct bank recapitalization instrument of the ESM. In principle this instrument could be used once the SSM is established and working. The ECB expects this to be the case in fall of 2014.
- A condition for this instrument to be enforced is that the 17 euro Member States unanimously agree on its creation, and they would only do that once the Bank Recovery and Resolution Directive (BRRD) and the Deposit Guarantee Scheme Directive (DGSD) have been finalized.
- Furthermore, discussions on the set-up of a Single Resolution Mechanism have just begun.
- Taking all this into account, it is quite evident that the work of this committee in the months to come will be absolutely critical for the definition and establishment of the Banking Union.
- Thank you very much for your attention!