1. The Euro: a young but ambitious currency

2. Current state of play

3. Completing EMU: why and how?
MORE THAN A YEAR AFTER BREXIT

“We are going to make progress. We will keep moving. We will move on because Brexit isn’t everything. It isn’t the future of Europe.”

Jean-Claude Juncker, State of the Union Address, 13 September 2017
Tangible benefits for citizens, firms and governments

The symbol of European integration

While the crisis shook confidence, popular support for the euro has been consistently high

Source: European Commission and Eurobarometer 2017
Following Brexit, the euro area GDP will be 85% of the GDP of the European Union.

The perspective is for all Member States (except Denmark) to join the common currency.

Brexit makes completing the Capital Markets Union more challenging, yet more important.

Budget drop reinforces the focus on new European public goods.
ELECTION CYCLE 2017: A WINDOW OF OPPORTUNITY

- Last year this time: economic recovery hampered by huge political uncertainty
- Populism in check: NL, AU, FR, ...and yes DE
- From depression to euphoria and back: wrong perception
- A more inward-looking Germany? I don't think so
OUTLINE

1. The Euro: a young but ambitious currency
2. Current state of play
3. Completing EMU: why and how?
STRONG RECOVERY, YET NOT COMPLETE
CONDITIONS IN PLACE TO DEAL WITH FISCAL AND FINANCIAL FRAGILITIES

- Public debt
- Budget deficit
- NPLs
- LT Interest rates
- Fiscal space
- Deleveraging needs
- snowball risk
- Bank profitability space

Countries represented: DE, EA, IT, FR
OUTLINE

1. The Euro: a young but ambitious currency
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A DETERMINED RESPONSE TO THE CRISIS STABILISED THE SITUATION, BUT THE EMU INSTITUTIONAL SET-UP IS STILL INCOMPLETE

- Remaining sources of financial vulnerability and risk of renewed financial instability, especially given high public and private debt
- Insufficient collective stabilisation tools
- Impossible to achieve simultaneously:
  - an appropriate fiscal stance for the euro area as a whole
  - an optimal distribution of the fiscal effort
- Persisting economic and social divergences
- Complex governance and democratic deficit
A NEW POLITICAL SYNTHESIS IS NEEDED

Risk Sharing and risk reduction

Financial Union

Economic Union

Fiscal Union

Sound budgets and fiscal capacity

Reforms and incentives
FINANCIAL UNION: INTERNATIONAL COMPARISON

Source: IMF
FINANCIAL UNION: THE MOST URGENT PRIORITY FOR EMU

- Advancing on risk reduction and risk sharing and providing more diversified financing options for firms

- Short-term measures
  - Further reducing risks and building on banks' better capitalisation
  - Completing the three pillars of the Banking Union (BU)
  - Delivering on the Capital Markets Union (CMU)
  - Possible instruments beyond BU and CMU: Sovereign bond-backed securities

- Post-2019: possible additional successive measures
  - European Safe Asset
  - Regulatory treatment of sovereign bonds
ECONOMIC UNION: REFORMS HAVE BEEN UNDERTAKEN SINCE THE CRISIS, ESPECIALLY IN CRISIS-HIT COUNTRIES

Source: OECD, Commission Labref database
ECONOMIC UNION

- Economic rationale for improving further the economic union:
  - Potential for stronger convergence
  - Increased economic resilience in case of future crises

- Strengthening convergence and resilience by better using existing tools:
  - Economic policy coordination—more dialogue, stronger euro area dimension, multi-annual approach
  - EU budget—stronger link between funding and reforms
  - Technical assistance

- New tools in the longer term:
  - Five Presidents Report: binding convergence standards
FISCAL UNION

• Rationale behind a fiscal Union (Reflection paper on the deepening of the EMU):
  • i) sound public finances and the existence of fiscal buffers which help economies to be more resilient to shocks;
  • ii) complementing common stabilisation tools at the level of the euro area as a whole;
  • iii) the combination of market discipline and of a shared rulebook which would allow these rules to be more effective and simpler to understand and operate.

• In the longer term: review of EU fiscal rules
• Transformation of the European Stability Mechanism into a European Monetary Fund
GOVERNANCE AND ACCOUNTABILITY

The ESM should now progressively graduate into a European Monetary Fund which, however, must be firmly anchored in the European Union's rules and competences.

A European Minister of Economy and Finance:

• promotes and supports structural reforms in Member States, building on the work the Commission's Structural Reform Support Service
• should coordinate all EU financial instruments that can be deployed if a Member State is in a recession or hit by a fundamental crisis.
• ideally also a VP, who should also preside the Eurogroup.
• must be accountable to the European Parliament.
### EMU ROADMAP: BROAD OVERVIEW

#### By 2019
- NPL strategy
- Common backstop Single Resolution Fund
- European deposit Insurance scheme (EDIS): agreement
- Capital Market Union finalisation
- Work on sovereign bond-backed securities
- Preparation of the new Multiannual Financial Framework (MFF)
- Proposal for the creation of a dedicated euro area budget line within the EU budget
- Stabilisation function: reflection
- Steps: integrate the Fiscal Compact in EU law
- Proposal: transform the European stabilisation mechanism (ESM) in a European Monetary Fund (EMF)

#### 2020-2025
- Capital Market Union (CMU): implementation
- European deposit Insurance scheme (EDIS): roll-out
- Possible euro area safe asset
- Changes to the regulatory treatment of sovereign exposures
- New Multiannual Financial Framework (MFF)
- New convergence standards linked to a central stabilisation function
- Stabilisation function: implementation
- Stability and Growth Pact (SGP) simplification
- Unified external representation
- Possible permanent European Minister of Economy and Finance and institutional implications
## AN ACCELERATED STEP BY STEP APPROACH

<table>
<thead>
<tr>
<th>The US and the USD</th>
<th>The EU and the EURO</th>
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<tbody>
<tr>
<td><strong>1776</strong>: Declaration of independence. The US are 241 years old</td>
<td><strong>1967</strong>: Treaty of Rome. The EU has just celebrated its 60th birthday</td>
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<td><strong>1791</strong>: Congress establishes the First Bank of the United States on the impulse of treasury secretary Alexander Hamilton. 1792: USD coinage act</td>
<td><strong>1971</strong>: The Werner report puts forward the first proposal of a Monetary Union</td>
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<td><strong>1979</strong>: European monetary system</td>
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<td><strong>1913</strong>: President Wilson signs the Federal Reserve Act into law</td>
<td><strong>1998</strong>: The European Central Bank is founded</td>
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<td><strong>1917</strong>: Small central government budget** (&gt;5% GDP)</td>
<td><strong>1999</strong>: Creation of the Euro</td>
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<td><strong>1932</strong>: 1st time US federal budget used in a counter-cyclical manner</td>
<td><strong>2002</strong>: Euro in circulation</td>
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<td><strong>1934</strong>: Federal Deposit Insurance Corporation (FDIS)</td>
<td><strong>2012</strong>: Banking Union, ESM</td>
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<td><strong>2015</strong>: EDIS</td>
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* Though not a central bank, its power and scope made it a precursor of the FED
** Without military spending

LESSON FROM THE US: FISCAL UNIONS TAKE A LONG TIME TO CONSTRUCT AND THE IMPACT OF WARS IN THE US IS NO BENCHMARK FOR THE EU

EU Budget in 2014 = ~1.17% of EU GDP

Better economic times and stronger financial stability: defy the "Ultima ratio"

Creating bridges makes sense politically and economically

Populist pressures should not be underestimated but we have a chance to relaunch Europe

Main goals: complete EMU (BU in primis), foster reforms to lift potential growth, deliver on new EU public goods

Lesson from US history: virtue of patience
BACKGROUND
THE GLOBAL ROLE OF THE EURO

Source: European Central Bank, June 2016