

European Central Bank Conference

Priorities for the EMU deepening in the next 5 years

Frankfurt, 19 December 2019

Introduction

- Many thanks for giving me the opportunity to speak today to such an eminent audience about how I see the priorities for the Economic and Monetary Union in the next 5 years.
- The von der Leyen Commission will speak up for Europe and for the aspirations that Europe represents. My generation was born when the Rome Treaties were signed – or shortly before - and we have since experienced the Union coming to maturity. With its single currency, free movement, unique internal market and waves of enlargement to countries that share the belief in Europe. We should now speak to the generation of our children, who aspire to live in a sustainable society that allows all of us to reap the benefits of new opportunities.
- Over 200 million EU citizens voted in this year's European elections and asked us to lead on the major challenges of our times: the transition to a healthy planet, harnessing a new digital world, upgrading our social market economy, promoting democracy and the rule of law.
- As Commissioner for Economy, ensuring inclusive and sustainable growth is my main task. Because a society that stands by inclusion and solidarity, is a community that brings people and nations together. And because solidarity makes economic sense. As President von der Leyen put it, we need to embark together on a transformation, which will touch every part of our society and of our economy. In embarking on that journey, we need to embrace a vision that reconciles *the social* and *the economy* in today's Europe.

Achievements

- The scale of the political project ahead of us is large, some may say daunting. It is important therefore to recall other great achievements, deemed for long as illusory, but which, through vision and determination, nevertheless took shape. What better example to keep in mind than the euro and the Economic and Monetary Union, today being a natural part of our daily life. We celebrated this year the 20th anniversary of the euro.
- The euro, our common currency, is more than the coins and notes in our pockets. It is a symbol of our shared identity and of Europe's promise of prosperity and protection.
- EMU has had its fair share of bumps during its teenage years. One expects that from a youngster. But together we overcame the deepest economic and financial crisis experienced by our generation, and saved the integrity of the euro, which has come out stronger and more mature. Jobs, growth and investment are now back to or beyond their pre-crisis levels. Public finances continue to improve, our banking system is more robust and the foundations of our Economic and Monetary Union are stronger.
- That said, we still have a collective responsibility for supporting EMU in its adulthood.
- It is very reassuring that public support for the euro is currently at its highest level since 2002 [76%]. It is less reassuring that the legitimacy of the euro and the institutions mandated to underpin it seems to be under some fire, also in Member States that have undoubtedly been among the first beneficiaries. How do you say in the language of this town? "Prügelknabe"? We should redouble our efforts, not to artificially talk up the euro, but to strive for an Economic and Monetary Union that lives up to the expectations of our citizens. For an Economy that works for people.
- Several key elements of the Banking Union have been achieved. The euro area has been equipped with a single supervisor, and with common crisis management and crisis resolution mechanisms. The macroeconomic and fiscal surveillance of Member States has been significantly strengthened.
- The independent and active policy that the ECB has conducted has been instrumental. Without it, I doubt that I would stand here today on the back of 26 quarters of uninterrupted economic growth.

Challenges

Ladies and gentlemen,

- With clouds forming on the horizon, some linked to trade tensions and others to slower global growth, we must keep up. We need a more attractive investment environment and growth, which creates quality jobs, especially for young people. Many citizens paid a high toll to the crisis. We have not forgotten them. Not at all. And our endeavours for a deeper, stronger EMU are guided by the well-being of all citizens.
- Europe faces a combination of short-term and longer-term challenges, which are already knocking on our door. Subdued economic performance will be the major one for the years to come, against a background of an ageing population, increasing inequalities among our citizens, and climate change.
- Growth in the longer term is held back as productivity growth remains low and challenges related to ageing are becoming visible. Yes, Europe has seen several years of recovery, but rather less progress in social and environmental sustainability.
- We now face headwinds. And the long-term challenge of making our economies more productive, more sustainable and more inclusive is starker than before. Euro area growth is set to remain relatively weak at around 1% over the forecast horizon, down from around 2% in what we used to consider trend growth. Unless something changes, the underlining factors point to a low-for-longer growth scenario. In spite of all efforts made, core inflation remains in the 1-1½ % range. Inequality is on the rise, with the richest 1% of the population accumulating more and more wealth.
- We have for some time lived with unusually challenging macroeconomic conditions in the euro area. A low growth and inflation rate environment constrains monetary policy to a policy of low interest rates, operating close to (or, indeed, at) the effective lower bound. If conditions were to deteriorate, the risk of monetary policy being constrained could materialise. This is clearly not the macroeconomic environment that the signatories of the Maastricht Treaty could have envisaged when they agreed on the instruments for fiscal policy. They assumed monetary policy and automatic stabilisers are enough to stabilise the economy.

- At the same time, the needed policy answers are made more difficult by the breakdown of multilateralism at the global level. Multilateralism has been put into question by emerging trade conflicts. This year and next, the contribution from trade (net exports) to growth is expected to be zero or negative. Given the EU's position as a highly open economy with large export-dependent sectors, the evolution of trade disputes has the potential to touch the foundations of our growth model.
- A coherent strategy – beyond monetary policy - is therefore needed to avert the perspective of a 1% economy. To steer the economy towards sustainable growth and jobs, our political will and the full set of policy tools available in the euro area needs to be deployed in four priorities:
 - Meeting the demand for the EU to play a more assertive global role
 - A true Financial Union as the key element in completing EMU
 - A fiscal policy and a fiscal governance appropriate to the new environment
 - Efficient decision-making, reviving the Community method

1. Play an assertive global role

In the current global environment, which is challenging the multilateral system as we had come to know it, there is both space and international demand for the EU to play a more assertive global role. President von der Leyen has claimed a geopolitical role for the Commission. This encompasses foreign and defence policy and commercial policy, of course - but also enhancing the role of the euro internationally. This would make the global financial system less vulnerable to shocks, strengthen 'monetary sovereignty' of the euro area and improve the liquidity of, and preference for, euro assets.

- The new Commission is equally committed to a more strategic use of economic and environmental diplomacy, with EU bodies and institutions leading by example and encouraging the use of the euro in their operations, i.e. debt issuances and international payments.
- A strong euro externally needs a strengthened architecture of the Economic and Monetary Union internally: said differently, it will not be possible to have a stronger global role for the euro without delivering on the domestic agenda. Banking union, the capital markets union in the medium term, and a more balanced policy mix in the short term, are conditions sine qua non for Europe to count more in global governance.

II. Completing EMU

- Many of the objectives the von der Leyen Commission has set for its mandate require decisive progress in completing EMU: this is an overarching priority for the euro area to become the engine of growth, prosperity and stability for the whole Union.
- We have now reached a critical point. While there have been important first steps [the agreement in principle on the reform of the European Stability Mechanism, the budgetary instrument of convergence and competitiveness], the overall progress toward completing the EMU has been so far unsatisfactory and below par of what is truly needed.
- We need to be able to go further. We collectively need to cross those red lines that have generated a stalemate in completing the EMU. We need to take action now to have EMU completed by the end of this mandate.
- In the short term, taking concrete steps towards completing EMU, which requires increased political determination, would reduce uncertainty and thus be positive for investor confidence and economic growth.
- It is clear that the level of ambition we have seen so far is not sufficient.
- Completing the Financial Union is a prerequisite for ensuring its stability and spurring private investment on the scale needed to address the medium-term challenges, including the green transition. Member States will not be able to generate sufficient funds on their own. The Banking and Capital Markets Union are also necessary to address the remaining pockets of instability and the fragmentation of banking and capital markets. These are still a source of concern for investors, especially global ones, and a key obstacle to investment.
- Europe has shown that we can act as catalyst with the Juncker Plan and its European Fund for Strategic Investments. The new tools that we could devise for addressing climate change could also have a positive side effect for stabilising our economy, for instance if we were to give our banks access to common green assets [in the future].
- One of the instruments that could make our currency union more resilient is a euro area safe asset. Let me refer here to a recent speech given by Benoît Cœuré who considered the introduction of a safe asset as instrumental to break the sovereign-bank nexus, to support transmission of monetary policy, to strengthen the international role of the euro and, finally, to integrate our capital markets.

III. A Fiscal policy appropriate to the new environment

- I believe that we need to reconsider the role of fiscal policy given the current macroeconomic environment. Some economists have argued that fiscal rules should incorporate a “knock out” clause when monetary policy reaches the zero lower bound.¹ This would allow fiscal and monetary authorities to cooperate to implement a fiscal expansion. I will not go so far. We should not “knock out” our fiscal rules. Let us not forget the experience of the euro area sovereign debt crisis: having a sustainable debt – in those Member States with high public debt – remains a key objective for fiscal policy. An important discussion needs to happen, however, on the role of coordination between the monetary and fiscal authorities. I fully agree with Mario Draghi’s point that “*monetary policy can still achieve its objective, but it can do so faster and with fewer side effects if fiscal policies are aligned to it*”.²
- The Stability and Growth Pact gives the power to enforce maximum thresholds for Member States’ deficits and debt levels, but the EU has no power to compel Member States to undertake a fiscal expansion. This limits our ability to achieve an appropriate fiscal stance for the euro area. It may not be a problem in a normal macroeconomic environment but, as I have said, the conditions that we are living through are not normal - though they may persist. Since budgetary policies are the responsibility of Member States, the coordination of fiscal policy becomes essential. Fiscal responsibility in high-debt countries should go hand in hand with more supportive policy action in low-debt countries.
- Let me be clear on this: the need for coordinated fiscal policy action does not mean a more lenient fiscal discipline. Those Member States that have high public debt must put it on a safe downward path. We should not forget the original aim of our fiscal rules, namely: to ensure the sustainability and safety of public debt. This is also a matter of responsible behaviour vis-à-vis future generations.
- This also means that the large public investment needs mentioned earlier must be met in a way that ensures debt sustainability and respects of our rules. We will therefore continue to make full use of the flexibility allowed within the Stability and Growth Pact, while promoting a growth-friendly composition of public finances.

¹ See, for example, this article from Jonathan Portes and Simon Wren-Lewis:
<https://www.economics.ox.ac.uk/materials/papers/13342/paper704.pdf>

² <https://www.ecb.europa.eu/press/key/date/2019/html/ecb.sp191028~7e8b444d6f.en.html>

- A last word on fiscal policy: the journey will not be complete without building a central fiscal capacity for the euro area. This is key to provide the European Union with some powers over macroeconomic stabilisation policy.
- In a few weeks, the Commission will present its review of the six- and two-pack. This will provide us with a timely opportunity to start a thorough debate with Member States, the European Parliament, the stakeholders, on the future of our fiscal framework. So today's discussion is also timely from this point of view.

IV. More efficient decision-making and accountable institutions

- The institutions built under the extreme pressure of the crisis were based on the intergovernmental method in decision-making, which has now become dominant. But this method is unsatisfactory both in terms of efficiency and democratic accountability. Effective democratic checks and balances can be fully achieved when decisions affecting the euro area as a whole are taken by supranational institutions.
- It is now the right time to reflect on the appropriate institutional structure for the long-term. This could be discussed as part of the conference on the future of Europe announced by the Commission President.

Ladies and gentlemen,

- We need to have a 'vision' of what the Economic and Monetary Union would be once it reaches its steady-state. We need to be ambitious but also cautious. We must tread carefully ahead to have support of Member States and of citizens.
- Most of our interlocutors acknowledge the challenges of our institutional architecture. Still, views are very different on what is required to address them. The differences of views, however, are mostly due to an underlying lack of trust.
- This brings me to my last point. The economic crisis has undermined trust among Member States with a sharp divide between debtor and creditor countries. To reform the EMU and build strong and legitimate institutions, we have to overcome the divide between creditors/debtors, risk reducers/risk sharers and responsibility/solidarity.
- We need to rebuild confidence. To do so, a diplomatic effort will not be enough. Confidence must be built up around a common vision and project. This is the opportunity offered to us by the challenge of the climate transition, which President von der Leyen has put at the heart of the Commission's action.

- We must heed the opportunities from the climate transition whilst reducing inequalities. Addressing inequality and climate change are at the centre of citizens' concerns. And the Commission will include them in the strategy of the new European Semester that for the first time integrates the Sustainable Development Goals. The economic impact of climate change is one of the biggest systemic risks facing the world economy, financial systems and societies today. The most vulnerable in our society will be the hardest hit from environmental degradation, with large divergences in income already existing within and between Member States.
- However, if tackled in the right way, environmental and inequality challenges could be an opportunity to revitalise the European economy, reorienting it towards sustainable development. That's why one of my key priorities for the coming year, as I explained earlier this week, will be to make a success of integrating the UN Sustainable Development Goals into the European Semester of economic policy coordination. It will be a process, not a snap decision.

And that's why the Commission will present next month its Sustainable Europe Investment Plan. Because this extraordinary transformation of the European economy that we want to deliver will require an extraordinary plan for investments.

- Accompanied by an appropriate regulatory framework, a review of the taxation on energy and appropriate financial instruments, the Green Deal, along with the digital revolution can be formidable means of generating sustainable growth. But they must be underpinned by a new framework for investments, state aid rules and taxation. We will experience change in economic sectors – ranging from transport, to energy, to housing – without precedent since the decades following the Second World War. It is a unique opportunity that we cannot allow ourselves to waste. It is also a very heavy responsibility.
- Today the EU is facing a demanding but exciting agenda for the years to come. In order for the Economic and Monetary Union to be successful, we need to continue work in a spirit of openness and solidarity. As Christine Lagarde said in her first speech as ECB President last month: "The answer lies in converting the world's second largest economy into one that is open to the world but confident in itself – an economy that makes full use of Europe's potential to unleash higher rates of domestic demand and long-term growth."
- Achieving that goal calls for policies that go beyond the business as usual. Whether we rise to this challenge will decide the quality of life of the European citizen in the short term and in the long term.