Lorenzo Bini Smaghi: Whither Europe after the crisis?

Speech by Mr Lorenzo Bini Smaghi, Member of the Executive Board of the European Central Bank, at the inauguration of the Academic Year 2011, Institutions Markets Technologies (IMT) Lucca Institute for Advanced Studies, Lucca, 11 March 2011.

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Introduction

To understand how Europe will develop after the crisis, let me start with two observations. First, the crisis has caught Europe unprepared. Second, Europe has, in a sense, responded to the crisis in a surprising way.

The lesson to be drawn is that Europe is still evolving, growing, continuing on its path of integration. This is not happening, however, according to some pre-defined, agreed plan, but rather in response to the challenges it faces, which in some cases are likely to endanger the very existence of the Union. Europe moves forward when it finds itself at risk of taking a step back. At that point the costs of immobilism exceed those of mobility. It manages to find the energy needed to overcome the political difficulties of making another step forward. That step is difficult because it requires a decision of all members – now 27 – who together are forced to accept that the costs of losing the common good are higher than the benefits of maintaining their national prerogatives, often more symbolic than substantive.

Europe’s integration is therefore largely unpredictable because it depends on the challenges and shocks facing European society, and on its ability to understand that the step forward brings more advantages than immobilism.

Such unpredictability is the logical consequence of the original route that the EU countries are following, which neither takes inspiration from existing institutional and other political realities, like the United States, and nor does it seek to apply pre-defined constitutional models. Rather, it follows the principle of subsidiarity, according to which only those powers and competences are centralised which cannot be exercised more effectively at local level. This principle cannot be applied theoretically. It is experience that permits an assessment of how the national implementation of certain competences may lead to an inefficient outcome. An awareness of the need to assign powers to a European institution – powers which previously were exercised primarily at national level – can only arise after the failure of the decentralised approach. This kind of choice cannot however be taken for granted because no institution, national or international, readily surrenders its powers to another body.

For example, it is not possible to determine in theory if the euro area is an optimum currency area according to pre-established objective criteria. A thorough analysis would probably stipulate the opposite. But experience has shown that the euro area is certainly not one in which it is an optimum arrangement to have 16 different currencies that float freely against each other or are tied by intervention mechanisms. The experience of the European Monetary System and the currency turmoil of the 1980s and 1990s were instrumental in establishing that the transition to a single currency was needed, particularly to avoid the collapse of the Single Market, from which all the countries have benefited. The “cold” operation, attempted with the Werner Plan several decades earlier, at the end of the Bretton Woods system, did not and could not succeed because it was too much theory and too little “policy”. Without the failure of Bretton Woods and the European Monetary System, we would not have the euro today. There would have been no need.

Proceeding on the path of European integration in this empirical way has two risks. The first is that, on one hand, the failure of the existing institutional framework must be sufficiently obvious to convince Member States of the need to take another step forward, but on the other hand it should not be so devastating as to put into question the entire Community structure. The second risk is that the constraints that are applied with each step forward in

the integration process to define its boundaries should not be irremovable to the point of making the next step impracticable. That next step could in turn become necessary in the future if the preceding proved to be insufficient.

I would like to develop these thoughts in three ways: first, remembering how Europe behaved during the crisis, then, considering the lessons to be drawn from the integration process, and finally, thinking about the long term and the path that has to be taken by economic and monetary integration.

Europe facing the crisis

My first observation is that the crisis has caught Europe – by which I mean the euro area – unprepared. The institutional design of the euro did not take into account the possibility of a crisis like the current one. In some ways it is understandable. Such crises happen rarely. Indeed, the specific characteristics of the euro area, having a single currency with no centralised taxing power nor a single system of financial regulation, eluded few people. However, it was felt from the outset that the incompleteness could be offset by rules of conduct and disciplinary procedures aimed at preventing crises. It was expected – perhaps naïvely – that the rules would be respected.

But then, what was the alternative? To wait, as some had suggested, until the necessary conditions were created for a more complete fiscal and political integration before proceeding to monetary integration? That would risk delaying monetary integration and seeing a repetition of the turbulence, and perhaps led to an implosion of the system and of the Single Market. It was then decided to make a start to Monetary Union without taking into account the possibility of serious financial or budgetary crises of the Member States.

This type of behaviour is not surprising. It characterises innovation in general, even in the institutional field. The first cars did not have advanced safety systems such as reinforced bumpers or air bags to protect drivers. Neither could they have been developed and patented before the first car appeared on the road. People had trust in the prudence of drivers, in the slow speed of the first cars and presumably believed that the limited number of cars on the road would keep accidents to a minimum. After realising that the accident rate was far higher than expected, the car makers decided to develop better systems of protection and the public authorities decided to regulate the issuing of driving licences.

The experience of the first ten years of euro has shown that even with strict rules of conduct and coordination mechanisms the members of a monetary union may find themselves in a financial and budgetary crisis. The reasons vary. One is the circumvention of the rules, as in the case of Greece, which managed to double its public deficit for many months without notification. A second reason is the accumulation of financial imbalances in the private sector, which in the event of a crisis can become public debt. Under these conditions a country may lose access to the financial markets. What is described in the literature as a “sudden stop” in the influx of capital occurs. This phenomenon is typical of developing countries, which borrow in foreign currency to facilitate the inflow of capital. In advanced countries this type of problem is rare because the debt is generally denominated in the national currency, and if need be the central bank moves in and funds the Treasury, replacing private operators. The credit risk of the sovereign issuer is avoided, and transformed into a risk of monetisation of public debt and therefore of inflation.

The euro area is in a particular position even for the constraints that are applied every time a step towards further integration is taken. In the case of Monetary Union the Treaty contains at least two provisions that do not make it possible to take the next step towards fiscal union without a further change to the Treaty itself.

The first is the prohibition imposed on the central bank to directly finance the budgets of Member States, as this would create an incentive for them to pursue deficit spending in the expectation that this will be financed through the common tax of inflation. The other provision

of the Treaty is the so-called “no-bail out” clause, which forbids member countries from assuming the debts of other countries, transferring resources to repay them. These two provisions entail, in fact, the full separation between the monetary power, exercised at EU level, and the fiscal power of the Member States. In other words, it’s as if the public debt of the euro area countries were denominated in foreign currency, outside the control of the country itself, with no possibility of being monetised.

These constraints were put in the Treaty precisely to discipline the governments of member countries so that they avoid excessive borrowing at the risk of them losing access to the financial market. Returning to the analogy above, it was decided to create a euro without air bags or safety net to cope with a country’s public or private financing crisis. It was believed that, to avoid crises, the member countries had sufficient budgetary disciplinary mechanisms in the form of the Stability and Growth Pact.

Experience has shown however that even with the best of intentions, with prevention policies and strict controls, road accidents occur and may be caused either by inappropriate behaviour or by external factors. Without appropriate safeguards, not only do those who drive recklessly may be injured, but also those who happen to be passing by.

Outside of Europe, the crisis was deemed by some as showing that the euro experiment was a failure. A number of scenarios were foreseen in turn: the implosion of the euro, a split-up into several parts and the exit of some countries.

Evidently the reasons underlying the creation of the euro have not been understood. For this reason, the reaction of the European institutions has evoked surprise among those who had prematurely announced the death of the euro. On the other hand, continuing the analogy that I made earlier, giving up the euro when the first crisis comes would be like taking up cycling again after having your first accident with a car.

Contrary to what was suggested by those who perhaps had an interest in European countries returning to pedalling rather than driving fast cars, the engineers in Europe got down to work to repair the car and make it safer, but also to ensure that the drivers are more cautious, with the penalty of costly fines.

In less than 12 months, the institutional structure of the euro has changed dramatically. It is interesting to look back at where the euro was 12 months ago. In less than a year, the euro area countries have approved the €110 billion rescue package for Greece, against a drastic fiscal and structural adjustment programme; approved the creation of a European Financial Stability Facility with €440 billion; decided to amend the Treaty to create a permanent mechanism, inspired by the International Monetary Fund. The Stability and Growth Pact has been amended to constrain fiscal policy more and make sanction more automatic. A system of macroeconomic surveillance has been created to identify and counteract the payment and competitiveness imbalances within the euro area. Several countries have adopted serious measures of fiscal adjustment and implemented structural reforms. Meanwhile, the European Union has set up three new supervisory authorities: for securities and markets, for banking, and for insurance, as well as a European Systemic Risk Board. Another important aspect, to which I will return, is strengthening the coordination between the countries of the euro area, at the highest levels of government.

A year ago, who could imagine that all these decisions would be taken? Certainly not those who foresaw the disintegration of the euro and did not understand the base on which Monetary Union was built. Fortunately, many of them changed their minds and no longer consider that the euro is at stake, but rather the solvency of some of the member countries.

A surprise was not only the reaction to the crisis, but also the manner and timing of the decision-taking. Often late and under the pressure of the market.

Lessons of the crisis for European integration

Without retracing all the steps that have characterised the last few months, some important aspects can be highlighted that can help us understand how Europe will evolve in the future.

The first is the discovery by the political authorities and citizens of the euro area members, of what the founding fathers such as Kohl and Mitterrand, but also Thatcher, had sensed from the outset, namely that monetary union is a political union. It took a crisis to understand this, but only the crisis made us realise that the failure of the euro, its disintegration, would hurt everyone, poor and rich countries alike, creditors and debtors. Sharing the same currency inextricably links the economic destinies of the member countries. It means suffering the consequences of the behaviour of others, even when they are undisciplined. We cannot look away, as was done when the currencies of other countries were allowed to devalue in an effort to regain competitiveness. We need to restore order and prevent divergences, otherwise we shall be affected directly. We cannot even wait for someone else, such as the financial markets, to discipline our neighbour, neither can we threaten to push it into bankruptcy, because the contagion would be immediate.

The analogy of the joint ownership that Carlo Azeglio Ciampi has often applied to the European currency has never been so pertinent as in recent months. The awareness that the euro is a common good, to be safeguarded at all costs, has been repeatedly confirmed and led to courageous decisions.

On the other hand, the public has been mobilised in support of joint intervention only when it perceived the possibility of losing the benefits that come from the *acquis communautaire*. This explains why on several occasions over the last year political leaders of various countries have said that the euro was in danger. This was aimed at building a consensus for measures which in normal times would have been very difficult to accept. This approach to the problems has fuelled tensions on financial markets and in the end required interventions on an even broader scale. Instead of a broad and definitive plan, which would have solved the problem at its root, actions were taken which filled the gaps, one after the other, when it was needed.

A second important aspect that has characterised the action in recent months concerns the difficulty of changing the European institutional structure towards greater integration. As I mentioned before, monetary unification has been designed in such a way that it does not involve the transfer of other powers to the European level. Such a transfer is not possible without starting a complex procedure for amending the Treaties. This makes it very difficult to make the next steps. This is why the financial support created to help countries in difficulty (the Financial Stability Facility) has been defined so as to prevent it from being considered as a budget transfer mechanism. It will provide funding only at penalty rates and on condition of macroeconomic adjustment by the debtor country. Ultimately it became necessary to change – even if only one paragraph – the Union treaty.

A third aspect that has characterised the decisions of recent months is the balance between solidarity with countries in difficulty and the pressures to be exerted so that they take the necessary measures to correct the imbalances. Agreeing to support countries in difficulty unconditionally would have fuelled moral hazard. Conversely, refusing to support them risks plunging the area into a financial crisis.

It is difficult to strike a balance, especially when the economic and political difficulties are inspiring a search for scapegoats, even abroad. It's easy to nourish nationalist sentiments in the countries in difficulty, shifting responsibility to the European institutions for having caused the crisis or for not having done enough to prevent it. The ECB, for example, was reprimanded for having exacerbated the Irish crisis in November 2010, after demanding for a long time that the government swiftly adopt the necessary measures for fiscal consolidation. Recently, a former Irish Prime Minister has even had the honour of front page headlines when he reproached the ECB for not having sufficiently monitored the Irish banking system

when it is well known that in Europe the powers of prudential supervision are the responsibility of the national authorities, a competence that you do not want to give up.

Faced with the crisis the European institutions often find themselves playing the role of scapegoat. The national press of different countries, unfortunately, tends to pander to anti-European sentiments and sometimes fuels conflict, without trying to explore the themes or to present the opposing viewpoints.

This crisis has shown the difficulty of dialogue between public opinion in different countries, which obviously have access to news through the national media which in turn do not always try to present the views of the other party, much less that of European institutions. Such a mechanism tends to feed extreme and opposing positions between countries. It hinders the search for solutions that benefit the common interest. I think we should reflect further on this matter.

The fourth aspect of this crisis has been a tendency to address and resolve issues mainly through an intergovernmental approach, rather than a Community method. This is obviously a problem when the common interest of the euro area does not necessarily correspond to the sum of national interests. It is one of the reasons why the Council's decisions have often been taken at the last minute, under pressure from the markets, when the danger of immobilism is evident to all.

One reason is that the political dimension of Monetary Union does not match the structure of European institutions, now 27, and includes countries that do not share the conception of common destiny associated with the euro. The European Commission, which considers itself a political and not a technical institution, has problems putting forward proposals which only concern monetary integration. Often it tends to act as a mediator, replicating the functions of the Council. The Council, in turn, does not exist in the restricted composition of the euro area, except for the Eurogroup, comprising the finance ministers. The mechanism for enhanced cooperation provided for in the Treaty of Lisbon is too cumbersome. The European Parliament seems to be the only political institution that aims to favour the Community method, but does not have sufficient powers to assert itself. It played a limited role in managing the crisis.

The ECB is the monetary policy institution of the 17 members of the Union that has the ability to take decisions quickly on the basis of a common goal. It has had, at the most difficult moments, to ask the governments and parliaments of the Member States to take decisions in line with the challenges and objectives that they themselves were given and with the commitment to do everything necessary to defend the currency. The national political institutions have not yet, however, incorporated in their decision-making processes the fact that they share a single currency, which requires new and joint responsibilities. There is insufficient capacity to "think European", that is, to channel national decision-making in a broader framework, linked in particular to the single currency. For this reason it is necessary to strengthen the decision-making capacity of the Eurogroup and extend it to other fora, particularly the heads of state and government of the euro area and perhaps even to labour ministers and others which affect, for example, the competitiveness of the European economy.

We should not however ignore the fact that significant results have been obtained. As I mentioned earlier, the euro is in a very different position compared to where it was a year ago. Any institutional innovation is inevitably incremental, as is engineering. It is also stimulated by the accidents along the way, if one knows how to draw the right lessons. This method of working however makes it difficult to draw a definitive framework for the European institutional structure, able to bring definitive stability to the system.

We are expecting important decisions to be taken this month. There is a risk that, as in the past, attempts may be made to minimise the domestic political costs. The piecemeal approach followed in recent months may be easier for domestic public opinion to digest. But the lack of individual measures with respect to the overall size of the problem and market

expectations may further prolong the uncertainty, as has happened in the past months. This may in turn increase the political cost of inaction. It is better at some point to take definitive measures that calm markets and convince them that the euro countries are indeed willing to do whatever is necessary to safeguard the financial stability of the area, as their governments have been claiming for months.

One of the problems this crisis has shown is that the political authorities and the markets find it difficult to understand each other. On the one hand, markets do not understand why the governments of European countries are slow to adopt the necessary measures to solve problems, postponing decisions and creating uncertainty about their actual intentions. On the other hand, the political authorities often do not understand how the financial markets work; they deeply despise them but at the same time depend on them to finance their budgets. They do not understand that announcements and good intentions are only valid in normal times, but when the crisis spreads the risk of losing credibility can only be limited with effective and timely action. They do not understand that market participants are looking for profit opportunities, and when they are offered one, they hurl themselves onto the next, in the expectation of making a similar gain. This phenomenon is the source of contagion. Threatening the markets with retaliation and coercive measures often discourages the more stable, long-term investors, while it rewards speculators with short horizons.

The long period

The piecemeal approach followed in recent months risks losing sight of the long-term goal. The measures may not be completely coherent. We came close to it last autumn, with the Franco-German proposal, endorsed by other countries, to make it easier for countries to go bankrupt. Fortunately, the idea has not gained acceptance, not only because of the ECB's dislike but also because of the devastating effect it has had on financial markets. It will take time to recover from the loss of credibility suffered by Europe with that proposal.

The proposal was based on the assumption that the best way to discipline governments and to ensure sounder public finances is to make it easier for a country to declare bankruptcy. As soon as a country has problems with its public finances, it should seek a restructuring of its debts or automatically extend its bond maturities as a necessary condition for receiving help from European and international institutions.

This idea is mistaken for several reasons. Firstly, it attributes the main task of disciplining governments to the financial markets. The markets – according to its proponents – work better if the conditions under which a state may fail are more explicit. This hypothesis – dear to many academics – does not however reflect reality. In the private sector bankruptcies are possible and are subject to regulation, but markets often incorrectly assess the risk of securities issued by the private sector. The markets were wrong both before and after the crisis, and continue to make mistakes, even with regard to sovereign risk. Moreover, they often behave inefficiently and facilitate collusion, especially when it is possible to buy derivatives that allow you to "bet" on a country's bankruptcy, even without having invested in it. Giving the market the exclusive power to decide the fate of millions of people seems to me quite irresponsible. The recent European decision to limit the possibility of buying derivatives to hedge sovereign risk without the underlying security is therefore justified.

It is precisely because this approach is wrong that the International Monetary Fund was created more than 60 years ago. It intervenes to prevent markets from having the exclusive power to declare countries bankrupt, particularly when they are intent on consolidating their public finances. It is not clear why Europe should be more masochistic than others and do without the tools they have.

Another reason is that the credit rating of a country is not as simple as that of a private company. It depends on the ability and willingness of the national authorities to tax and spend. You cannot be sure that financial markets are better equipped to assess such

willingness and ability. Experience shows the opposite, since the vast majority of the countries that have resorted to the IMF in the last 20 years have also repaid their creditors. Moreover, a sovereign default has contagion effects on others. In such conditions it is not always easy to make a country go bankrupt if the costs of paying for it are to be borne by the rest of the area.

We need start from the objective, which is to build a stronger euro, based on a more globally competitive economy and with sound public finances, to reflect on possible long-term solutions. I wish to put forward my thoughts in a personal capacity.

To strengthen the foundations of the single currency it is necessary to encourage virtuous behaviour both in the public and private sectors, which are largely the responsibility of the Member States. This can be achieved through monitoring processes, peer pressure as in the case of the Lisbon agenda, constraints and automatic or semi-automatic rules. Efforts in this direction are to be encouraged, bearing in mind that the more automatic the rules, the greater the devolution of sovereignty.

This crisis has shown, however, that the procedures and restraints on public and private behaviour are not always effective. We cannot exclude a housing crisis in one country, excessive private debt in another, a cyclical or trend slowdown in yet another, a gradual loss of competitiveness. We need to avoid the same mistake as the one committed in recent years, assuming that crises will not occur.

Efforts must therefore follow at least two lines. The first is to minimise the risk of crises. The second is to minimise the impact of the crisis, in particular the contagion effect on other countries.

The first line of intervention is one on which work is being done with great intensity and therefore I will not dwell on that. It is to strengthen the discipline of and restraints on fiscal policies and the behaviour of private operators. The first is obviously easier to do than the second. The proposals on the table aim to strengthen existing constraints and procedures via monitoring mechanisms and more or less automatic sanctions.

If the objective is to ensure healthy and robust public finances in the euro area, it cannot be achieved only through monitoring procedures and under pressure from the financial markets. In my opinion, we have to turn the problem on its head. We need to ask ourselves what it takes to prevent countries from getting into a solvency crisis. In other words, if the goal is to have sound public finances, a country should not be allowed to be insolvent. Countries belonging to Monetary Union should be prohibited from defaulting or restructuring their debt.

The best way to prevent euro countries from defaulting is to lay down rules for debt which have constitutional weight. These rules may have Community status or be incorporated in national constitutions, as is already the case in some countries. But how to make sure that such rules are followed? How to make sure that the inevitable margins for discretion are not bypassed?

One way to ensure that the discipline is actually binding is to empower a supranational entity in the euro area to issue government bonds for the Member States. The countries would in fact no longer have the capacity, technically or politically, to issue public debt on the market. This could be a first step towards a single European bond, which would be emitted by the supranational agency to finance public budgets of all countries, or those which share similar characteristics such as the highest rating. This development would not necessarily require an integration of budgetary policies, or therefore an integrated tax system. What is in common is just the tap, i.e. an integrated system of securities for issuing on the market the proceeds from which are then allocated to individual countries, according to joint decision-making mechanisms. The European Council of Ministers, in accordance with a procedure to be specified, should decide how much debt can be issued by the agency as a whole and how to distribute it to individual states. In fact, by controlling the volume of emissions, the Council would have the power to decide the budgetary balance of individual countries. It might seem

at first glance to be a premature step in the euro area's integration policy. In reality, the current procedures already envisage the Council approving the budgets of individual countries, as part of the stability programmes presented each year by them. Its opinion is however not binding, while in our case it would indeed be so, through the decision on whether to issue debt securities. A key issue is the decision-making mechanism with which the Council would approve the total volume and that of individual states. It is therefore necessary to maintain the overall discipline of the system and avoid having to keep pace with financing larger public deficits. On the other hand, countries should have a strong incentive to limit the indebtedness of others to avoid becoming "contaminated".

I will stop here with this proposal which, I admit, is almost a provocation. Surely there is a need for more thought. But the goal must be to make financial crises less likely.

The second line of action is how to reduce the impact of a crisis in one country on the rest of Monetary Union. Crises in fact cannot be ruled out, in particular as regards the private sector, and even phases of low growth or relative decline of one country compared with the rest of the area. What matters is to prevent one country's problems from becoming problems for the others.

Crisis contagion mainly passes through the financial system, particularly banking. Europe's financial system is sufficiently integrated to transmit impulses related to a local crisis, but insufficiently diversified to permit its mitigation. Moreover, given the decentralised structure of the regulatory and supervisory systems, the impact of a banking crisis is ultimately absorbed by the national budgets. The Irish crisis shows the danger of a fragile banking system becoming interwoven with fragile public finances.

To reduce the dependence of the euro area as a whole on local events the link between a country's public finances and its national banking system needs to be severed. This link stems from the assumption – mistaken as we shall see – that regulation and prudential supervision must be carried out at national level because ultimately the country's taxpayers have to bear the costs of any bank failures.

The crisis has shown that this assumption is not true. The errors and negligence arising from Irish regulation and supervision are paid by the taxpayers of that country – but they also expose others to enormous risks. The whole of Europe's banking system is influenced by what happens in that country. For example, the opaque way in which last spring's bank stress tests were carried out in Ireland has weakened the credibility of the stress tests in all the countries. In a truly integrated market supervision cannot remain decentralised because the decisions that supervisors take do not only affect national taxpayers.

The current decentralised system does not sufficiently penalise free riding, i.e. attracting to your country one part of the industry by lowering the level of regulation. In reality, taxpayers also benefit because the development of the financial sector, encouraged by deregulation, contributes to increased tax revenues that fund government spending. Only at critical stages, when a country's financial system is in trouble, do taxpayers find themselves having to compensate for the shortfall in tax revenues in that sector and in some cases seeking help from taxpayers in other countries.

There is thus a need, at least within the euro area, to reduce the incentive for the national supervisors to give preferential treatment to their national system compared with what is done elsewhere in the Union. The creation of the three European authorities in banking, capital markets and insurance is a step towards implementing a more homogeneous regulatory system. We have to see how these authorities manage to achieve a sufficiently harmonised system. The conduct of the next stress tests will be a way to verify it. A mechanism to monitor national supervisory authorities has to be established to check the way they do their work, including stress tests. It is surprising that the budgets of member countries are subject to assessments, for example by the European Commission, while banking supervision is not subject to supranational control.

The current decision-making system, based on consensus, tends to favour the positions of those who discourage transparency, the robustness of the tests, the flow of information. If the results of the next stress tests do not convince the markets that they have been done rigorously, national authorities will not be able to hide behind each other; all would lose credibility, including the newly created European Banking Authority. It inevitably would create the conditions for a subsequent institutional step, aimed at further transfer of sovereignty in respect of European supervisory affairs.

Looking ahead, we must – in my opinion – create the foundations for a more integrated mechanism, funded at European level, for preventing and resolving banking crises. Leaving crisis resolution to voluntary cooperation is not sufficient to prevent contagion between banking systems and between them and the public debt of member countries. The pooling of the costs arising from any erroneous assessments by supervisory authorities would entail a joint assumption of responsibility by these authorities. If we want to avoid any recurrence of a crisis like the Irish one, it is necessary to provide for an integrated European supervisory system, limiting the scope for discretion by the national authorities and subjecting them to close monitoring. The consequences of an oversized and highly indebted banking and financial system are not in fact suffered only by the citizens and taxpayers of that country but by everyone in the euro area.

One of the practical problems when following this path is that banking regulation is an issue that affects the entire Single Market, involving the 27 EU countries, not just those of the euro. Opposition to this integration in the banking sector mainly comes from countries outside the euro area. It requires therefore the ability and strength of the euro countries to give themselves greater powers with regard to their area which, as I said earlier, involves a much greater degree of political integration.

Conclusions

The euro's situation has changed in these past 12 months. Important decisions have been taken. The area has a system of checks and balances that others do not. I wonder sometimes what would happen if all the members of the European Council always thought along the same lines. It might seem an ideal world in which decisions would be taken quickly. But in what direction? If everyone thought in the most rigid and uncompromising way we might have risked an even more serious crisis, perhaps triggered by the failure of some countries, as happened after the collapse of Lehman Brothers. If everyone thought instead in the most flexible and lax way, we would risk providing unconditional aid and encouraging indiscipline in public budgets. The counterpositions between the various institutions – the Council, Commission, Parliament and Central Bank – and the internal discussion between the various members would permit the taking into account of various viewpoints, especially those of creditors and debtors, and allow the inclusion of the Community and intergovernmental approach as well as a combination of rules and discretion.

In recent months, decisions were taken late and often under pressure from the markets. There was a risk of immobilism and short-sightedness. These risks remain.

However, I am convinced that at times of crisis, Europe has something extra that makes it move forward in the right direction. The combination of common historical roots and the cultural diversity of its component countries, the mixture of cooperation and competition between them have been and continue to be a source of progress and wealth. I am hoping for wisdom.

Thank you for your attention.