

## Benoît Cœuré: Having confidence in Europe

Keynote speech by Mr Benoît Cœuré, Member of the Executive Board of the European Central Bank, at a conference organised by the Istituto Affari Internazionali, Rome, 26 September 2016.

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The European Union is going through a difficult phase.

The economic crisis, the threat of terrorism and the arrival of an unprecedented number of migrants are posing challenges to Europeans. The EU's responses to these challenges have not removed doubts about its ability to act coherently and effectively when common solutions are needed.

Following the UK's referendum on EU membership, Europe has become embroiled in a wide-ranging discussion about its *raison d'être*. This discussion will however not be successful if it is merely a diplomatic exercise: if Europe is about bringing Europeans closer together, it needs to relate to its citizens and listen to civil society. In other words, the *res publica* needs to be discussed in the various parts of the *forum*, not just the *Curia*, where senators met here in Rome, but also the *Comitium*, where citizens could openly debate the matters of the time. I am thus grateful for your invitation and the opportunity to speak here at the Istituto Affari Internazionali today and to engage in a discussion with you.

What I will present are observations and assessments from the perspective of a European central banker who can analyse and provide suggestions. But, as you will see, quite a number of the issues that I will discuss today lie outside the realm of central banking and can in fact only come about through political debate and ultimately political leadership.

In my view, the European Union today lacks confidence in two important ways:

First, there is a lack of confidence *in Europe*; that is, in the ability of European policies to address today's challenges, reap the benefits of globalisation while controlling its costs, and increase Europe's economic potential. This lack of confidence is reflected in the low levels of public trust in EU institutions, in the rising support for Eurosceptic parties, and was evident in the outcome of the UK referendum in June this year.

Second, there is also a lack of confidence *between Europeans*. This is compounded by a perceived lack of a strong unifying bond or joint identity as EU citizens. The divergence between national public discourses on economic governance has reached disturbingly high levels in the euro area. Sometimes, there is not even a common analysis on what has gone wrong. Policymakers are increasingly speaking about each other and not with each other.

Let's therefore set aside the preconceptions and ask ourselves how we can restore confidence *in Europe* and *between Europeans*.

First, I will argue, there is need for **resolute actions at national level**. Second, there is need to provide **clarity** and ensure **consistency** in European integration. And, third, to overcome political fragmentation, there is need to reinforce **common fora** for debating the future of Europe.

## There are good reasons to have confidence in Europe

First, I believe that there are in fact good reasons to have confidence *in Europe* and I want to mention some of them<sup>1</sup>.

Alongside the United States and China, the European Union is currently one of the three biggest economic blocs in the world, each of roughly equal size in terms of purchasing power parity. Europe protects its citizens from external economic disruption and offers them a unique social model. A social model that we can be proud of and that can inspire the world, provided we can make it sustainable.

Furthermore, we have managed to largely mitigate the recent financial and economic crisis, which for many countries in the EU was the most serious crisis since the Second World War. It was only four years ago that the euro area looked into the abyss. But today, we find ourselves in a significantly better environment. In summer 2012, financial fragmentation was at its peak but has since then strongly receded. Five Member States were in economic adjustment programmes, four of them are now again standing on their own feet. Unemployment, although still unacceptably high in some countries, declined in 2016 for the third consecutive year, and employment growth in the euro area has beaten our expectations.

The euro, despite the deficiencies in its architecture, has tangible benefits for the people of Europe. It is the second most important currency in the world, and it has delivered measurable economic benefits for Europeans since its introduction<sup>2</sup>. Investment and competition have likewise benefited from the reduction of currency risks and transaction costs. The euro protected the Single Market by eliminating the possibility of competitive exchange rate devaluations. And without the euro, it is unlikely that our small or medium-sized economies would have better weathered the global financial turmoil.

During the crisis, the euro was arguably the greatest bond holding Europeans together: the commitment to protect the single currency and the integrity of the euro area determined key decisions taken by European institutions and Member States. Its force as a common bond is also reflected in public opinion: popular support for the euro has remained high throughout the crisis. In spring 2016, support for the single currency stood at 68% in the euro area<sup>3</sup> with a majority of citizens in favour of the euro in all euro area Member States.

The ECB as the institution tasked with safeguarding the price stability of the euro has proven that it is able to act decisively within its mandate, even in very difficult situations, and to adapt its policy tools to a changing economic environment. We estimate that all other things being equal the measures we have taken since 2014 will raise the inflation rate by more than half a percentage point, on average, in 2016 and 2017. And they will help to increase real euro area GDP growth more than one and a half percentage points cumulated over 2015–2018.

Finally, the establishment of European banking supervision has brought some important improvements to the financial architecture of Economic and Monetary Union (EMU). For almost two years the ECB has now been supervising around 130 of the most significant banks of the euro area and indirectly supervising all other banks. And banks have substantially strengthened their capital positions in that time: since 2012, the CET1 ratio for significant banks, for instance, has moved up from 9% to more than 13% today. Moreover,

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<sup>1</sup> See also Cœuré, B., “The future of Europe: building on our strengths”, introductory remarks at the plenary session on “The Future of Europe” during the fifth German Economic Forum in Frankfurt, 6 December 2013.

<sup>2</sup> Consider trade, for example: some estimate that the introduction of the euro has led to a rise in trade of around 50%. See Glick R. and Andrew K. Rose, “How Much Does the EMU Benefit Trade?”, FRBSF Economic Letter, 21 March 2016.

<sup>3</sup> Standard Eurobarometer No 85, conducted in 28 Member States from 21 to 31 May 2016.

ECB Banking Supervision is operating at arm's length from banks and enforcing a level playing field in the euro area by harmonising supervisory practices.

In summary, the EU's economic potential, the euro as our single currency backed by a single, credible and effective institution and the establishment of the single supervisor are all very good reasons to have confidence in Europe.

Nevertheless, I won't deny that we need to do much better in a number of areas.

As mentioned previously, monetary policy has been very effective in supporting output and inflation. But as I have said elsewhere<sup>4</sup>, our monetary policy measures were taken on the implicit assumption that they would be transient: on the one hand, because monetary stimulus would ultimately help counter the cyclical forces depressing the real equilibrium rate and on the other hand because other economic and fiscal policies would provide cyclical support and tackle the more structural drivers of low real rates.

But if fiscal and economic policies do not in fact play this role, we risk being trapped in a low growth, low interest rate equilibrium. Moving from interest rates being "low for long" to being "low forever" would severely limit the room for manoeuvre for conventional monetary policy tools, but even more worryingly, it would threaten the contract between generations as well as risk tearing up our social fabric. Today, building confidence in Europe also means showing that together with national governments, it can steer us away from that outcome.

There are two ways in which we need to improve economic and fiscal policies. On the one hand national governments need to live up to their responsibilities for these policy areas. On the other hand, we need to strengthen economic and fiscal policy tools at European level. Let me explain this in more detail.

### **National governments need to live up to their responsibilities**

The solution to this situation must start at national level. One important cornerstone of the current set-up is the principle that responsibility for economic and fiscal policies lies largely with national governments. There are coordination tools at European level, but ultimately, decisions are made by the elected representatives at national level. Therefore, national governments need to live up to this responsibility: economic and fiscal policies need to be used more decisively so as to reduce structural unemployment and boost potential output growth in the euro area<sup>5</sup>.

Italy has taken key steps in these areas. A comprehensive reform of the labour market was carried out last year. The new rules on open-ended contracts and the subsidy for new hires seem to be having an initial positive impact on the creation of permanent jobs.<sup>6</sup> Important measures have also been taken to address the challenges of the banking sector and to reduce the administrative burden on firms and households.

However, more structural reforms are necessary in Italy as in all euro area countries. The focus should be on actions to raise productivity and improve the business environment, including the provision of adequate public infrastructure, all of which are vital in increasing investment and boosting job creation. Fiscal policies should also support the economic recovery in a sustainable way. There is room everywhere to focus public expenditure more on items which will raise productivity. Those countries that have fiscal room for manoeuvre

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<sup>4</sup> See Cœuré, B., "The ECB's operational framework in post-crisis times", speech at the Federal Reserve Bank of Kansas City's 40th Economic Policy Symposium in Jackson Hole, 27 August 2016.

<sup>5</sup> See Cœuré, B., "Structural reforms: learning the right lessons from the crisis", speech at the Economic conference organised by Latvijas Banka in Riga, 17 October 2014.

<sup>6</sup> See Sestito, P. and Viviano, E. (2016), "Hiring incentives and/or firing cost reduction? Evaluating the impact of the 2015 policies on the Italian Labour Market", Banca d'Italia Occasional Paper 325.

should use it wisely; but others that don't have such room should not bend the commonly agreed rules— that is in their own interest as well as in the interest of Europe. Stretching rules to the point where they lose credibility will not pave the way for a stronger and safer Economic and Monetary Union.

### **Clarity and consistency in integration**

This leads me to my second point: we need to strengthen economic and fiscal policy tools at European level by pursuing *clarity* and *consistency* in European integration.

*Clarity* in integration is about making it easy to understand who is responsible for what. In the current set-up, loose coordination of economic policies at European level and ad hoc intergovernmental arrangements may give the impression that a competence has been passed to the European level, when in fact it continues to be exercised largely by Member States. This opens the door to shifting the blame for unpopular measures to the EU when in fact it does not effectively have the power to adopt policies. In addition, a clearer demarcation of competences between the European and national levels would allow the EU to prove to national audiences that Europe is part of the solution and not part of the problem.

*Clarity* is also about pointing out which institution takes which decisions at European level. This is why I support the establishment of a euro area finance ministry, accountable to the European Parliament.<sup>7</sup> This body could be responsible for preventing economic and fiscal imbalances, managing crises in the euro area, as well as representing euro area governments in international economic and financial institutions.

*Consistency* in integration means assigning the competences for strongly complementary policy areas to the same level of government. We cannot partially disempower national states without creating – at Union level – the capacity to provide at least as much security to citizens as before.

Let me illustrate. The Single Market is a point in case: it requires not only the opening of borders but also joint rules to ensure financial stability and a level playing field with fair competition. And joint rule-setting requires enforcement and judicial review, that is, supranational sovereignty sharing and political procedures that lead to common decisions.

And there are some good recent examples where the EU has exercised its power in this area for the benefit of European citizens. Take the recent state aid decisions by the Commission on some national tax schemes or the progressive abolition of roaming charges across the EU.

*Consistency* in integration is equally important – if not more so – for the half-finished construction of EMU. I understand very well, as a European citizen, why political attention is today focused on security and addressing the challenges of migration. But Europe will not build the resources needed to protect itself and manage migration flows without a strong and sustainable economy. Making our Economic and Monetary Union strong and sustainable requires a complete banking union and elements of a fiscal and economic union. None of us want to live in a half-built house because it will get very uncomfortable as soon as the next storm hits. We need to work on completing EMU also after Brexit.<sup>8</sup>

Today, there are clear disagreements on the balance between private and public risk-sharing, on the mix of national and EMU-wide responsibilities, and on the speed towards

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<sup>7</sup> See B. Cœuré, “Drawing lessons from the crisis for the future of the euro area”, speech at “Ambassadors Week”, Paris, 27 August 2015.

<sup>8</sup> See the Five Presidents' Report and, more recently, Enderlein, H., Letta, E. et al. (2016). “Repair and Prepare: Growth and the Euro after Brexit”, Gütersloh, Berlin, Paris: Bertelsmann Stiftung, Jacques Delors Institut Berlin and Institut Jacques Delors in Paris.

possible new arrangements. This discussion will take time. In my view, it should be embedded more broadly in a new convergence process, as suggested in the Five Presidents' Report. Significant progress towards common convergence criteria would be regularly monitored and would be a condition for members to benefit from further risk-sharing instruments. This way the convergence process would set a clear incentive structure for Member States to overcome the current deadlock and would establish full transparency about the design of EMU.

However, for new projects and further integration steps there must be a consensus that joint action is truly necessary and linked to people's needs. And we know from surveys<sup>9</sup> that there are areas where citizens would like the EU to become more active than at present.

On that note, I want return very briefly to an aspect that is really for another speech or maybe even another speaker – someone not from the central banking world – to address. It is the lack of confidence *between* Europeans.

### **Common fora for debate**

As I have said before, we need to be honest with ourselves: the Single Market and Economic and Monetary Union are not technocratic mechanisms but inherently political undertakings. And as political undertakings they require support and acceptance beyond the legitimacy gained via elected national governments or even through the provision of effective and efficient solutions. As laid down in the Treaty, supranational law and supranational institutions assume that we are not only nationals of our respective countries but also citizens of Europe. Being European citizens is in turn linked to a feeling of common identity.

The late President Ciampi embraced this principle emphatically:

*Our common historical legacy, the awareness of possessing a European identity, our membership of a single value system, the principle of shared sovereignty mark out European citizenship and identify the European Union; they underpin its institutional, political and economic scaffolding.*<sup>10</sup>

A common identity allows us to accept that the political undertakings we pursue together can temporarily produce losers and winners. It enables the minority to accept the decisions taken by the majority. When such an acceptance is not there but only national interests and national perspectives prevail, then confidence *between* Europeans is seriously undermined. One way of strengthening these conceptual underpinnings of Europe in my view would be to create more space for common debates on European issues.

Let me be clear: having common debates should not be understood as having the same view at all times. It is absolutely normal to disagree and it is entirely natural considering that the people of Europe have different histories, have grown up in different circumstances and express a wide variety of preferences. However, the problem starts when we are having 28 or 19 different discussions without channelling them into a common debate. Too often, domestic media and political actors take a national perspective in these debates. Too often the debtor-creditor dichotomy overshadows the debate of how we want to organise the economic governance of the euro area in the future.

The result is a fragmentation of the democratic debate on Europe. This fragmentation is heightened by intergovernmental decision-making that involves endless negotiations and highlights the differences between the positions of various Member States. And such a fragmentation of our discourse sets a trap: the more divided we become over common solutions, the less effort we put into implementing them. As a result, Europe cannot deliver

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<sup>9</sup> Special Eurobarometer of the European Parliament, conducted in 28 Member States from 9 to 18 April 2016.

<sup>10</sup> See C.A. Ciampi, "The Identity and the Unity of Europe", Lecture at the University of Leiden, 5 March 2003.

effectively and European policies, once again, appear ineffective. This only adds to people's impatience and dissatisfaction with Europe, making it even more difficult to find effective European solutions.

To overcome this fragmentation we need to reinforce our common fora for debate. The European Parliament is an important element, but we should foster dialogues between Europeans also outside of existing institutional structures.<sup>11</sup> The result should be a positive "politicisation" of the EU<sup>12</sup>, on which I understand analytical work is also being carried out here at the institute.

## **Conclusions**

Confidence in Europe and among Europeans is low. And there are clearly areas where we need to do much better. National governments need to live up to their responsibilities for fiscal and economic policies, and we need a clear and consistent path of integration to avoid half-built houses and allow Europe to deliver. A new convergence process can offer such a path to break the deadlock. And achieving this goal will be much easier if we strengthen our common fora for debate and decision-making.

This requires political leadership. But it also will help to meet citizens' demands for a more effective Europe. We should have confidence in Europe. As Winston Churchill once said, "For myself, I am an optimist – it does not seem to be much use being anything else". I now look forward to your questions and our discussion.

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<sup>11</sup> See Cœuré, B., "Towards a political convergence process in the euro area", speech at the Interparliamentary Conference "Towards a Progressive Europe" in Berlin, 16 October 2015.

<sup>12</sup> See Pirozzi, N. and Tortola, P. D. (2016), "Negotiating the European Union's Dilemmas: Proposals on Governing Europe. Istituto Affari Internazionali Working Paper 16/24.