Benoît Cœuré: Making our monetary union stronger and more resilient

Speech by Mr Benoît Cœuré, Member of the Executive Board of the European Central Bank, at the Finanzmarktklausur of the CDU Wirtschaftsrat, Berlin, 14 March 2018.

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Let me thank the organisers for inviting me here today.

Our common monetary policy has been much discussed in recent years, also here in Germany, where the highest court has been asked to examine the lawfulness of some of our measures. While the European Court of Justice has confirmed that the ECB has acted at all times within its mandate, many of the institutional failings which caused and perpetuated the crisis, and which contributed to the ECB adopting a series of unconventional policy measures, remain unresolved.

These shortcomings are well known. When there's growth and the sun is shining, euro area Member States have few incentives to pursue sound policies and keep their economies productive and flexible enough to prosper in a monetary union on a sustainable basis. This leaves them vulnerable when rainy days come.

In such an environment, where the governments of the 19 Member States have retained core responsibilities in crucial areas such as fiscal policy, business environments and labour market policies, the central bank can quickly become a scapegoat or be the focus of unrealistic expectations. Worse, there is hardly a single European public discourse in which the common monetary policy can be communicated. Take the title of this panel as an example. The connotation that people attach to the term "Nullzins" will likely be different from, say, "geldpolitischer Impuls" – although both terms in essence describe the same thing.

Worse, monetary policy can quickly become overburdened if national fiscal and economic policies fail to internalise the effects they have on the common currency. The temptation to free-ride is always present in a monetary union. It is easy to see that if fiscal policy is loosened during an expansion, or tightened during a recession, the burden on the central bank to stabilise the economy increases mechanically.

Even today, euro area growth still relies too much on monetary policy support. According to ECB staff estimates, the contribution of our easing measures to annual euro area GDP growth was half a percentage point in 2017 and will still be around one-third of a percentage point in 2018. And monetary policy can do little to lift the long-term growth rate of our region.

All of this means that our currency union needs further reform – both at Member State and euro area level. I believe there is wide agreement on this. Where we still lack agreement, however, is on how these reforms should look in practice.

I have described elsewhere the requirements of reform from the perspective of the single monetary policy.[1] As the central bank of the euro area, we have a stake in the success of the current discussion. Without further reforms, and depending on the nature of the next crisis, we may well be forced to test the limits of our mandate – a concern that has been voiced by Germany in particular.

I offered three "lines of defence" that any well-functioning monetary union depends on: flexible markets, adequate national fiscal buffers and a common fiscal instrument to cope with large shocks.

The logic is simple and compelling. Flexible markets for goods, services, labour and capital reduce the need for costly macroeconomic stabilisation and curb contentious debates about crisis management. They reduce both the likelihood and impact of shocks and allow economies to bounce back more quickly. And they save much of the precious political capital governments had to spend on acrimonious crisis discussions.

But flexible markets come at a price. In a downturn, they often impose economic hardship on workers through job losses or wage cuts. Governments can mitigate these effects. Unlike the United States, however, the European Union is not a federation. This means that – as a rule – stabilisation needs first to take place at Member State level. Building and maintaining adequate room for action at national level is therefore essential. This is what our fiscal rules are about. And contrary to common perceptions, this is not only about bringing general government deficits under the 3% line, but it is also about bringing them closer to balance or to surplus in the medium term so that fiscal space can be used in the event of a recession.

But even ex ante solvent governments can come under pressure in the face of very large shocks. Absent national stabilisers, such as an autonomous monetary policy and exchange rate, such shocks have already tested the cohesion of the currency union as a whole. This is why a common monetary policy needs a complement in the form of a common fiscal instrument that can support – under proper democratic control – aggregate demand if need be.

Many of the Economic and Monetary Union (EMU) reform proposals that are currently being discussed would help bolster these three lines of defence.

Enhancing national ownership of structural reform efforts, for example, could help make our economies more agile. A true capital markets union, leveraging the benefits of fintech innovation, would significantly boost the capacity of our financial markets to diversify and reduce risk, while the ECB has often argued that a European deposit insurance scheme is a precondition for a truly integrated banking system and safe money. And the Single Market still has a lot of untapped potential, in particular in the field of services. These should be priorities.

More credible fiscal rules and greater market discipline would strengthen the second line of defence. A nimbler European Stability Mechanism, meanwhile, together with steps towards an area-wide stabilisation budget, could effectively complement the euro area’s institutional architecture.

Reforms along these lines are needed to help us create a more stable and safer currency union.

A stable, resilient and more integrated euro area is in everybody’s interest, including, and maybe especially so, Germany’s. That is why Germany for decades joined forces with its European partners to strengthen the European Union, including by establishing a monetary union. It is reassuring to see that the coalition agreement gives strong support to the European project. Indeed, governments and parliaments of Member States, together with the European Parliament, must be the driving force in this process.

This is particularly important at a time when the multilateral order based on cooperation is being challenged, at a time when one of Germany’s long-standing partners, the United Kingdom, is about to leave the European Union, and at a time when anti-European forces, elected and unelected, in other parts of the Union are calling into question not just the EU’s four freedoms but also the values of an open, free and democratic society.

In this environment, Germany, as one of the founding members of the Union, has a responsibility to promote and nurture a reform debate that is constructive and that will help to bridge differences of opinion. A strong Franco-German commitment is a necessary condition for moving forward, but all Member States have to be on board. It means that we should move beyond the north-south divide which has too often shaped past discussions on EMU. Economic fragmentation is receding on our continent, thanks to a broad cyclical recovery, the ECB’s actions and the bold reforms initiated in several countries. We should be careful not to allow political fragmentation to jeopardise these achievements.

Ultimately, what matters is that we strike the right balance between solidarity and responsibility and that we embrace a vision which secures the integrity and resilience of the euro area. We all know that this is not easy. But failure to do so would leave the ECB alone at the forefront of macroeconomic stabilisation in the euro area. This is a risk not worth taking.

Thank you.

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[1] See Cœuré, B. (2018), “The euro area’s three lines of defence”, speech at the conference “Deepening of EMU”, Ljubljana, 2 February.