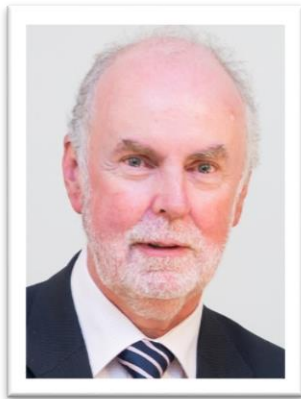




Completing the Architecture of the Euro

Opening remarks Governor Jan Smets, Belgian Financial Forum,
Brussels, 18 November 2016



Jan Smets, Governor National Bank of Belgium

Ladies and gentlemen,

Thank you for allowing me to take the floor for a few minutes to share some thoughts with you on EMU and the way ahead. We are quickly approaching the 25th anniversary of the Maastricht summit of December 1991, which provided for the initial architecture of Europe's economic and monetary union. It would be an understatement to say that the following quarter century has been more turbulent than most of the Maastricht Treaty negotiators had expected.

The euro area crisis led to profound debates and rekindled the issue of the relationship between monetary union and political union. This book, "Architects of the Euro" is then very timely, as it places these discussions in a broader historical context. I would like to commend Kenneth Dyson and Ivo Maes for their excellent job.

Over the last few years, there have been significant reforms in economic governance in the euro area. Moreover, a new blueprint for EMU, "Towards a Genuine Economic and Monetary Union", was drawn up by a committee chaired by European Council President Herman van Rompuy. The report put forward a vision for EMU with a banking union and moves towards a political union to complement its economic and monetary arm. This vision has been elaborated and refined in the so-called "Five Presidents Report" published in June 2015.

It was not the first time that these types of ideas have been formulated. In fact, they are close to the traditional Belgian vision of a symmetric economic and monetary union. They were already clearly present in the January 1970 Snoy Plan, named after the then Belgian Finance Minister. The Belgian plan argued that for a "European monetary community" two conditions had to be fulfilled: a unification of economic policies and a certain homogeneity of the economies of the Member States. It further emphasised that the establishment of two new supranational Community institutions was



essential for the final phase of EMU: a "Community Monetary System and a supranational European economic government, with the necessary powers to conduct a single economic policy". Moreover, the Community budget should gain in importance and certain Community transfer mechanisms should be developed.

Where are we now, 46 years later? We have made considerable progress, let us keep that in mind, especially in the uncertain times we live in:

- in the euro area we share a single currency, which has brought about more efficiency and more stability, and has become the second major currency in the world.
- we now have a real federal European institution, the European Central bank, the policy of which has made a crucial contribution to the economic recovery, and that has proved to be efficient, as it has improved credit conditions throughout the euro area and reduced financial fragmentation.
- economic fragmentation between the member states has decreased.
- a banking union has been set up providing unified supervision.
- there is also a Single Resolution Mechanism.
- governance as to fiscal discipline and macro-economic imbalances has improved.

All that has made us more resilient.

But we should remain vigilant. We are in the middle of the river and there is still a whole area to be crossed to reach the other side, to have all the required coherent instruments needed for the optimal functioning of a monetary union:

- the banking union is still to be completed by a backstop for the Single Resolution Fund, and the third pillar, a deposit insurance system.
- we need a capital markets union. This is important to deepen the internal market and thus to be a source of economic growth and extra benefits from our common currency. CMU is an ambitious project as it will take a long time to transform the bank based Euro area economy to one closer to the markets based American system. For its realisation it is important to tackle thorny but important issues such as the harmonisation of insolvency law and taxation. It will also strengthen cross-border risk-sharing through deepening integration of bond and equity markets, strengthening the euro area's resilience in the face of asymmetric shocks.
- and in the final EMU blueprint, a need for a public euro area insurance function to help cushion asymmetric shocks, as already proposed in the 1970 Snoy Plan, will remain. Of course, a euro area budget should not lead to permanent or one-way transfers and should not undermine the incentives for sound economic policymaking. Moral hazard should be avoided.



In general terms, all these risk sharing mechanisms have to be accompanied by mechanisms of risk reduction. Solidarity should go hand in hand with domestic ownership and national responsibility.

What does this imply? This implies

- due respect of the provisions of the stability and growth pact. The communication of the European Commission earlier this week shows that unfortunately there is still a lot of work left to be done. This is detrimental to the countries themselves, as they thus vouch insufficiently for the sustainability of their budgets, the capacity to address the challenge of ageing populations and consequently also for the confidence held by their populations. And they considerably complicate the possibility to accompany the monetary policy, as should be proper, through an adequate euro area fiscal stance, for in numerous, perhaps even in most member states of the euro area, there is not enough room available.
- risk reduction in the banking system, by an adequate approach to non-performing loans which hinder recovery, but also by weakening or even removing the doomed loop between banks and their sovereigns.
- and, last but not least, unremitting efforts by the member states to focus their economic policy on a stronger growth potential, more innovation, a more appropriate functioning of labour markets, the enhancement of real productivity.

The political consensus on all these issues now seems rather far away, which is unfortunate but is also a real risk. We are faced with divergences as to the right balance between risk reduction and risk sharing. In addition, Europe is faced with shocks moving towards disintegration, the most material expression being the Brexit.

But especially in these circumstances, in times of major uncertainty, we now more than ever should convince our populations that we are indeed pursuing the right policies and reinforce the basis of our joint action.

As often observed by Alexandre Lamfalussy, one of the great architects of the euro, “we are better at crisis fighting than at crisis prevention”. However, as also argued by Lamfalussy, it would be the wrong lesson of history to become complacent. On the contrary, we should take this moment to strengthen the resilience of EMU and complete its architecture.

History teaches us that it would be unwise to wait for a new crisis to do this. The book on the architects of the euro shows that, whatever their background, the architects cooperated to make a success of this historical project. They accepted the trust which Europe’s leaders had bestowed on them, to advance the European integration project. Let us build further on that trust.