Economic and monetary union

SUMMARY

Launched almost three decades ago, economic and monetary union (EMU) represents a very important step in the process of European economic integration. However, the recent sovereign debt crisis highlighted its incomplete design and some inherent instabilities. A series of measures were therefore taken to deepen EMU and thereby to increase its resilience. They can be grouped in three main categories: monetary measures, measures intended to complete the single market, and measures aimed at strengthening the economic union dimension of EMU. The current coronavirus pandemic has shown the urgency of many of them; recently submitted important proposals could lead to a noteworthy evolution in the architecture of EMU. This Briefing groups and highlights some of these proposals. The table at the end features a number of additional proposals in summary form.

Launch of economic and monetary union

Launched by the Treaty of Maastricht in 1992, economic and monetary union (EMU) involves the coordination of economic and fiscal policies and the launch of a single monetary policy for a common currency, the euro, which became legal tender in the participating EU Member States (the 'euro area') on 1 January 1999. Today, the euro is used in 19 of the 27 Member States – by more than 340 million people. It is the second largest international currency after the US dollar and, as such, it has been instrumental in ensuring price stability, fostering trade within the EU and increasing resilience in turbulent times. The Treaty of Maastricht introduced economic convergence criteria for countries wishing to join the euro area, as well as rules to protect the integrity of EMU (notably a no-bailout clause). It has since been complemented by primary legislation – for example, the Treaty on Stability, Coordination and Governance, TSCG, in 2012 – and secondary legislation – for example, the Stability and Growth Pact, SGP, in 1997. The latter has itself been significantly amended, in 2005, and in 2011 with the 'six-pack', and in 2013 with the 'two-pack', sets of legislative measures. The single monetary policy lies within the remit of the euro system, which acts independently from political influence and is tasked with preserving price stability by keeping inflation under, but close to, 2 %.

First 20 years of EMU

First decade (1999-2009)

The years between the introduction of the single currency and the global financial crisis are generally considered to have been a positive period for euro-area economies. The value of imports and exports of goods within the euro area increased, as did trade in intra-euro-area services. EMU also contributed to an increase in trade flows with non-euro-area countries. Inflation rates within the euro-area countries decreased significantly and converged among them. Low and stable interest rates substantially reduced the costs of servicing public debt for national governments.

In addition, EMU was associated with a substantial increase in cross-border financial integration across the euro area, which lowered transaction costs in equity and corporate bond markets and

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expanded volumes of financial assets. At the same time, spreads in government-bond markets narrowed and tended to move together. While retail banking activities remained fragmented, inter-bank markets showed considerable integration. The international use of the euro increased and remained relatively stable, despite the geo-political challenges facing the EU and the 2007-2009 global financial crisis.

European sovereign debt crisis (2010-2014)

The 2010-2013 sovereign debt crisis laid bare the incomplete design and inherent instabilities of EMU, with yield spreads shooting up to levels never registered before, since its launch, and the international use of the euro declining for the first time since its adoption. The EU's reaction came in the monetary domain (by the European Central Bank, ECB) as well as in the financial and fiscal domains. EU leaders resorted initially to extending bilateral loans to the countries in distress, before increasing the number, scope, lending capacity and tools at the disposal of EU supranational issuers (notably the European Financial Stabilisation Mechanism – EFSM, the European Financial Stability Facility – EFSF and the European Stability Mechanism – ESM). As a counter-balance, EU leaders strengthened the regulatory framework for EU economic governance – specifically the measures taken to enhance fiscal and macroeconomic surveillance (the 'six-pack' and the 'two-pack' reforms; the macroeconomic imbalance procedure; and the Treaty on Stability, Coordination and Governance) and the enhanced supervision of EU banks (banking union). For its part, the ECB adopted unconventional monetary policy measures (longer-term refinancing operations (LTROs) and the securities markets programme) and signalled that it would do 'whatever it takes' to preserve EMU and its single currency. These measures strengthened the system and increased the euro's resilience, as demonstrated by the broad stabilisation of its international use after 2013.

Initiatives following the crisis (2015-2019)

To exit the crisis, enhance EMU and further increase its resilience, several initiatives were taken after 2015. These can be grouped in three pillars.

The goal of the first pillar was to complete the single market.[1] Here, the most important new policies were banking union and capital markets union. Banking union originated from the observation that the sovereign debt crisis in most EU Member States (apart from Greece) started as a banking crisis. The goal therefore was to break the link between banking crises and sovereign debt crises, by adopting common prudential rules for banks and common mechanisms for the resolution of banking crises and deposit insurance, while also centralising bank supervision and resolution for major euro-area banks. This was also instrumental in restoring the proper functioning of the interbank market and facilitating single monetary policy transmission. The capital markets union built on the impetus created by the banking union, and sought, among other things, to increase capital flows across the EU and to contribute to reducing and sharing financial risks.

The second pillar related to economic (and/or fiscal) policies, where – in parallel to strengthening the existing economic governance framework through the ESM and the amendments to the Stability and Growth Pact (SGP) – proposals were formulated on how to further integrate frameworks for budgetary matters and economic policy, while also adding greater democratic legitimacy and accountability to the process. An important milestone in this process was the European Commission's 2015 report (or 'Five Presidents' Report') on 'Completing Europe's Economic and Monetary Union',[2] based on which initiatives were proposed in two main waves, the first in 2015 and then in 2017. Finally, given that the recovery from the crisis in terms of GDP and employment growth was not shared equally among EU citizens within and among Member States, EU leaders proclaimed the European Pillar of Social Rights at the Gothenburg Social Summit in November 2017.

In the third pillar (monetary policy), the ECB followed the example of other central banks (for example, the US Federal Reserve and the Bank of England) and engaged for the first time in quantitative easing through its public-sector purchase programme (PSPP).

The coronavirus pandemic

In less than three months earlier this year, coronavirus evolved from a localised outbreak in China to a global pandemic, severely affecting the lives of millions and dealing a huge blow to economies worldwide. The particular characteristics of the virus, as well as the absence of a vaccine or treatment, prompted most governments to impose strict containment measures, to allow their health systems to cope with the increase in cases by 'flattening the curve'. To limit the economic damage during confinement, Member States' governments put large programmes in place to support companies (to avoid bankruptcies), and workers (to dampen income losses and avoid a surge in unemployment), as well as measures to avoid a financial meltdown. The national liquidity measures, including schemes approved under temporary and flexible EU State aid rules, currently exceed €2.5 trillion.

Member States' actions have been complemented by actions at EU level that include: the activation of the SGP's general escape clause to (temporarily) give national governments greater flexibility to adopt counter-cyclical budgetary measures for their economies; the related simplification of information requirements for the 2020 cycle of the European Semester; the adoption of a temporary framework for State aid measures to accelerate public support to companies; and a banking package (targeted amendments to the prudential rules and an interpretative communication) to facilitate lending to households and businesses.

The shock dealt by the pandemic to EU economies could be described as symmetric (it hit most countries the same way); however, the fact that Member States are in different debt situations risks rendering it asymmetric. Despite the amendments to the State aid and public-finance rules, the immediate fiscal stimulus provided by some Member States (for example, Italy and Spain) as a first reaction to the lock-downs was more timid than that provided by others, such as Germany. It was therefore feared that, if the EU response to the crisis limited itself to this timid relaxation of measures, it could lead to persistent economic, financial and social divergences between Member States, to severe distortions within the single market and potentially to a new sovereign debt crisis. For these reasons, further actions at EU level were put in place.

Fiscal measures

Proposals for three additional 'safety nets' were then put forward on 9 April 2020, as follows:

- the launch of SURE, a new €100 billion initiative aimed at protecting employment in the EU by supporting efforts to mitigate unemployment risks during the pandemic emergency period. This would be achieved by covering some of the costs of national public programmes that allow firms to reduce working hours, while at the same time providing income support;
- the creation by the European Investment Bank of a €25 billion pan-European guarantee fund to protect companies in the EU. The fund is expected to generate up to €200 billion in loans throughout the EU, primarily for SMEs;
- the provision, through the ESM, of loans to euro-area Member States of up to 2 % of their GDP (worth €240 billion in total), with little conditionality, on the basis of an existing precautionary credit line (the enhanced conditions credit line) adjusted in light of the pandemic.

In addition, a joint Franco-German proposal has been submitted for a €500 billion recovery fund to restart the EU economy. The fund would issue bonds and finance expenditure in the hardest-hit countries and sectors. Given the legal constraints on the EU budget, this amount would be raised by increasing the expenditure ceiling of the EU multiannual financial framework (MFF) from approximately 1 % to 2 % of gross national income (GNI) for the next three years.[3] The fund would thus be integrated into the EU budget and would serve to finance expenditure in the healthcare sector, while potentially also contributing to the green transition and helping the Member States most affected by the crisis. In line with the major Franco-German initiative, on 27 May 2020 the European Commission published a proposal to add temporary financial reinforcement through a €750 billion recovery instrument, 'Next Generation EU', alongside a revised proposals for the 2021-2027 MFF. The Commission plans to use its high credit rating to borrow the amount on financial markets, invest it across three pillars[4] through €500 billion in grants and €250 billion in loans, and repay the total amount over the 2028-2058 period through future EU budgets and from resources raised from new EU own resources.[5] As in the case of the Franco-German proposal, to enable borrowing at the envisaged level, the Commission plans to increase the own resources ceiling[6] on an exceptional and temporary basis, to 2 % of Member States' GNI. This latter measure is controversial, as it marks a departure in some Member States from previously expressed objections related to common debt issuance and transfers across Member States. Some commentators argue that these developments may represent a 'Hamiltonian Moment' for the European integration process, even if achieving the necessary agreement will require overcoming some long-standing differences of approach between Member States.[7]

Monetary measures

Since the outbreak of the coronavirus pandemic, the ECB has taken several measures to support the euro-area economy. To increase banks' lending capacity and to support markets, it has temporarily relaxed bank capital requirements[8] and rules under which loans are classified as non-performing.[9] Further, it has re-established its swap line with the US Federal Reserve.[10] To prevent runs in the money markets, it has announced it will conduct 'pandemic emergency long-term refinancing operations' (PELTROs) that will provide liquidity to banks and money market funds until September 2021.[11] That adds to expanded Targeted LTROs (TLTROs) offering to banks cheap, long-term loans to be used to lend to euro-area consumers and businesses.[12] To make participation in the programmes easier, the ECB has broadened the array of collateral it will accept.[13]

In addition, it has kept its negative interest rate policy: the deposit facility, the rate that banks receive for their deposits at the ECB, is currently at -0.5 %. The ECB has further offered forward guidance on the future path of its key interest rate,[14] in effect putting downward pressure on longer-term rates.

Lastly, the ECB has continued its purchases under its existing public-sector purchase programme, with the aim to push inflation up to its target;[15] furthermore, in March 2020, it launched a €750 billion pandemic emergency purchase programme (PEPP), which was increased to a total of €1 350 billion in June 2020.[16]

Going forward

The coronavirus crisis is not yet over and many new initiatives have been launched since March. While some of them are significant and could barely have been imagined at the beginning of 2020, many more have been identified in recent years as key to enhancing EMU in different ways. These initiatives too can be grouped depending on whether they refer to monetary policy, to economic policy or to the single market.

Further initiatives to strengthen economic union

Fiscal rules

Policy-makers can adjust fiscal policies to respond to unforeseen events in a timely manner, but this also carries the risk that their policy choices may entail significant costs. That is why the EU has constantly put limits on this discretion since the adoption of the Maastricht Treaty. Numerical fiscal rules, independent fiscal councils monitoring compliance with these rules, and clear coordination procedures are the main features of an effective surveillance mechanism.

Many economists view binding fiscal rules as necessary in a monetary union, because the markets do not, by themselves, discipline spendthrift governments until it is too late. Also, research has shown that countries with stricter fiscal rules have, on average, had lower deficits compared to countries without rules, and that fiscal rules have played a supportive role in many cases of large fiscal adjustments. As mentioned previously, such rules were first introduced at EU level with the Treaty on European Union and were subsequently included in the SGP, adopted in 1997 and extensively reformed since. The unwanted result of these reforms was the SGP's increased complexity: economists note that the current framework is not as effective as it could be, because it has two objectives (government deficit and debt), multiple ways of defining adjustment toward the medium-term budgetary target (the structural budget balance and the expenditure benchmark), various methods of assessing whether a country has complied with the recommended adjustment, and many exceptions. This has contributed to a poor compliance record in relation to the fiscal rules. As a result, there is an ongoing debate on the SGP's simplification, with three main ideas emerging in 2018 from various groups of economists.

One proposal would keep a long-term debt limit (for example, the 60 % debt limit) and an obligation to avoid excessive structural deficits in the medium term (the current structural budget rule), but to ensure compliance with this rule, a multi-purpose adjustment account would be created, which would capture deviations from the rule that Member States would be required to off-set within a certain period of time. These goals would be operationalised by an annual growth ceiling on nominal expenditure (a modified version of the expenditure benchmark). In addition, the number of exemptions and escape clauses would be reduced, as would discretion with regard to the imposition of sanctions, to increase their credibility.

A second proposal would replace the numerous and complex existing rules with one simple rule focused on limiting the annual growth rate of expenditure. This rule could stipulate that the growth rate of nominal public spending – net of interest payments and of unemployment spending and taking into account public investment – would be equal to the sum of real potential growth and expected inflation, minus a debt brake which would take into account the difference between the observed debt-to-GDP ratio and the 60 % debt rule. This rule would be based on a rolling five-year country-specific debt reduction target, so as to take into account the speed at which Member States would have to converge oo the long-term target.

A third proposal would rely only on the Maastricht Treaty's 60 % debt limit. This would be operationalised by placing a constant ceiling on the growth rate of primary nominal expenditure, net of discretionary revenue measures, ensuring that the debt ratio would reach the target in a given period under specific assumptions of growth and inflation. The ceiling, which this way would include a built-in debt brake, would be fixed for a three-year period, at the end of which it would be calculated anew, to take into consideration the effort needed to reach the reference value.

Policy coordination

Apart from the fiscal rules themselves, issues have also been identified with the EU's main economic policy coordination tool, the European Semester. Indeed, not only is compliance with the recommendations issued in the context of the Semester rather low, but, more worryingly, the trend is worsening. To remedy this, one proposal suggests a stronger analytical foundation for the country-specific recommendations matched by a higher level of engagement with national stakeholders. Another proposal welcomes the trend towards involving national fiscal councils and productivity boards in the Semester process, but stresses that their independence must be guaranteed both vis-à-vis their national governments and the EU, as otherwise the country-specific recommendations may still be perceived as being imposed by the EU.

In the short term, another important issue will be to integrate the United Nations' Sustainable Development Goals (SDGs) in the European Semester - a task entrusted to the Commissioner for the Economy, Paolo Gentiloni, and discussed at the Environment Council of 5 March 2020. The Sustainable Development Goals, 17 in all, were agreed in the context of the UN 2030 Agenda for Sustainable Development, and address global challenges such as poverty, inequality, climate change, environmental degradation, peace and justice. They are to be achieved by 2030. In this context, a recent paper noted that, just as fiscal rules rely on numerical values (the 3 % deficit and 60 % debt rules), the achievement of the SDGs 'could rely on "sustainable development pathways" defined for each Member State'. The paper further proposes that, just as fiscal parameters and coordination are dealt with by the Commission (DG ECFIN), in cooperation with the fiscal boards established in each Member State, the SDGs could be coordinated by the national productivity boards. Those institutions could be tasked with showing how national reforms – and the domestic transposition and implementation of EU rules – are contributing to the achievement of the SDGs.

Independent fiscal institutions

In addition to fiscal rules and the European Semester, some consider that the role of the independent fiscal councils (IFCs) must be enhanced, so as to reduce political incentives in the implementation and evaluation of compliance with the fiscal rules. In this sense, one proposal would aim to ensure that these councils are provided with the necessary resources, are guaranteed access to information and are provided with adequate media visibility. Following this, stronger use should be made of these councils, by delegating to them some of the necessary analytical work and by entrusting them with making recommendations to their governments on how to correct fiscal policies that violate the rules. A final step would involve the establishment of a European Fiscal Council, with a mandate to safeguard the proper implementation of the fiscal framework, focusing on gross errors and cross-border spill-overs. Its decisions would not be binding, but they would be made public.

A similar proposal suggests that the competent authority (for example, the European Stability Mechanism) point out breaches of the rules, compute adjustment paths according to terms agreed in advance, and recommend steps to be taken. The proposal notes that a *sine qua non* condition is that the independence of the ESM in this area be guaranteed.

Another proposal advocates enhancing the current requirement in the TSCG that euro-area countries establish independent fiscal councils (IFCs), based on three elements: i) the IFC should be in charge of putting the government's budgetary decisions into numbers; ii) the IFC should be tasked with determining whether the government's choices are compatible with fiscal discipline (as defined in the Member State's constitution), and its view should be taken into account by the parliament when it votes on the budget; and iii) the members of the IFC should be chosen on the basis of explicit criteria that focus exclusively on competence and non-partisanship, so that their competence (and the competence of the IFC) is beyond doubt.

EU unemployment benefit (re)insurance scheme

Lastly, given that national fiscal policies and the common monetary policy have limited capacity to mitigate the effects of asymmetric economic shocks, and that labour mobility in the EU is low (albeit increasing since the financial crisis), an important project is the design of a European unemployment benefit reinsurance scheme that could contribute to macro-economic stabilisation and efforts to address unemployment and encourage labour mobility. The creation of a stabilisation fund for national unemployment insurance schemes (a supranational automatic stabiliser) is not a new idea, but it has gathered momentum since the sovereign-debt crisis. The current pandemic has provided further impetus, and the SURE initiative could be considered a first step in this direction.

There are several variants of such a scheme. A recent paper groups them in two categories: 'genuine' unemployment benefit schemes would pay out benefits directly to any eligible unemployed individual, and collect contributions from employers and employees. Such schemes would require considerable harmonisation of the existing ones in the Member States, to ensure the European scheme can work as a stabiliser and mitigate moral hazard. In the case of the second category – a 'reinsurance' scheme – financial transfers would occur between the supranational fund and the Member States, which would only receive a pay-out when the scheme is triggered. This scheme would provide more flexibility to the Member States and would be more politically palatable, as it would demand less in terms of the social and fiscal sovereignty of Member States. The paper identifies, for both categories, the legal bases that could be used to create the schemes, the relevant legal and operational constraints, as well as (for reinsurance schemes specifically) the financing modalities and trigger conditions.

Another recent paper develops a framework to single out and quantify the smoothing potential of such a scheme among Member States and over time. The paper finds that, in the 2000-2016 period, a reinsurance scheme would have absorbed, through the smoothing channel, on average 15-25 % of the income losses originating from rising unemployment in deep recessions among Member States, in addition to the smoothing that can be achieved at Member-State level over time. Moreover, due to its activation and contribution rule, a reinsurance scheme would not have led to permanent transfers across Member States.

Further initiatives to complete the single market

European deposit insurance scheme

Along with the Single Supervisory Mechanism and the Single Resolution Mechanism, the European deposit insurance scheme is seen as a pillar of banking union. Such a scheme has been praised by proponents as being capable of bringing increased depositor protection, and – by increasing the credibility of insurance – of reducing the severity of financial crises and enhancing financial and monetary stability. However, while the Commission published its proposal in November 2015, potential risks, such as moral hazard, or the risk of some banking systems subsidising others ('cross-subsidisation'), resulted in the debate stalling at EU level.[17] The scheme is one of the priorities of Commission President Ursula von der Leyen.

According to a first proposal, a single authority at EU level (such as the single resolution board) would manage the European deposit insurance scheme. The system should include country-specific risk in the calculation of insurance premiums. In addition, losses should be borne first by the relevant 'national compartment' of the European deposit insurance scheme, and common funds should only be used in large, systemic crises that overburden one or several national compartments.

Another proposal examines first whether a fully mutualised system would be sufficient to cover losses during a crisis. After concluding positively, the authors examine whether it would potentially lead to a situation in which some banking systems systematically contribute less than they would benefit from the European deposit insurance scheme under certain loss scenarios. They find that, while the risk of cross-subsidisation could exist in the case of a mixed system (national and European funds), if the risk-based contributions followed the principle that a national banking system would contribute more to the common fund if it were more risk-prone relative to other banking systems in the banking union, there would be no unjustified systematic cross-subsidisation across Member States.

A third proposal also starts by investigating whether in its current design, a future European deposit insurance scheme may result in cross-subsidisation. After concluding that it may, the authors propose three design features that could remedy this issue: i) to require banks to hold a substantial amount of equity and debt that can be bailed in, because this way deposits become essentially risk-free; ii) to compensate the European Stability Mechanism for the backstop it would provide to the system, by asking banks to pay premiums; and iii) to involve non-bank private investors in risk-sharing.

Credit ratings and pro-cyclicality

During the early 2000s, the inclusion in key EU acts or financial regulations of the requirement for ratings to be performed by credit-rating agencies has reduced firms' incentives to develop their own capacity for credit risk assessment and due diligence. As demonstrated during the financial crisis, this 'mechanistic' reliance on external ratings without appropriate internal assessments contributed to herding behaviour and abrupt sell-offs of securities after their downgrade ('cliff effects'), which amplified pro-cyclicality.

Reforms implemented after the crisis on both sides of the Atlantic have reduced reliance on external credit ratings.[18] Despite these efforts, in a 2015 report, the European Commission noted that key regulations for banks, insurers and asset management still relied on external ratings, mainly due to the lack of alternative methods.[19] 'Cliff effects' of the kind observed during the financial crisis have not yet materialised during the current pandemic,[20] thanks to the quick measures taken by supervisors and central banks: i) banks have temporarily been allowed to operate below the level of capital defined by the Pillar 2 Guidance, the combined buffer requirement and the liquidity coverage ratio, without negatively judging those that make use of these relief measures; ii) banks and insurers have been called upon to delay their distribution of dividends and variable remunerations; and iii) the ECB has announced changes to its collateral framework until September 2021, to alleviate the impact of rating downgrades on the availability of collateral. Nevertheless, the risk remains; therefore, seeking credible and efficient alternatives, as well as eliminating reliance on credit ratings in the remaining key pieces of EU legislation would enhance systemic financial stability.

Concentration charges - Sovereign contingent debt instruments

Historically, sovereigns have been considered risk-free instruments because they have been backed by central banks. The regulatory treatment of such exposures has remained largely unchanged because sovereign debt plays a role in the implementation of monetary policy, contributes to the smooth functioning of financial markets, and can be a stabilising force in periods of economic stress.

Concentration charges target a particular aspect of the sovereign-bank nexus, namely the fact that the sovereign exposures of many euro-area banks are highly concentrated in the home country, instead of being diversified within the EU. A proposal suggests adopting a regulation applicable to all banks in euro-area countries that hold a concentration of euro-area sovereign exposures. This regulation would modify the calculation of the risk-based capital ratio for those banks, according to the sovereign exposures they hold.

Another proposal has a similar objective but follows a different approach: instead of penalising home bias, it suggests using regulatory incentives in order to encourage cross-border diversification. It therefore proposes to use a parameter embedded in the Internal Ratings-Based Approach (IRBA) of the Basel framework to allow banks with more diversified cross-border loan portfolios to have lower capital requirements.

The final proposal is on sovereign contingent debt instruments, defined as instruments that bear contractual debt service obligations tied to a pre-defined state variable. They are designed to alleviate pressure on a country's sovereign indebtedness and/or financing needs. Such instruments belong to two main categories: i) GDP-linked bonds, which have returns indexed to the real growth rate of GDP. (These are equity-like instruments, comparable to shares in a corporation, with dividends paid as a share of national income rather than of corporate profits); and ii) (sovereign) contingent convertible debt, which converts into a bond of extended maturity and can also stop coupon payments when a trigger breaches a threshold. Apart from weakening the bank–sovereign nexus, the two instruments can reduce liquidity and insolvency risk, diversify the funding base of investors, increase the transparency of risk-pricing and contribute to a speedy response to crises.

Monetary policy

In its recent ruling on the ECB's public-sector purchase programme, Germany's Federal Constitutional Court (GFCC) concluded that the ECB had failed to properly assess and explain the 'proportionality' of its policies.[21] It has been argued that the ruling: i) risks undermining the EU legal order and calls into question the authority of EU law at a time when a general trend of disregard can be witnessed;[22] ii) might be abused by the governments and courts of other Member States, which might cite it as a precedent justifying their own non-compliance with ECJ judgments; and iii) risks undermining the ECB's independence (and thus the constitutional foundation of monetary policy)[23] and having significant implications for two of the ECB's active programmes, the PSPP and the PEPP, given that the latter is extensively based on the former.

It has been noted that the GFCC's complaint that existing monetary policies impose costs on specific groups implies that the GFCC does not think price stability should be the ECB's primary objective[24] - in effect, that the ECB should pursue a different mandate. Until now and in contrast with central banks such as the US Federal Reserve, the ECB has had a single mandate of price stability, and not a dual one (such as, for instance, also ensuring maximum employment). While broadening the ECB's mandate is generally viewed with suspicion in policy-making circles, this is not so unusual in the world of central banking and could be more successful in helping to avoid problems such as that with the GFCC. Moreover, the timing to consider the question of any potential change in mandate is perhaps appropriate, as 20 years after its creation, the ECB is now engaged in a review of its monetary policy strategy that will last until mid-2021.

List of potential initiatives

	Initiative	Likely lead EU actor	What should be done?	
1	Adopt a European deposit insurance scheme	European Parliament (EP) and Council	Create equal protection for all insured euro-area depositors.	
2	Create an EU asset management company for non-performing loans (NPLs)	Council	In case the economic situation puts many banks at risk, quickly shifting these assets off banks' balance-sheets would safeguard systemic stability	
3	Improve the functioning of corporate bond markets	EP and Council	Facilitate company issuance; increase access and options for investors; enhance transparency; improve the supervisory framework	
4	Create a macro-prudential framework for non-banks	ESRB	Develop a system-wide or macro-prudential perspective for the non-bank financial sector to ensure financial stability	
5	Grant the Single Resolution Board (SRB) more responsibilities	EP and Council	Give the SRB prerogatives similar to those of the US Federal Deposit Insurance Corporation and assign it responsibility to resolve all significant failing banks	
6	Establish a supervisory body in charge of money-laundering / terrorist-financing issues at EU level	Council	Better exchange of information between supervisors; help Member States to improve their knowledge and expertise in these fields; strengthen supervisory independence and help create a level playing-field	
7	Establish a common (consolidated) corporate tax base	EP and Council	Enhance the single market by establishing a common corporate tax base (CCTB) and common consolidated corporate tax base (CCCTB)	
8	Reduce the sovereign–bank nexus	EP and Council	Encourage banks and investors to diversify their holdings of euro-area bonds. Create financing tools (e.g. sovereign bond-backed securities)	
9	Harmonise EU business law to increase cross-border investment	Academic initiative and national parliaments	Possible steps include a European code of business law and regulation in new areas, (a 'euro-mortgage', European preservation orders, insurance contracts, European business loans)	
10	Reduce the sovereign exposure of banks in the EU	EP and Council	Sovereign concentration charges, or a euro-area basket	

11	Harmonise insolvency frameworks	EP and Council	Reforms could involve adopting an EU-wide regime for out-of-court procedures, strengthening the supervisory framework, providing for higher sanctions and providing for redress procedures
12	Separate retail banking and investment banking	EP and Council	Reduce banking risk by diminishing the implicit public guarantees on market transactions
13	Encourage creation of pan-European banks with more diversified balance sheets	Private sector / EP and Council	Take advantage of economies of scale
14	Sever the mechanistic reliance on and the pro-cyclicality of credit ratings	EP and Council	Remove credit ratings from the remaining important pieces of EU financial regulation, to avoid spirals in crises
15	Entrust an EU body with the supervision of accounting standards and auditing companies	EP and Council	Increase the comparability of data
16	Set up recovery and resilience facility and the technical support instrument	EP and Council	Support Member States' efforts to implement reforms necessary to achieve economic and social recovery, resilience and convergence.
17	Engage in 'soft' measures (e.g. EU representation in international economic fora	EP and Council	Strengthen the EU's handling of future crises and increase its international influence
18	Reform EU fiscal rules	EP and Council	Simplify the Stability and Growth Pact, based on specific elements, and strengthen its enforcement[25]
19	Increase EMU's democratic legitimacy and the accountability of its institutions	EP and Council / national parliaments	Strengthen the involvement of the EP and enhance coordination between the EP and national parliaments
20	Reform the European Stability Mechanism	Council	Provide the Single Resolution Fund with a backstop. Move toward single-leg collective action clauses.
21	Enhance independent fiscal councils (IFCs)	EP and Council	Reduce political incentives in the implementation and evaluation of compliance with the fiscal rules
22	Create a more credible framework to ensure sovereign debt sustainability	Council	Ensure that creditors participate in crisis resolution and protect the ESM from lending to insolvent Member States
23	A central fiscal stabilisation capacity for the euro area	EP and Council	This could take the form of a common unemployment insurance scheme. The SURE initiative is a first step.
24	Amend the mandate of the European Central Bank	Member States (Treaty change)	Widen the ECB's mandate (e.g. commitment to maximum employment and environmental sustainability) to cover adequately its responsibilities

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ENDNOTES

1 While most people associate the term 'single market' with the four freedoms, it is in fact a much bigger and multi-layered endeavour, including, among other recent initiatives, the digital single market, banking union and energy union. It is of central importance to the EU and is mutually supportive with EMU: on one hand, EMU supports a more effective single market and, on the other, completing the single market can strengthen economic resilience in EMU.

2 The report drew inspiration from the 2012 Commission communication on 'Blueprint for a deep and genuine EMU', which was followed by the December 2012 report on 'Towards a genuine economic and monetary union'.

3 The Franco-German proposal would be based on Article 122 of the Treaty, which explicitly enables help to Member States in exceptional circumstances and the use of the EU budget, in the form of the next MFF, to help hard-hit Member States through grants, rather than providing them only with loans. This would allow making additional expenditure of around €165 billion per year and would add up to €500 billion over three years.

4 The three pillars of spending through the recovery instrument are: i) 'support to Member States for investment and reforms to address the crisis' (with the bulk of the funds (€560 billion) being channelled through a new Recovery and Resilience Facility, which will offer financial support for investments and reforms); ii) 'kick-starting the EU economy by incentivising private investment' (through a new Strategic Investment Facility built into the InvestEU programme and a new Solvency Support Instrument); and iii) 'learning the lessons of the crisis' (by strengthening existing programmes and mechanisms in the areas of health, civil protection, external action and the green and digital transitions).

5 Reference has been made to an extension of the Emissions Trading System (ETS); a digital tax on companies with a global annual turnover of above €750 million; and a tax on large companies that draw huge benefits from the EU single market.

6 The ceiling is the maximum amount Member States may be called upon to provide to finance EU expenditure.

7 The previous crisis revealed strong disagreement between the 'frugal core' and the 'profligate periphery' of the euro area on how best to manage it. Ten years later, while important steps – with significant social costs – have been realised by Member States under economic programmes, the debate remains the same.

8 On 12 March, it announced that banks can use the capital and liquidity buffers they have accumulated in recent years to lend to consumers, businesses and other banks. Accordingly, this change amounts to €120 billion in new capital that can be used to absorb losses or finance up to €1.8 trillion of lending. Banks are expected to use their additional capital to support the economy and not to increase dividends or share buybacks at least until October 2020.

9 This provides banks with more flexibility on what loans to classify as non-performing and allows them to set aside less capital to cover losses from non-performing loans.

10 The ECB is offering weekly US dollar operations with one-week maturity and 84-day maturity at interest rates slightly above the overnight rate. European banks borrowed US$130 billion within days after the swap line was reopened.

11 PELTROs allow banks with loans not eligible for the TLTRO, such as mortgage loans and loans to public entities, and banks that have exhausted TLTRO limits, to continue to access cheap liquidity.

12 Under the operations, banks can now borrow for three years at an interest rate of -0.5 %. Furthermore, banks that lend above a certain threshold to businesses and consumers will pay an interest rate as low as -1 %. In other words, the ECB is paying banks to borrow money from the central bank in the hope that this will encourage them to lend money.

13 The ECB now accepts as collateral an expanded set of non-marketable assets – including government-guaranteed loans, lower quality loans and small business loans – that are outside the general framework. It has also granted waivers to Greek sovereign debt, which, because of its non-investment grade status, was not previously considered eligible collateral. 'Fallen angel' bonds (bonds that have recently lost their investment-grade rating), are now accepted as collateral as well. In addition, the ECB has reduced the amount of collateral required in excess of the loan amount for

its lending programmes.

14 The ECB said that it expects rates will remain 'at their present or lower levels until it has seen the inflation outlook robustly converge to a level sufficiently close to, but below, 2 % within its projection horizon, and such convergence has been consistently reflected in underlying inflation dynamics'.

15 On 12 March, it announced it would buy an additional €120 billion under the APP.

16 The programme was announced on 18 March, and is expected to last at least until the end of 2020. The assets to be bought under the PEPP are more or less the same as under the PSPP, i.e. the biggest part is used to purchase national and regional government bonds, (including for the first time Greek sovereign debt), supra-national debt, and various types of private-sector bonds. Unlike the APP, it will also buy commercial paper issued by non-financial corporations.

17 In October 2017, the Commission attempted to break the deadlock with a communication in which it took stock of what had been achieved with regard to creating the banking union and enumerated the measures still needed to complete it.

18 One major outcome of CRA III was the introduction of a requirement that financial institutions should carry out their own credit quality assessments and should not rely solely or mechanistically on credit ratings for assessment of the creditworthiness of an entity or financial instrument.

19 Internal measures and ratings are costly and difficult to set up for small institutions; market-implied ratings can be volatile and have a short-term nature; accountancy-based measures are limited to corporate debt.

20 In the case of large downgrades across the board, such as those that happened in 2007-2009, banks, insurers or asset managers may decide (or be forced) to sell securities of entities that lost their investment grade status as a result of a downgrade. Given that the share of securities they currently hold is significant, markets may not be able to absorb this.

21 The main points of the court's argument could be outlined as follows: i) The ECB is entrusted with monetary policy while economic policy is in the remit of Member States; ii) The PSPP has side effects that belong to the area of economic policy; iii) Therefore, the ECB should have explained why the pursuit of its monetary-policy mandate justified undertaking the PSPP despite these side-effects (proportionality assessment); iv) the European Court of Justice (ECJ) should also have carried out such an assessment when it commented on the PSPP's compatibility with the Treaty at an earlier stage of the procedure.

22 It has been noted that the ECJ has explained repeatedly since the *Costa* ruling, that if national courts could over-ride the decisions of the ECJ and each of them give their own interpretation of EU law, then EU law would not be applied equally or effectively across all Member States, and the entire legal basis of the EU would be called into question.

23 It has been argued that, on acceding to the GFCC's ruling, the Bundesbank would waive its independence, exposing itself to a judicialisation of monetary policy. However, if it disregards the GFCC's demand, it would incite a constitutional crisis.

24 Every monetary policy-related decision the ECB takes, has economic effects on firms, households and governments. It has been further argued that, not only does it have such effects, but it partly works through causing them.

25 The integration into the EU Treaties of the Treaty on Stability, Coordination and Governance (TSCG – Fiscal Compact) has in the meantime been voted down in Committee and Council has not discussed it further.

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