POLICY PAPER 137 15 JUNE 2015

NOTRE EUROPE
JACQUES DELORS INSTITUTE

IMPROVING EMU

OUR RECOMMENDATIONS FOR THE DEBATE ON THE FIVE PRESIDENTS REPORT

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SUMMARY

At the upcoming European Council of 25/26 June, Commission President Juncker will present a report on the future of EMU. As a preparatory step, an Analytical Note published in February 2015 raised eleven questions on how to enhance economic governance in the euro area.
Our Policy paper sets out some guiding principles on the issue. We derive our approach from the principle that we need as much additional integration as necessary for the effective functioning of EMU, but as little as possible.

1. Compliance: conditionality, incentives, and moral hazard
The implementation and enforcement of the EMU governance framework needs to rely on an adequate balance between sanctions and incentives. Both need to be strengthened, but emphasis should lie on the incentives. Furthermore, social imbalances need to be taken into account when assessing convergence and imbalances.

2. Structural reforms and real convergence
Structural reforms could be encouraged by allowing member states that meet certain convergence requirements to participate in strengthened EMU risk-sharing mechanisms. The aims of reform should not only be limited to improving cost competitiveness, but target broader measures to improve non-cost competitiveness through financial support and technical assistance.

3. Financial markets: bank-sovereign nexus and shock absorption
The impact of future crises could be further mitigated by introducing a European deposit insurance, which would limit capital flight from countries under pressure, and adding a fiscal backstop to the Single Resolution Fund (SRF) in order to enhance its credibility.

4. Missing governance instruments
The ESM should be replaced by a European Monetary Fund that would feature a streamlined voting system and would provide emergency liquidity on the basis of predefined conditions. Furthermore, in order to prevent the renewed build-up of imbalances, temporary stabilizing payments may be needed to synchronise euro area members' business cycles.

5. Accountability and legitimacy
Improvements to EMU's accountability and legitimacy are needed. At the executive level, these include holding regular euro area summit meetings, creating a permanent president of the Eurogroup, and replacing the Troika by a "European team" under direct democratic control. At the parliamentary level, we need a "euro area subcommittee" in the European Parliament and greater involvement of national parliament members in EMU governance.

EMU needs to be developed further and the Five Presidents Report has the potential to play a key role in setting the reform agenda. Since there may be several alternative paths to a strengthened monetary union, the message of the Five Presidents Report should lay the foundations for discussing them in a systematic manner. We need a serious debate on EMU's long-term perspective.

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INTRODUCTION

What should be the next steps towards better economic governance in the euro area? The Analytical Note[1] – prepared by the President of the European Commission in cooperation with the presidents of the European Parliament, the European Council, the Eurogroup and the ECB – suggests a few answers and many questions. The note identifies growth-enhancing structural reforms and a deepening of the Single Market as short-term priorities. It is intended to start a discussion process on the future of EMU that will feed into a Five Presidents Report on this issue, to be expected in June. In order to structure discussions, the note formulates eleven questions. They touch upon five main topics: compliance, structural reforms, the role of financial markets, missing governance instruments and questions of political legitimacy.

> "THIS POLICY PAPER SETS OUT OUR PERSPECTIVE ON THE ISSUES RAISED IN THE ANALYTICAL NOTE"

This Policy paper sets out our perspective on these issues. It summarizes a set of proposals drawn from the work of the Jacques Delors Institutes of Berlin and Paris on the future of EMU[2]. The guiding principle in answering the questions is not to push blindly for further European integration, but rather – taking into account the constraints of a difficult political context – to present proposals where they are most urgently needed. We derive our approach from the principle that we need "as much additional integration as necessary for the effective functioning of EMU, but as little as possible."[3]

1. Compliance: conditionality, incentives, and moral hazard

RELEVANT QUESTIONS FROM THE ANALYTICAL NOTE

- How can we ensure sound fiscal and economic positions in all euro area members?
- How could a better implementation and enforcement of the economic and fiscal governance framework be ensured?
- What instruments are needed in situations in which national policies continue – despite surveillance under the governance framework – to go harmfully astray?

Various 'Juncker questions' relate to the general question of how to ensure compliance with existing EU rules and procedures. In our view, a pre-condition for good implementation is to make sure that rules are well-designed and that they are seen as legitimate by those subjected to them. In this respect, there is still some room for improvement. Concerning the Stability and Growth Pact, we see the new guidelines presented by the Juncker Commission[4] as a step in the right direction. The clarified rules may aid the economic recovery in euro area member states by supporting the domestic reform process. We welcome in particular the fact that deadline extensions for deficit correction will be based more explicitly on reform progress[5] and temporary deviations from the medium-term budgetary objectives will be acceptable in some cases, if they are justified

1. Jean-Claude Juncker, Donald Tusk, Jeroen Dijsselbloem and Mario Draghi, *Preparing for next steps on better economic governance in the euro area. Analytical Note*, February 2015.
2. Particularly from Enderlein et al (2012), Fernandes and Rubio (2012), Enderlein, Guttenberg and Spiess (2013), Fernandes and Maslauskaite (2013), Bertoncini (2013), Fernandes (2014), Bertoncini and Vitorino (2014), Rubio (2014), Enderlein, Vannahme and Haas (2014).
3. See Henrik Enderlein, Peter Bofinger, Laurence Boone, Paul de Grauwe, Jean-Claude Piris, Jean Pisani-Ferry, Maria João Rodrigues, André Sapir and António Vitorino, "Completing the euro. A road map towards fiscal union in Europe" (Report of the "Tommaso Padoa-Schioppa Group"), *Studies & Reports No. 92*, Notre Europe – Jacques Delors Institute, June 2012.
4. See COM (2015) 12 final.
5. As proposed in Eulalia Rubio, "Promoting structural reforms in the euro area: what for and how?", *Policy paper No. 119*, Notre Europe – Jacques Delors Institute, October 2014.

by necessary public investment. The latter aspect may encourage countries to spend less on consumption and more on their future growth. Further improvements could include extending the 'investment clause' to countries under the corrective arm since the same rationale applies to them. Furthermore, the Pact's legitimacy would be strengthened considerably by tackling the 'politicized' implementation of flexibility clauses, i.e. the tendency to treat big countries with greater leniency than small ones.

Further changes are also needed in the surveillance of macro-economic imbalances. Social imbalances need to be taken into account in the application of the macro-economic imbalance procedure (MIP). Otherwise, efforts to repair one aspect of the monetary union may damage another[6].

"EFFECTIVE CONDITIONALITY REQUIRES AN ADEQUATE BALANCE BETWEEN SANCTIONS AND INCENTIVES"

Moreover effective implementation requires an adequate balance between sanctions and incentives. The current EMU governance is mostly based on the threat of sanctions. This is not necessarily the most effective way, as sanctions are often seen as non-credible, and it reinforces the perception of actions dictated by Brussels, thus hardening domestic resistance. There is a need to introduce positive incentives, particularly for implementing structural reforms. Financial incentives might be an option. Another promising approach is to directly couple progress in the implementation of structural reforms to participation in an enhanced institutional framework at the European level (as proposed in Enderlein et al 2014)[7]. We discuss both options in more detail in the following sections.

Finally, one of the main reasons why it is so difficult to deal with non-compliance in the EMU is the fact that the major, ultimate sanction – an exit from EMU – is seen as non-credible. A way of solving that could be considering in the future feasible options for an orderly exit from EMU, although any such step would need to be regarded as a last resort after a long and transparent process (thus avoiding "surprise exits")[8]. Furthermore, and in contrast to the majority of our proposals, the introduction of an exit option would necessarily require a treaty change. Imposing increased market discipline on non-compliant member states would constitute a more moderate option. This could be achieved by permitting sovereign defaults in exceptional cases[9]. However, such a threat is credible only if the banking union and assistance schemes for compliant countries are further reinforced so that one default cannot trigger a financial meltdown in the entire euro area.

2. Structural reforms and real convergence

RELEVANT QUESTION FROM THE ANALYTICAL NOTE

- Under what conditions and in which form could a stronger common governance over structural reforms be envisaged? How could it foster real convergence?

Any discussion on ways to promote structural reforms in EMU should start by clarifying what type of reforms should be promoted and for what reason[10]. Many structural reforms improve the competitiveness and growth of national economies, and have positive spillover effects on the whole EMU. These reforms should be promoted through soft coordination but there is no need for stronger governance mechanisms on the European level, as they are not essential for the EMU to work properly.

6. Sofia Fernandes and Kristina Maslauskaite, "A social dimension for the EMU: why and how?", *Policy paper No. 98*, Notre Europe – Jacques Delors Institute, September 2013.
7. See Henrik Enderlein, Joachim Fritz-Vannahme and Jörg Haas, "Repair and prepare: strengthening Europe's economies after the crisis", *Study*, Jacques Delors Institut – Berlin and Bertelsmann Stiftung, January 2015; Enderlein Henrik and Jean Pisani-Ferry, *Reforms, investment and growth: an agenda for France, Germany and Europe*, Report to Sigmar Gabriel, Feder Minister for Economic Affairs and Energy and Emmanuel Macron, Minister for the Economy, Industry and Digital Affairs, 2014; Rubio (2014), *op. cit.*
8. Enderlein et al (2014), *op. cit.*
9. Enderlein et al (2012), *op. cit.*
10. Enderlein et al (2014), *op. cit.*; Rubio (2014), *op. cit.*

There are two cases in which a stronger EU involvement might be desirable. First, certain reforms are crucial in order to guarantee EMU's long-term viability. As the analytical note points out, current account imbalances between EMU member states were among the main causes of the crisis. If we want to avoid the re-emergence of large and persistent imbalances, we need to ensure that euro area economies are able to flexibly adjust to shocks through export and import prices *(see also section 4)*. More adjustment capacity also enhances the synchronization of business cycles, mitigating the "one size fits none" problem in monetary policy. Structural reforms can help by improving price and wage elasticity, but there is no easy way of ensuring that EMU countries pursue such reforms. Merely tweaking the economic and fiscal governance frameworks as outlined in section 1 is unlikely to be sufficient by itself and financial incentives risk being ineffective when dealing with countries in a strong budgetary position.

A promising approach to promote these reforms would be creating a direct link between the implementation of structural reforms on the country-level and the establishment of new EMU institutions[11]. This could be done by establishing minimum requirements (e.g., concerning market flexibility and openness to competition) for member states' participation in future EMU risk-sharing institutions *(as outlined in section 4)*. The prospect of joining these institutions can work as a powerful incentive for both economically weak members (that, at least in the short-term, are more likely to benefit from the risk-sharing mechanism) and economically strong member states (who could enjoy the benefits of the common currency without having to worry about renewed imbalances and bailouts).

TABLE 1 ► Incentives of joining new EMU risk-sharing institutions

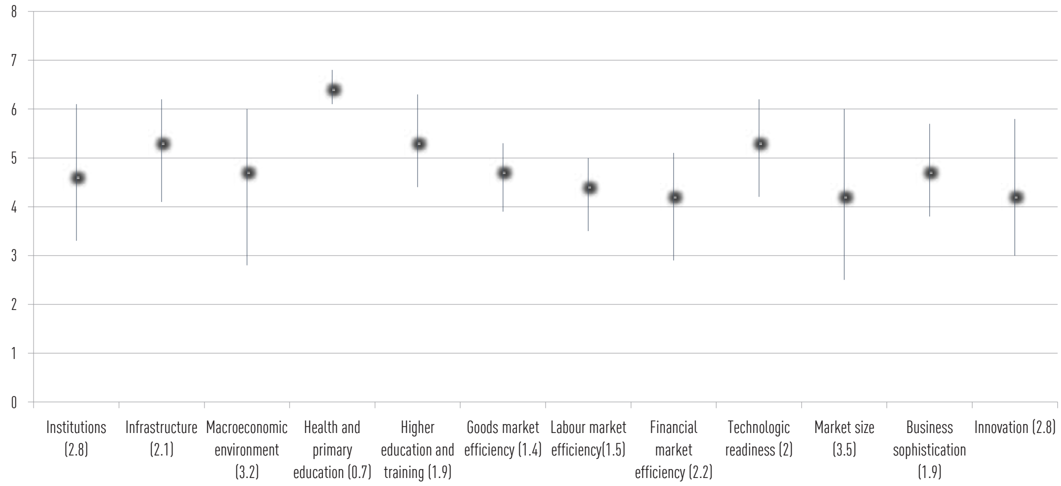
	ELEMENT	ADVANTAGES FOR COUNTRIES IN A STRONG ECONOMIC POSITION	ADVANTAGES FOR COUNTRIES UNDER PRESSURE
New instruments (available to reformed countries)	• Cyclical stabilisation mechanism	• EMU works as intended • No net transfers over the medium term • Will receive payments during cyclical downturns	• Payments support reform efforts • Prevents divergences in inflation rates and competitiveness
	• ESM+/European Monetary Fund with streamlined voting system and clear rules ("sovereignty ends where liquidity ends")	• Provides stability but deters excessive deficits • No hostage situation	• Makes self-fulfilling crises less likely • Conditions for emergency lending are known ex ante • Less uncertainty on the markets
	• Complete banking union, including deposit-insurance scheme and credible backstop	• Lower costs due to market failures and "too big to fail" situations	• Panic and capital outflows become less likely

Source: Based Enderlein Henrik, Joachim Fritz-Vannahme and Jörg Haas, "Repair and prepare: strengthening Europe's economies after the crisis", *Study*, Jacques Delors Institut – Berlin and Bertelsmann Stiftung, January 2015

Second, to the extent that large structural divergences threaten the stability of the euro area, there is a case for EU action aimed at reducing the current intra-euro area competitiveness gap. Over the last years the emphasis has been on eliminating wage and price rigidities, but in fact the current intra-euro area competitiveness gap is largely explained by differences in non-cost competitiveness factors such as capacity to innovate, institutions, technological readiness or financial market efficiency *(see Graph 1)*.

11. Henrik Enderlein, Lucas Guttenberg and Jann Spiess, "Blueprint for a cyclical shock insurance in the euro area", *Studies & Reports No. 100*, Notre Europe – Jacques Delors Institute, September 2013; Rubio (2014); Enderlein et al (2014).

GRAPH 1 ► Intra-euro differences in competitiveness factors (12 pillars composing the Global Competitiveness Index)



Source: Global Competitiveness Index 2013-2014.

While we acknowledge that fully removing these structural differences is difficult if not impossible, we think that two complementary avenues of action need to be explored. The first is the establishment of a temporary financial assistance mechanism to support a process of real convergence within the EMU (a sort of 'super cohesion' fund, as proposed by Jacques Delors in a speech made in June 2013)[12]. The objective of this mechanism would be to provide targeted financial support and technical advice to euro area countries undertaking major reforms to improve the productivity basis of their economy in the long run[13]. The second avenue of action is to improve the use and allocation of structural and cohesion funds in euro area countries, and particularly the capacity of structural funds to promote reforms[14].

3. Financial markets: bank-sovereign nexus and shock absorption

RELEVANT QUESTIONS FROM THE ANALYTICAL NOTE

- Has the fiscal-financial nexus been sufficiently dealt with in order to prevent the repetition of negative feedback loops between banks and sovereign debt?
- How could private risk-sharing through financial markets in the euro area be enhanced to ensure a better absorption of asymmetric shocks?

The creation of a banking union has undoubtedly marked a milestone in efforts to limit the risk of a 'diabolical loop' between failing banks and highly indebted sovereigns. However, the banking union is not yet complete. The Single Resolution Fund (SRF) is small compared to banks' balance sheets and the use of European Stability Mechanism (ESM) resources is subject to numerous constraints. Besides, the recent bank deposit outflows from Greece have put into evidence that, in the absence of a common euro area deposit insurance, banks are still very vulnerable to doubts about their country's solvency. The impact of future crises could be further mitigated by introducing a European deposit insurance, which would limit capital flight from countries under pressure, and adding a fiscal backstop to the Single Resolution Fund (SRF) in order to enhance its credibility[15].

12. Jacques Delors, "Rethinking the EMU and making greater Europe positive again", *Tribune*, Notre Europe – Jacques Delors Institute, June 2013.
13. Eulalia Rubio, "Which financial instrument to facilitate structural reforms in the euro area?", *Policy Paper No. 104*, Notre Europe – Jacques Delors Institute, December 2013.
14. Sofia Fernandes and Eulalia Rubio, "Solidarity within the eurozone: how much, what for, for how long?", *Policy Paper No. 51*, Notre Europe, February 2012.
15. Enderlein et al (2012), *op. cit.*

Financial markets can contribute to the absorption of asymmetric shocks and help reverse the current regional fragmentation in the euro area financial system. The establishment of a banking union can help by progressively normalizing credit conditions in crisis-hit economies, but this will take time and in any case it will not be enough to ensure a well-integrated euro area financial market.

The establishment of a Capital Market Union might in principle provide the basis for more integration in equity and bonds market, thus improving private risk-sharing. However, this is a long-term project, and we do not know whether it will suffice to induce cross-border equity flows within the euro area. Even if capital markets are completely integrated within a currency union, private insurance against asymmetric shocks is likely to remain suboptimal. It will need to be supported by additional governance instruments.

4. Missing governance instruments

RELEVANT QUESTIONS FROM THE ANALYTICAL NOTE

- Is the current governance framework – if fully implemented – sufficient to make the euro area shock-resilient and prosperous in the long run?
- To what extent can the framework of EMU mainly rely on strong rules and to what extent are strong common institutions also required?
- To what extent is the present sharing of sovereignty adequate to meet the economic, financial and fiscal framework requirements of the common currency?
- Is a further risk-sharing in the fiscal realm desirable? What would be the preconditions?

While Europe has had some success in achieving stability through "exploratory governance"[16], the current EMU framework, even if fully implemented, will not suffice to make the euro area shock-resilient and prosperous in the long run. It is focused primarily on combatting symptoms, not the root causes of the crisis. Imbalances are still likely to emerge, adjustment remains slow and a unified crisis response is far from guaranteed.

Improving common rules and "top down" procedures of co-ordination, is necessary, but not sufficient, to ensure a well-functioning EMU. As Tommaso Padoa-Schioppa liked to remind us, a real EMU can only work adequately if the Union is an actor rather than a mere coordinator (not only in the monetary realm but also in the economic and budgetary realm). The euro area should have a capacity for joint action. This requires the establishment of strong common institutions, able to take quick decisions and shielded from national political pressure. The EMU architecture needs to be completed with at least two additional elements[17].

> "WE NEED ADJUSTMENT MECHANISMS THAT WOULD PREVENT LARGE IMBALANCES BETWEEN EURO-AREA MEMBER STATES FROM ARISING"

First, we need efficient adjustment mechanisms that would prevent large imbalances between euro-area members from arising. The analytical note describes how such imbalances have contributed to the crisis. The underlying dynamics can be addressed in part by strengthening the real-exchange-rate channel (through measures such as the full implementation of EU single market legislation, the setting of common euro area standards in areas such as the labour market, taxation or pension rights, or actions to promote intra-euro area labour mobility). However, these measures will take effect only slowly and complete convergence is neither realistic nor desirable. Temporary transfer payments may therefore be needed to synchronise euro area members' business cycles, thus mitigating the build-up of imbalances[18]. This should not be confused with permanent transfer mechanisms which are geared towards income convergence. A cyclical mechanism based on output-gap deviations could result in net transfer payments close to zero in the medium term and could contribute to ensuring that the ECB's monetary pol-

16. Hertie School of Governance (ed.), *The Governance Report 2015*. Oxford: Oxford University Press, 2015.
17. Enderlein et al (2012), *op. cit.*
18. Enderlein et al (2012), *op. cit.*; Enderlein et al (2014), *op. cit.*

icy does not amplify inflation differentials between member states as it did in the 2000s[19]. A Europe-wide unemployment insurance programme might have a similar effect.

> "WE NEED A MORE EFFECTIVE CRISIS PREVENTION AND RESOLUTION MECHANISM. (...) THIS COULD BE ACHIEVED THROUGH (...) A EUROPEAN MONETARY FUND"

Second, we need a clearer, more effective crisis prevention and resolution mechanism, able to reduce uncertainty and contagion by encouraging fiscal responsibility while ensuring the credibility of assistance schemes. This could be achieved through the creation of a European Monetary Fund (EMF) which would protect euro area countries against self-fulfilling solvency crises[20]. The EMF would replace the current European Stability Mechanism (ESM) which has two main weaknesses: it is not based on the principle of joint and several liability, which reduces its credibility, and it requires unanimity for decisions to provide stability support, which constrains its ability to reactly quickly and decisively. The EMF would have a streamlined voting system and would provide emergency liquidity on the basis of predefined conditions. It would make assistance above a certain threshold subject to increasingly intrusive external budgetary surveillance (following the principle of "sovereignty ends when liquidity ends"). This condition would limit the risk of moral hazard. The EMF could also provide the backstop for the banking union's Single Resolution Mechanism.

The creation of these new institutions implies a further risk-sharing in the fiscal realm. The EMU needs some pooling of budgetary resources and/or an autonomous power to raise resources to provide a credible assistance scheme in case of self-fulfilling crises, insure countries against country-specific shocks and provide a credible backstop to the bank resolution scheme.

These enhanced risk-sharing institutions are in turn only viable when accompanied by increased sovereignty-sharing. The present level of sovereignty-sharing is not adequate to meet the economic, financial and fiscal framework requirements of the common currency because it is not clear to what extent sovereignty is de facto being shared at the moment. Indeed, despite the treaty provisions stipulating that economic policy is a "matter of common concern" (Art. 121 TFEU), several member states seem to continue to look at EMU as a grouping of economically independent sovereigns that subscribe to a framework of rules, but within this framework act severally, not jointly.

5. Accountability and legitimacy

RELEVANT QUESTION FROM THE ANALYTICAL NOTE

- How can accountability and legitimacy be best achieved in a multilevel setup such as EMU?

Without doubt, an institutionally reinforced EMU as proposed above requires, to an even greater extent than EMU in its current form, enhanced accountability and legitimacy. Several complementary improvements are needed, both at the executive and parliamentary levels. We can start by pointing out three sets of political and institutional adjustments[21].

First, there should be regular euro area summit meetings (at least twice a year, as it is foreseen in the rules of March 2012). These summits, gathering together the Heads of State and Government of the euro area and the "euro area summits" president, should exercise leadership over the key euro area issues, by requesting

19. See Enderlein et al (2013) for a detailed proposal of a cyclical shock insurance mechanism.
20. Enderlein et al (2014), *op. cit.*
21. See Yves Bertoncini and António Vitorino, "Reforming Europe's governance. For a more legitimate and effective federation of nation states", *Studies & Reports No. 105*, Notre Europe – Jacques Delors Institute, September 2014.

expertise and recommendations from the Council, the Commission and the ECB. With this in mind, and as suggested by the French and German authorities, it would be extremely useful for the euro area summits to rely on the Eurogroup, but also on the Council of Employment and Social Affairs ministers and any other type of Council that is likely to provide a vision that is not limited to economic and financial issues alone.

Second, the euro area countries should appoint a permanent president of the Eurogroup. The public good that the euro represents should actually be supported and embodied continuously rather than sporadically. This office, possibly created by merging the duties of the Eurogroup president with those of the commissioner of Economic and Monetary affairs, would ensure the follow-up of decisions taken within the EMU framework and would be accountable to member states and parliament members.

Finally, the experience of the "Troika" was particularly disastrous in terms of legitimacy and accountability. In the future, the supervision of the implementation of adjustment programmes in the context of a European financial assistance plan should be ensured by a "European team" made up of the European Commission, the Eurogroup and the ECB (for the banking part) and, once the EMF is in place, by representatives of this new institution. The European team would function best if there was a clear division of responsibilities between the Eurogroup and the Commission, under the direct supervision of the European council and European Parliament (EP).

In addition, three complementary improvements are needed at the parliamentary level to have a more accountable and legitimate EMU.

"A 'EURO AREA SUBCOMMITTEE' SHOULD BE ESTABLISHED WITHIN THE EUROPEAN PARLIAMENT"

First, the European Parliament needs to play a stronger role in this new governance. To this purpose, a "euro area subcommittee" should be established within the EP, through a modification of EP's rules of procedure. Such subcommittees already exist in fields where the EU does not have as much powers as for euro area governance, such as human rights or defence: it is therefore logical that a subcommittee of the same type could be established, for both functional and political reasons (the euro is a public good that is sufficiently valuable to merit a specific parliamentary group). This subcommittee should not be reserved to parliament members elected within the euro area countries alone, but should be open to all parliament members wishing to join it, in the limit of 60 members, for legal (articles 10.2 and 14.4 of the TEU), political (not to re-establish boarders within the EP) as well as philosophical reasons (all the EU countries are concerned by the EMU).

Second, a greater involvement of national parliament members in EMU governance should be organised on the basis of Article 13 of the "TSCG", which provides for the establishment of a "conference of representatives of the relevant committees" of the national parliaments and of the EP in order to discuss economic and fiscal issues. The organisation of such a conference is useful on two counts: it allows greater involvement of national parliament members at EMU level, given their role in adopting euro area bailout plans and in decisions relative to national fiscal and economic choices; it brings together representatives from all the specialised committees linked to EMU governance, in particular the Economic and Financial Affairs Committee, and not only the European Affairs Committee. In short, this conference is to play the role devoted to the "COSAC", but in the sphere of the EMU, and should be both a forum for discussion and an influential stakeholder. This objective will naturally be easier to achieve if the conference has the necessary resources and publicity to strengthen and maintain the motivation of the national parliament members concerned. In this perspective, the agreement reached by the parliaments at the occasion of their 2013 and 2014 meetings has shown the need for a much stronger organisation: If this conference adopts genuine "rules of procedure", mentioning the number of its members and the nature of its activities, it will be able to play a useful role on the basis of a functional distribution of tasks between the parliaments.

Last but not least, national parliaments should play a more effective role in controlling and supervising national governments' decisions and actions on EMU issues. In those member states where parliaments do not play a sufficiently strong role, institutional and legal adjustments should be introduced in order to strengthen the democratic aspect of EMU's governance. In particular, compulsory debates on euro issues should be held by national parliaments (such as the assessment of country specific recommendations once adopted by the Council), including on the basis of treaty amendments if needed.

TABLE 1 ► Completing the institutional architecture for the euro area

THE "GOVERNANCE" OF THE EURO AREA	
Presidency level	**Regular** euro area summits with permanent president and with input from the president of the Commission
Ministerial level	Eurogroup **with full time president** and with input from the Commission
THE EURO AREA'S PARLIAMENTARY DIMENSION	
European Parliament	**Sub-committee for the euro area** (open to all MEPs, maximum 60 members)
National parliaments – European level	**Interparliamentary conference for the EMU** (open to representatives of the 25 national parliaments having ratified the TSCG, in the limit of 150). Participation of up to 30 MEPs
National parliaments – National level	**Strengthening *ex-ante* and *ex-post* control** over their government when deliberating and voting on euro area issues
STRONGER SERVICES FOR THE EURO AREA	
Bail out	ESM, then **expanded EFSM / Commission, Eurogroup, ECB "European team"** (instead of Troika)
Budget supervision	Commission – Eurogroup Secretariat – **European Treasury**
Economic coordination	Economic and Financial Committee – Eurogroup working group

NB: already put in place, **yet to be implemented**

Source: Yves Bertoncini and António Vitorino, "Reforming Europe's governance. For a more legitimate and effective federation of nation states", *Studies & Reports No. 105*, Notre Europe – Jacques Delors Institute, September 2014.

CONCLUSION

Even after six years of crisis, EMU is lacking crucial elements. It is therefore welcome that the Five Presidents process undertakes a renewed effort to identify what steps towards better economic governance in the euro area could look like. The Five Presidents Report has the potential to play a key role in setting the reform agenda. In order to do so, it should clearly spell out which building blocks are needed to ensure the functioning of the monetary union and what exactly is yet unknown.

This document has argued that a strengthened EMU should contain the following elements:

- Common rules that take into account the broader goals of the monetary union and provide an adequate balance between sanctions and incentives.
- Real convergence among EMU countries through structural reforms. Countries undertaking major reforms to improve their competitiveness in the long term should receive support from a temporary financial assistance mechanism.
- A complete banking union that includes a fiscal backstop and a European deposit insurance.
- Stronger institutions in the area of economic governance, namely a European Monetary Fund to effectively protect countries against self-fulfilling insolvency and a shock insurance mechanism to synchronise EMU member states' business cycles.
- A more explicit institutional structure for the euro area that increases the accountability and legitimacy of the new governance instruments on the parliamentary and executive level.

Together, these elements can constitute a framework for reform if European countries start viewing the process as a positive-sum game. All European economies can profit from preventing the build-up of imbalances through structural reforms and improving governance capacity. All countries would profit from a clearly defined approach to risk-sharing as opposed to the ad hoc negotiations we are seeing today with their huge cost in terms of economic uncertainty and increasing tensions between EU member states. The key issues are credible commitment and timing.

"WE NEED A SERIOUS DEBATE ON EMU'S LONG-TERM PERSPECTIVE"

One solution would be a staged process that assures the participants that they will enjoy the protection of the governance instruments discussed above if – and only if – they achieve a level of convergence and adjustment capacity that is in line with the requirements of a stable monetary union. The message should be that a package deal will offer genuine advantages, but can only work for countries willing to engage in reform[22].

Lastly, we should not forget that there may be several alternative paths towards a strengthened monetary union. The most important contribution the Five Presidents Report can make is to lay the foundations for discussing the options in a systematic manner. We need a serious debate on EMU's long-term perspective.

22. Enderlein et al (2014), *op. cit.*

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ISSN 2256-9944

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