SPEECH

The euro at 25: what next for Economic and Monetary Union?

Introductory remarks by Piero Cipollone, Member of the Executive Board of the ECB, at the European Parliamentary Week 2024

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Thank you for the opportunity to discuss the future of our Economic and Monetary Union (EMU).[1] The introduction of the euro in 1999 was a milestone for European integration. And this year marks its 25th anniversary. Used by millions of people every day, it has become the most tangible symbol of European integration in our daily lives.

The euro was a democratic choice, and it has seen continued popular support and political commitment. This has proved essential during the economic crises that we have faced. And it remains essential in the unstable world we are living in today. Support for the euro and EMU is in fact at a historical high, with 79% of euro area citizens in favour.[2] And young Europeans have known only the euro as their currency.

So it is fitting that we are discussing the future of EMU during the European Parliamentary Week. The euro, just like the European Union, is only as strong as our commitment to it. And all of you, whether national or European parliamentarians, are essential to this enduring commitment. The euro is our money. It makes us stronger together, and together we make it stronger.

The euro could not have been established were it not for the vision of Jacques Delors, whose passing in December saddened us deeply. Jacques Delors was widely seen as the founding father of EMU. So when thinking about its future, we should reflect on whether we are living up to the spirit that drove him. He believed that the European economic model should rest on three principles: “La concurrence qui stimule, la coopération qui renforce et la solidarité qui unit” (competition that stimulates, cooperation that strengthens, and solidarity that unites).[3]

Today I will examine the state of our EMU through the lens of these three principles, highlighting how they help us identify common priorities for the future.

Competition that stimulates

Let me start with competition – both within Europe and globally.

EMU and the Single Market

One of the fundamental reasons for introducing the euro was to strengthen the Single Market. By removing currency exchange costs and risks, the euro has enabled people and businesses to take greater advantage of the Single Market and its four freedoms.[4] In surveys, four out of five euro area respondents say that the euro simplifies doing business and shopping in different countries, and that it makes it easier to compare prices across borders.[5] In other words, the single currency benefits consumers by broadening their choice and lowering prices.[6] And it allows firms to benefit from economies of scale – which incentivise innovation – and from lower costs of intermediate inputs.

However, despite the euro's success, the Single Market remains incomplete. This reduces both our resilience to shocks and our ability to reap the full benefits of the single currency. I will focus on two areas: labour mobility and financial integration. Both areas have untapped potential to spread risks more evenly[7], enhance our ability to absorb asymmetric shocks, and bring us closer to an optimum currency area.[8]

Higher labour mobility would increase the resilience of our labour markets[9] and strengthen our growth potential by facilitating labour matching across the euro area. It would broaden the pool of workers available to firms and the pool of vacancies available to workers. We can support labour mobility by simplifying the recognition of skills and qualifications, including for regulated professions. And teleworking has the potential to facilitate cross-border digital work if we address the labour and taxation law issues that it raises.[10]

Further deepening financial integration would also enhance risk sharing. In the United States, capital markets smooth out around 30-35% of state-specific shocks, compared with 10-15% across euro area countries.[11] This notably reflects that European equity markets are less developed and integrated, and that there is a lower propensity to invest across Member States. While cross-border integration and competition has been supported by the progress made so far on the banking union and capital markets union, as well as the creation of the Single Euro Payments Area (SEPA), we still lack a unified banking, capital and payments market. We need to redouble our efforts if we are serious about bolstering Europe's capacity to invest and innovate.[12]

For instance, very few bank loans are extended across borders and there are still significant obstacles to cross-border mergers. So we need to give renewed impetus to completing the banking union, including by making progress towards a European deposit insurance scheme that would ensure a level playing field among European banks and limit the bank-sovereign nexus.[13]

Similarly, European digital payment solutions remain largely fragmented along national lines. This would be unthinkable in the United States. Imagine not being able to use a payment card issued in New York to buy something in San Francisco, or having to use a card issued by a foreign company to pay in both cities. A digital euro would remedy this fragmentation. It would provide a European digital means of payment that is available to everyone, can be used everywhere in the euro area, and is free for basic use, just as cash is for physical payments. It would also provide a platform for European payment service providers to offer their services throughout the euro area, fostering competition and innovation.[14]

EMU's external competitiveness

The importance of “competition that stimulates” becomes even clearer when we look beyond our borders. The euro area is confronted with multiple challenges to its global competitiveness.

As a large open economy, we are particularly exposed to risks of global trade fragmentation. The pandemic and the energy crisis have starkly highlighted the vulnerabilities of supply chain disruptions and a dependence on energy commodity imports, which led to cost spikes that directly affected the competitiveness of European firms. And supply chain risks are forcing firms to adapt their decisions about where they produce their goods and from where they source their inputs.[15]

All of this means that we need to act on several fronts at the same time.

First, we need to rebalance the euro area’s economic model by shifting from an over-reliance on foreign demand to a stronger emphasis on domestic demand, supported by robust investment. Weak domestic demand has become a factor that firms are citing in their decision to relocate out of the EU.[16] And because savings have consistently exceeded investment in the euro area, we have been exporting our net savings to the rest of the world. We should instead be using these savings to invest more at home. If we do not sufficiently reinvest our savings in our domestic supply chains and infrastructure, we will lose external competitiveness over time.

Second, pressure on Europe’s cost competitiveness emphasises the importance of investing in key areas such as technology and education, which support the euro area’s non-price competitiveness. This in turn means that we need to direct public expenditure more towards investment, notably in human capital and research and development. In the years that preceded the pandemic, euro area public investment barely compensated for the depreciation of the capital stock[17], which had direct implications for the quality of public infrastructure. And the share of public money spent on education is at a historic low.[18] We may already be seeing the results of this underinvestment. According to the OECD Programme for International Student Assessment (PISA)[19], since 2009 the average performance of 15-year-olds in the euro area has dropped by 19 points in mathematics, and 14 points in reading and science.[20]

Third, we need to ensure that European companies can reap the benefits of the Single Market. In practice, this means enabling them to operate seamlessly across the entire continent. Otherwise, we will be left with the status quo where global players that benefit from a large domestic market also end up dominating the European market, while firms in Europe remain confined to their national markets. This reduces competition in Europe and undermines our competitiveness. And the risk is further accentuated by the ongoing global subsidies race. This is best addressed by a common European response that protects fair competition for all European companies, rather than uncoordinated national strategies that risk further undermining the Single Market.

In other words, the external competition we face should stimulate us to act together to support and create the conditions for higher domestic investment. And ensuring open and fair competition within the Single Market is a necessary condition for the euro area’s external competitiveness.

Cooperation that strengthens

Let me now turn to the second principle of the economic model envisaged by Delors, “cooperation that strengthens”.

As long as the euro area remains primarily a monetary union, with fiscal and economic policies conducted mainly at the national level, cooperation is crucial for us to achieve our shared objectives. [21] As an example, in 2022 EU budgetary spending was equivalent to a mere 2.5% of EU Member States’ total government spending. This means that the stabilisation, allocation and redistribution functions of fiscal policy remain overwhelmingly in the hands of national governments.

But if Member States cooperate with each other, they can exchange valuable insights and practices. For instance, the success of the short-time work schemes that were available in some countries during the global financial crisis led to other euro area countries replicating them. During the pandemic, these schemes helped protect employment, incomes and productive capacity across the entire euro area, enabling a swifter recovery. And at European level, the SURE[22] instrument enabled these schemes to reach their full potential.[23]

The need for cooperation among Member States was formalised in an economic governance framework that incorporates rules on national government spending, as stipulated in the Stability and Growth Pact. Although these rules were strengthened and expanded in response to the sovereign debt crisis, the first 25 years of the euro have highlighted some limitations. Fiscal governance in particular has suffered from excessive complexity and a lack of ownership. It did not prevent procyclical policies and high levels of public debt in some Member States. And it failed to incentivise public investment.

The review of the economic governance framework was launched to address these issues and I welcome the political agreement reached by co-legislators. While the revised framework remains fairly complex, it will help strike a balance between sustainable public finances and debt reduction on the one hand, and incentives to commit to reforms and investment on the other, while also supporting countercyclical fiscal policies. But it is essential that the revised framework is implemented in a manner that remains faithful to its objectives, otherwise it will not be credible.

At the same time, fiscal rules remain complex and focused on national circumstances, with limited consideration for their implications for the aggregate euro area fiscal stance. And a purely rules-based approach entails a difficult trade-off between discretion and credibility. This requires moving the focus of the governance framework from rules to institutions.[24] While our rules are of course a crucial anchor of confidence, there are several good reasons for granting European institutions greater discretionary power where needed.

First, European institutions can play a pivotal role in facilitating cooperation among Member States. The European Commission is a case in point.

Second, European institutions can establish stronger ownership, underpinned by clearer and more direct accountability. This applies both in a democratic sense, towards the European Parliament and the Council, and in a judicial sense, towards the European Court of Justice. In this respect, the ECB has long supported integrating the European Stability Mechanism (ESM) into the EU’s legal framework [25], particularly in view of its expanded powers. A commitment to bringing the ESM under the EU’s legal framework during the next legislative term could help unlock the current stalemate on the ratification of the revised ESM Treaty – which is essential to make the Single Resolution Fund's common backstop operational and an integral step towards completing the banking union.

Third, strengthening the role of European institutions can help to account for spillovers across countries and policy areas. For instance, it enables us to better account for the implications of individual countries' fiscal measures for the fiscal stance of the euro area as a whole. And this in turn makes it easier to define macroeconomic policies. Demand shocks, for example, require fiscal policy and monetary policy to work in the same direction. The response to adverse supply shocks, meanwhile, can benefit from a situation in which fiscal policy and monetary policy complement each other. Targeted and temporary fiscal support can smoothen the inflationary impact of such shocks, helping monetary policy to keep inflation expectations anchored.[26] And fiscal policies that support supply reduce the need for monetary policy to dampen demand. Combined with a monetary policy aimed at preserving price stability, such fiscal policies lower the risks of stagflation. Over time, they also reduce the risk of scarring the economy, which would reduce potential output.[27]

But today, supply shocks are unwinding. Supply disruptions have eased and energy prices have fallen, therefore a different combination of macroeconomic policies is required. On the one hand, governments should continue to roll back energy-related support measures, while seeking to reduce the euro area's exposure to volatile fossil fuel prices by diversifying their sources of energy. On the other hand, with demand still weak and inflation expectations anchored, there is no need for monetary policy to generate further slack to keep inflation in check. The unwinding of supply shocks creates scope for demand to recover without fuelling inflation.

In this phase, another type of cooperation is useful – cooperation between and with social partners. This was close to Jacques Delors' heart, and he often stressed its importance. For me it is not a solely theoretical issue: my university mentor Ezio Tarantelli was assassinated by terrorists because of his ideas about combating inflation through social dialogue.[28] But social dialogue is as relevant today as it was in their times. In the euro area, for example, the terms of trade tax that resulted from the energy shock has been absorbed mostly through workers' lower real incomes, while profits have held up. Lower energy prices now create scope for some wage catch-up, especially if profits normalise. But it will ultimately be a combination of these dynamics that determines whether inflation converges durably to our target. This is why we need to remain data-driven as we consider our next monetary policy decisions.

Solidarity that unites

Let me now turn to the third principle of the economic model advocated by Delors: "solidarity that unites". We cannot expect solidarity to emerge if it is not understood to be in the best interests of both the euro area as a whole and each of its members. And we cannot maintain solidarity in our Economic and Monetary Union if it is seen as a "transfer union". EMU will only be supported if there is a shared understanding that we all benefit when we act together and support each other.

Responding to exogenous shocks

Owing to intertwined supply chains, financial networks and trade links, euro area countries' economies are closely interconnected. Trade between them, for instance, represents around half of euro area GDP.[29] So while much of Europe's strength stems from this interconnectedness, it also means that economic developments in euro area countries cannot be seen in isolation: a downturn in one part of the euro area can lead to lower growth and employment across the entire region.[30]

When faced with exogenous economic shocks, everyone stands to benefit from this solidarity.[31] A common response carries more economic weight as benefits in one country spill over to other countries. We saw this clearly in the European response to the pandemic. Unlike during previous crises, Europe responded in a way that was both countercyclical and united. As a result, the economic cost for the euro area was much lower than that of the financial and sovereign debt crises. It took two years for GDP and employment to return to their pre-pandemic levels. This was much faster than after the global financial crisis, when it took GDP seven years and employment nine years to return to pre-crisis levels. And the cost in terms of higher public debt as a share of GDP has been much lower.[32]

Responding to common structural challenges

Our ability to act together is also crucial in responding to the common structural challenges we face. This is particularly evident in areas such as the energy and digital transitions, as well as defence, where there are large economies of scale and mutual benefits to joint initiatives. Given the size of the financing needs and the implications for the euro area's competitiveness and resilience, investments in these public goods are best made together.[33] The Commission has estimated that the EU's green and digital transitions will require additional annual investments of €620 billion and €125 billion respectively.[34] And while much of this will have to come from private funding, estimates show that between one-quarter and one-fifth of the additional investment for the green transition will need to be funded by the public sector.[35]

During the pandemic, European solidarity gave rise to a significant new instrument: Next Generation EU (NGEU). It offered a European safe asset, supporting confidence at a time of crisis and preventing financial amplification. It focused on common priorities – digitalisation and the green transition – and protected competition by reducing the temptation of beggar-thy-neighbour policies within the Single Market. And with Member States reviewing each other's recovery and resilience plans, it gave fresh impetus to cooperation. NGEU illustrates the potential of European initiatives and its implementation is now well under way.

But we must ensure that NGEU lives up to its full potential. This will depend crucially on the quality of the reforms and investments implemented under the Recovery and Resilience Facility (RRF). Despite significant progress on both the reform and investment fronts, we see that Member States are finding it challenging to maintain the pace envisaged in their recovery and resilience plans.[36] As we approach the end of NGEU's disbursement horizon, we need to deal with the challenge of disbursing available RRF funds by end-2026. Considering the RRF's positive track record and the major challenges ahead for Europe, we should think carefully about how to strike a balance between ambition and speed. The positive impact of these funds on potential output depends not only on the capital contribution they represent but also on their ability to lift total factor productivity growth. And this hinges on the funds being used well. With the RRF mid-term review upcoming, now is a good time to reflect on how best to ensure good use of funds and whether the disbursement period could be extended for this purpose.[37]

At the same time, if we want to be able to take the action needed to finance the investments required to respond to our common challenges, we also need to start discussing what comes after NGEU – a key question for the next Commission.

Conclusion

Let me conclude.

As external – and especially geopolitical – challenges become more frequent and severe, bolstering Europe's resilience to these challenges and the associated economic shocks becomes more crucial. Put simply, the "costs of non-Europe", a key reason behind Delors' initiative to establish the Single Market and EMU[38], are on the rise. It is therefore vital that we further strengthen these two central elements of our European project. Initiatives like NGEU have shown the potential benefits of taking action at the European level and embracing the principles of Delors' economic model. If we want to strengthen our union through competition, cooperation and solidarity, this should not be a one-off.

Thank you for your attention.

1.

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2.

European Commission (2023), "Standard Eurobarometer 100 – Autumn 2023".

3.

Delors, J. (1995), "Speech before the European Parliament", Strasbourg, 19 January.

4.

The four freedoms are the free movement of goods, the free movement of capital, the freedom to establish and provide services, and the free movement of people.

5.

European Commission (2023), "Flash Eurobarometer 538: The euro area", November.

6.

See, for example, Ottaviano, G.I., Taglioni, D. and Di Mauro, F. (2009), "The euro and the competitiveness of European firms", *Economic Policy*, Vol. 24, No 57, pp. 6-53. The authors find that enhanced price transparency and lower transaction costs generate several benefits when compared with counterfactual scenarios without the single currency. These benefits arise from countries increasing their specialisation in sectors in which they are more efficient, a richer variety of products, individual firms having less market power, a better exploitation of economies of scale, and improved production efficiency as the least efficient firms exit the market.

7.

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8.

Mundell, R.A. (1961), “A Theory of Optimum Currency Areas”, *The American Economic Review*, Vol. 51, No 4, pp. 657-665.

9.

Beyer, R.C.M. and Smets, F. (2015), “Labour market adjustments and migration in Europe and the United States: how different?”, *Economic Policy*, Vol. 30, No 84, pp. 643-682. For statistics on intra-EU labour mobility, see European Commission (2023), *Annual Report on Intra-EU Labour Mobility 2022*.

10.

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11.

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12.

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13.

ECB (2021), *ECB contribution to the European Commission’s targeted consultation on the review of the crisis management and deposit insurance framework*, May.

14.

ECB (2023), *A stocktake on the digital euro – Summary report on the investigation phase and outlook on the next phase*, 18 October.

15.

Attinasi, M.G., Ioannou, D., Lebastard, L. and Morris, R. (2023), "Global production and supply chain risks: insights from a survey of leading companies", *Economic Bulletin*, Issue 7, ECB.

16.

Ibid. Firms cite the changing geographical distribution of sales as one of the main factors for moving production out of the EU.

17.

Panetta, F. (2022), "Investing in Europe's future: The case for a rethink", speech at Istituto per gli Studi di Politica Internazionale (ISPI), 11 November.

18.

European Commission (2023), *Investing in education 2023*.

19.

The decline in educational performance identified in the results of PISA 2022 is only partly attributable to the COVID-19 pandemic. See OECD (2023), "Decline in educational performance only partly attributable to the COVID-19 pandemic", 5 November.

20.

Source: OECD PISA database and ECB staff calculations.

21.

Jacques Delors referred to a lack of cooperation as a key missing link in EMU on several occasions. See, for example, Delors, J. (2012), "The Single Market, Cornerstone of the EU", speech at a conference on the occasion of the 20th anniversary of the Single Market, 22 November.

22.

The temporary support to mitigate unemployment risks in an emergency (SURE) instrument provided financial assistance of up to €100 billion in the form of loans granted on favourable terms from the EU to affected Member States to address sudden increases in public expenditure for the preservation of employment.

23.

Anderton, R. et al. (2020), "The impact of the COVID-19 pandemic on the euro area labour market", *Economic Bulletin*, Issue 8, ECB; Dias da Silva, A. et al. (2020), "Short-time work schemes and their effects on wages and disposable income", *Economic Bulletin*, Issue 4, ECB.

24.

Draghi, M. (2015), "Speech by the President at SZ Finance Day 2015", 16 March.

25.

See also Opinion of the European Central Bank on a proposal for a regulation on the establishment of the European Monetary Fund (CON/2018/20), OJ C 220, 25.6.2018, p. 2.

26.

Chi Dao, M., Dizioli, A., Jackson, C., Gourinchas, P.-O. and Leigh, D. (2023), "Unconventional Fiscal Policy in Times of High Inflation".

27.

Fornaro, L. and Wolf, M. (2023), "The scars of supply shocks: Implications for monetary policy", *Journal of Monetary Economics*, Vol. 140, November, pp. S18-S36.

28.

Cipollone, P. (2023), "Opening statement to the Economic and Monetary Affairs Committee of the European Parliament", Strasbourg, 9 October.

29.

Intra-euro area trade is measured as the sum of intra-euro area imports and intra-euro area exports.

30.

Panetta, F. (2020), "Why we all need a joint European fiscal response", contribution published by Politico, 21 April.

31.

See Farhi, E. and Werning, I. (2017), "Fiscal Unions", *American Economic Review*, Vol. 107, No 12, December. The paper shows that international fiscal transfers in response to asymmetric shocks improve macroeconomic stability in a currency union.

32.

In 2012 the euro area debt-to-GDP ratio was 27 percentage points higher than in 2007. In 2023 it was 4 percentage points higher than in 2019 according to the European Commission Autumn 2023 forecast (and is expected to be lower in 2024 compared with 2023).

33.

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34.

European Commission (2023), "2023 Strategic Foresight Report: Sustainability and people's wellbeing at the heart of Europe's Open Strategic Autonomy", communication from the Commission to the European Parliament and the Council, 6 July.

35.

Darvas, Z. and Wolff, G.B. (2021), "A green fiscal pact: climate investment in times of budget consolidation", *Policy Contribution*, No 18/21, Bruegel, 9 September.

36.

ECB calculations suggest that payment requests linked to about 5% of funds in the planned envelope are overdue.

37.

This would need to be limited in time and would need to include a quality review.

38.

Cecchini, P., Catinat, M. and Jacquemin, A. (1988), *The European Challenge 1992: The Benefits of a Single Market*, Wildwood House.