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**COMMUNICATION FROM THE COMMISSION**

**A roadmap to stability and growth**

*"We reaffirm our commitment to the Euro and to do whatever is needed to ensure the financial stability of the Euro area as a whole and its Member States."*

(Statement by the Heads of State or Government  
of the Euro area and EU institutions, 21 July 2011)

## INTRODUCTION

What the EU most needs now is to deploy all the necessary means to deliver future stability and growth at once and to the full. Many far reaching decisions have been made in the past eighteen months. In order to restore confidence in the Euro area and the EU as a whole, these decisions need to be integrated and completed. The crisis threatens to become systemic. A solution to break the vicious circle between doubts over the sustainability of sovereign debt, the stability of the banking system and the EU's growth prospects is more necessary than ever. The elements presented in this paper are interdependent and must be implemented together as quickly as possible to have their intended effect. No single element by itself will be sufficient to resolve the current crisis. Only taken together and simultaneously will they convincingly demonstrate that the EU can:

1. Give a decisive response to the problems of Greece
2. Enhance the Euro area's backstops against the crisis
3. Strengthen the banking system, namely through recapitalisation
4. Frontload stability and growth enhancing policies
5. Build a more robust and integrated economic governance

### **1. A DECISIVE RESPONSE TO THE PROBLEMS OF GREECE**

The continuing doubts over Greece have contributed very significantly to undermining confidence in the financial stability of the Euro area as a whole. They must be immediately and definitively removed.

Subject to the assessment of the EU/ECB/IMF troika, this will require:

- Provided the current programme is back on track, disbursement of the payment of the sixth tranche of the programme for Greece.
- Deciding a sustainable solution for Greece within the Euro area, through an effective second adjustment programme, based on adequate financing through private sector involvement (PSI) and the public sector, leaning on robust implementation and monitoring mechanisms.

- Continued support from the Commission Task Force on Greece, underpinning full and timely implementation of the programme and channelling the available structural funds to strengthen competitiveness and return to growth.

## 2. ENHANCING THE EURO AREA'S BACKSTOPS AGAINST THE CRISIS

As recently as 21 July 2011, the Heads of State or Government of the Euro area and EU institutions have reaffirmed the determination to continue to provide support to countries under programmes until they regain market access, provided they successfully implement those programmes. They emphasised that as far as private sector involvement is concerned, Greece requires an exceptional and unique solution.

The Euro area must be fully equipped with the instruments needed to meet any future crisis scenarios. The availability of the necessary instruments would widen the spectrum for alternative solutions while providing much needed reassurance to market participants. Recent decisions to create the EFSF and ESM have gone a long way towards building these instruments but they still need to be completed and complemented.

The first step is to make rapidly operational the decisions taken by the Euro area summits in March and on 21 July 2011 to increase the flexibility and effectiveness of the EFSF (and the ESM) in particular with regard to:

- Precautionary programmes. Access to such channels should be conditional upon requesting Member States agreeing to graduated macro-economic adjustment programmes, on which there should be prior consultation of the Commission and the ECB. Stronger monitoring and surveillance is needed and could be agreed politically and included in the Code of Conduct on the Stability and Growth Pact.
- Assisting Member States with the banking recapitalisation process through loans to non programme countries, as a complement to private sector solutions and national means where necessary.
- Improving the capacity of the EFSF to intervene by purchasing government debt in primary markets and to intervene in secondary markets where exceptional market circumstances and risks to financial stability exist, under appropriate conditionality.

Moreover, the firepower of the backstop mechanisms should be enhanced by maximising the use of the EFSF, without increasing the guarantees underpinning it and within the rules of the Treaty of Lisbon, in particular on monetary financing.

Early introduction of the ESM would also reinforce confidence in the crisis resolution mechanism and bring the advantages of a more robust, permanent instrument. Efforts should be made to accelerate the technical preparation and ratification procedures to have the ESM operational by, for example, mid 2012.

The ECB plays a crucial role in securing the financial stability of the Euro area as a whole by ensuring sufficient liquidity for the Euro area banking sector and supporting the proper functioning of sovereign bond markets while preserving price stability.

### 3. STRENGTHENING THE BANKING SYSTEM, NAMELY THROUGH RECAPITALISATION

Both in regulatory and financial terms huge efforts have been deployed to strengthen Europe's banks given their role in the stability and functioning of our economy. . Banks have also considerably improved the quality and quantity of their capital base.

The EU has overhauled the way banks are supervised and has taken legislative measures to increase the amounts of regulatory capital banks have to hold, to address risky re-securitisation operations, to ensure remuneration policies do not encourage excessive risk, and to increase protection of citizens' bank deposits up to a present threshold of €100 000. Swift adoption of CRD IV will establish a robust capital ratio for banks and implement the Basel III standards.

Ongoing uncertainty in the sovereign debt markets has led to increasing volatility and is putting the banking sector under mounting pressure. For the foreseeable future, efforts need to focus on facilitating banks' access to term liquidity in particular restoring long term liquidity in the sector, accompanied by **steps to strengthen the capital of banks that need it**.

To restore confidence in the EU banking sector, a coordinated, targeted recapitalisation effort is needed, in conjunction with the other elements of this strategy. This requires the combined efforts of Member States, the European Banking Authority (EBA) and the European Central Bank alongside the Commission. A bank recapitalisation strategy following the work of the EBA should include the following elements:

- Covering all potentially systemic banks across all Member States – i.e. the banks that were covered by EBA's July 2011 stress tests, excluding some smaller domestic banks with no international activities.
- Accounting for all exposures to EU sovereign debt of the banks concerned (prudent valuation of all sovereign debt, whether in the banking book or the trading book) to ensure full transparency on asset quality.
- Requiring a temporary significantly higher capital ratio of highest quality capital after accounting for exposure. The definition of capital broadly equates to the definition set out by the Basel III international agreement for attainment in 2015.
- Banks that do not retain the necessary capital should present recapitalisation plans and implement them as swiftly as possible. In practical terms, national supervisors should set these requirements through their existing supervisory powers in the form of additional buffers which prevent the distribution of dividends or bonuses pending the recapitalisation.
- Banks should first use private sources of capital, including through restructuring and conversion of debt to equity instruments. If necessary the national government should provide support, and if this support is not available, recapitalisation should be funded via a loan from the EFSF. Any recapitalisation from public sources should be compatible with the EU state aid rules. The Commission intends to extend the applicability of the existing state aid framework for bank support beyond 2011.

At the same time, the on-going **work on a new system of regulation for the financial sector needs to be completed** as swiftly as possible. The Commission will deliver the remaining proposals by the end of this year, namely reinforced rules on credit rating agencies, transparency and market conduct on all trading platforms, a strengthened framework to combat market abuse, including criminal sanctions and a European framework on bank resolution. It will be essential to ensure swift adoption of all these proposals by the co-legislators, ideally within 12 months of their presentation by the Commission.

The proposed **Financial Transaction Tax** should be adopted equally quickly on the EU level as a means to ensure that the financial sector contributes fairly to recovery. The EU should continue to advocate its adoption at the global level.

#### **4. FRONTLOADING STABILITY AND GROWTH ENHANCING POLICIES**

Most Member States do not have room for a new fiscal stimulus because they need to give top priority to fiscal consolidation. We need to focus on implementing the country specific recommendations made under the first European semester and on prioritising public spending on growth areas, removing obstacles and tapping into underutilised potential. Member States, in particular those experiencing tensions in sovereign debt markets, should commit to stronger growth enhancing structural reforms.

We have several structural growth levers to hand at EU level – getting more out of the single market, maximising our trade performance and exploiting the potential of recently concluded trade agreements are just some of the elements. Moreover, the current crisis shows that we have to mainstream competitiveness into EU policies. Particular gains can be obtained from actions focused on technology sectors with high growth potential through development of a digital single market.

A targeted boost to growth and employment could be achieved by the following:

- **Getting more out of what has already been agreed at EU level**, for example:
  - Full implementation of the Services directive
  - Completion of the integrated market for energy which would give consumers choice between suppliers and make markets fully accessible for energy providers.
  - Implementation of the late payments directive should be advanced from March 2013 to January 2012, in order to help SMEs
  - Full implementation of the Free Trade Agreement with Korea
- **Accelerating adoption of what is pending in co-decision:**
  - The proposed unitary European patent protection valid in 25 Member States would lead to an estimated 80% reduction in costs for companies.

- The pending revision of the directive on annual accounts would simplify reporting requirements in particular through exemptions for micro enterprises
  - Increasing co-financing rates for Structural Funds in programme countries as proposed would enable the rapid mobilisation of EU funds in support of growth.
  - The proposed energy savings directive would promote more efficient use of energy
  - Concluding the further trade agreements which are underway with key strategic partners.
  - Adopting the proposals on savings tax and other tax initiatives already presented.
  - Giving the Commission the mandate to negotiate tax agreements for the whole EU with third countries to effectively fight tax evasion whilst avoiding double taxation.
  - Adopting the optional Common European Sales Law
- **Fast-track future proposals that the Commission will propose in the coming months, including:**
    - The twelve proposals of the Single Market Act including:
      - Facilitating access to venture capital across Europe through an EU passport
      - Providing a common legal base for mutual recognition of e-authentication and electronic signature across borders.
      - Revising the public procurement framework to provide simpler rules and more transparent procedures.
    - Other proposals:
      - A Young Opportunities initiative to boost youth employment, in particular access to a first job.
      - Collective rights management/copyright law to create a single market for copyright – it is estimated that this could treble on line music sales.

Where it proves difficult to find agreement on fast tracked proposals the use of enhanced co-operation should be envisaged.

This should be complemented by **targeted investment at the EU level**. Next week the Commission will launch the Europe 2020 Project Bond Initiative by proposing a pilot phase during the current financial framework. That way, we will be able to expand the investor base for funding some of the major infrastructure investments the EU and the Single Market need. The initiative will be developed further in the Commission's proposal for the Connecting Europe Facility under the next Multi-annual financial framework. The Union and its Member States should also urgently consider how to allow our policy-driven bank, the EIB, to do more to finance longer term investment, including through the use of innovative financing instruments. To do so, the Commission will explore ways to reinforce the EIB's resources and capital base so that it can lend to the real economy.

## **5. BUILD ROBUST AND INTEGRATED ECONOMIC GOVERNANCE FOR THE FUTURE**

Fundamentally, the restoration of stability and sustainable economic growth in the Euro area and the wider EU can only be achieved by the pursuit of sound policies at the national level, in the context and under the guidance of the appropriate Community governance. This must come from a reinforced commitment among Member States to restore and reinforce public debt sustainability via an appropriate combination of budgetary consolidation and growth-enhancing structural reforms. The European Semester and the new "six-pack" legislation already provide a strong governance framework which needs to be strengthened further, including in its Community dimension. There should be a stronger Euro-area dimension in the planning, implementation and ex-post assessment of Member State policies to ensure stronger economic policy co-ordination, based on surveillance procedures that become increasingly tighter (i.e. imply greater constraints on national budgets and economic policies), thereby entailing a greater integration and discipline of economic policy responsibility at the Euro-area level, through rules that cannot be broken. In this context, the further reinforcement of the role of the commissioner responsible for economic and monetary affairs will also be considered. The Commission has announced that it intends to work towards a single, coherent framework for better economic governance on the basis of the Community method. It will make the necessary proposals to that effect.

In keeping with the decisions of the Euro area summit on 21 July 2011 the President of the European Council, in close consultation with the President of the Commission and the President of the Eurogroup, will make concrete proposals on how to improve working methods and enhance crisis management in the Euro area, namely through a more streamlined process between the Euro area summit, the Eurogroup and the Euro area working group.

In addition, to deliver better economic governance for the future we need to:

- Implement the "six-pack" as soon as possible including through stronger preventive and corrective tools under the Stability and Growth Pact (deficit/debt criteria) and by implementing the new macro-economic imbalances procedures (Excessive Imbalances Procedure).
- Strengthen the European Semester of economic policy coordination to intensify surveillance of economic and fiscal policies, including by integrating the Euro Plus Pact into its procedures.

Even though rapid and strict implementation of the new "six-pack" will be challenging there is a need to go further by:

- Setting out provisions for strengthening the economic and budgetary surveillance of Euro area Member States requesting or receiving financial assistance from the EFSF, ESM, IMF or another IFI. The Commission will make a proposal to the Council and the European Parliament under Article 136.
- Monitoring the national budgetary policies of Euro area Member States in excessive deficit procedure/programme countries through a Commission/Council procedure which would enable the Commission/Council to intervene, for example to examine national draft budgets ex-ante, to request a second reading in serious cases, to suggest amendments in the course of the year and to monitor budgetary execution. The Commission will make a proposal to the Council and the European Parliament under Article 136 setting out the graduated steps and conditions that should apply in such cases.
- In keeping with stronger internal governance of the Euro area there is a need to move towards more unified external representation for the Euro area. The Commission will make proposals on steps to achieve this.
- Assessing and developing options for "stability bonds" as part of the arsenal of policy instruments for the Euro area within the further reinforced economic governance. The Commission will publish a Green Paper on the main options before the end of the year.

In order to speed up the delivery of better economic governance, enhanced cooperation should be envisaged in all cases where otherwise decisions would be kept pending for a longer period.

Finally, it may be appropriate to enshrine some or all of these steps in the formal framework of a Treaty revision. This would not serve as an immediate response to the current crisis which must be addressed through the swift and decisive implementation of the measures presented in this Communication. Once this has been done, Treaty changes could be envisaged to consolidate and give even greater impact to the new Community architecture that is now being put in place via secondary legislation. Treaty change may also be helpful to ensure the coherence of deeper integration within the Euro area with the Union as a whole, in particular the Single Market.