
DEEPENING OF THE EMU: ARE BANKING UNION AND FISCAL UNION SUBSTITUTES OR COMPLEMENTS?



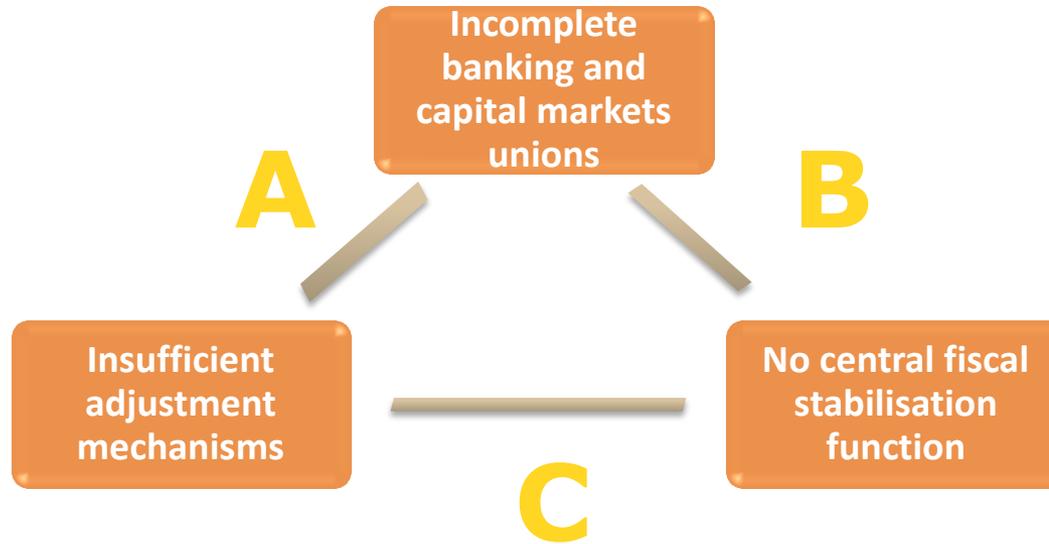
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EMU today: An unstable equilibrium



- **Insufficient private and public risk-sharing**
- **Overburdening of monetary policy**
- **Risk of renewed financial instability**

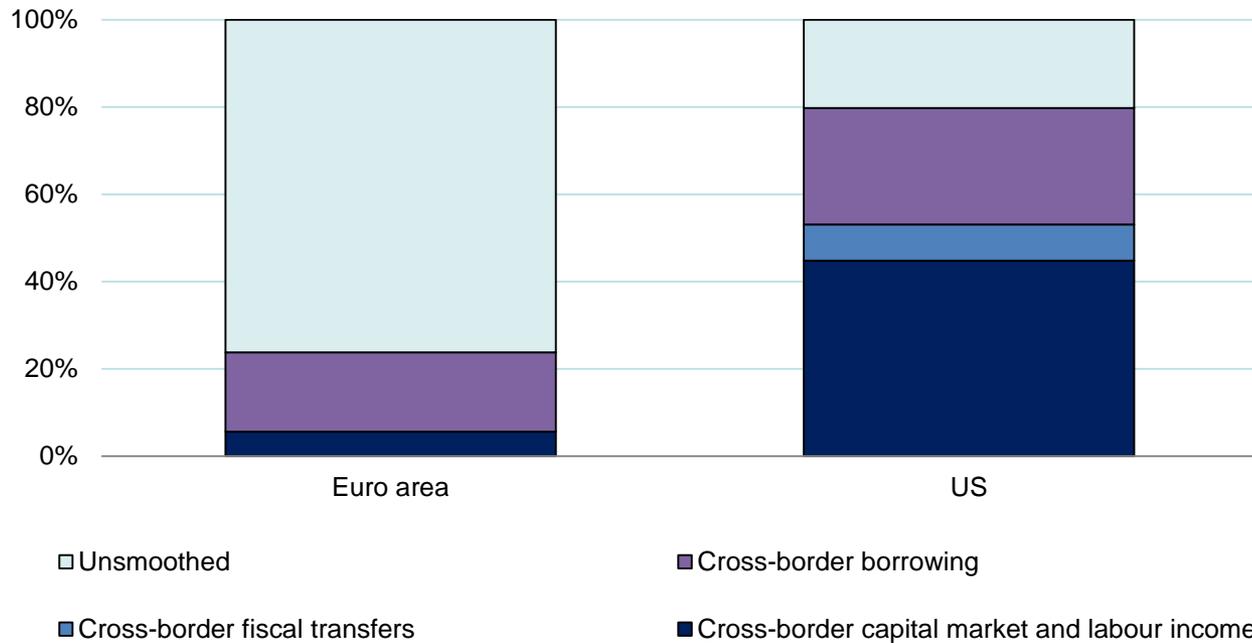
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Financial union: the most urgent priority for EMU

Smoothing income shocks via financial markets remains low

Cross-border risk sharing through different channels, in % of total asymmetric shock to output

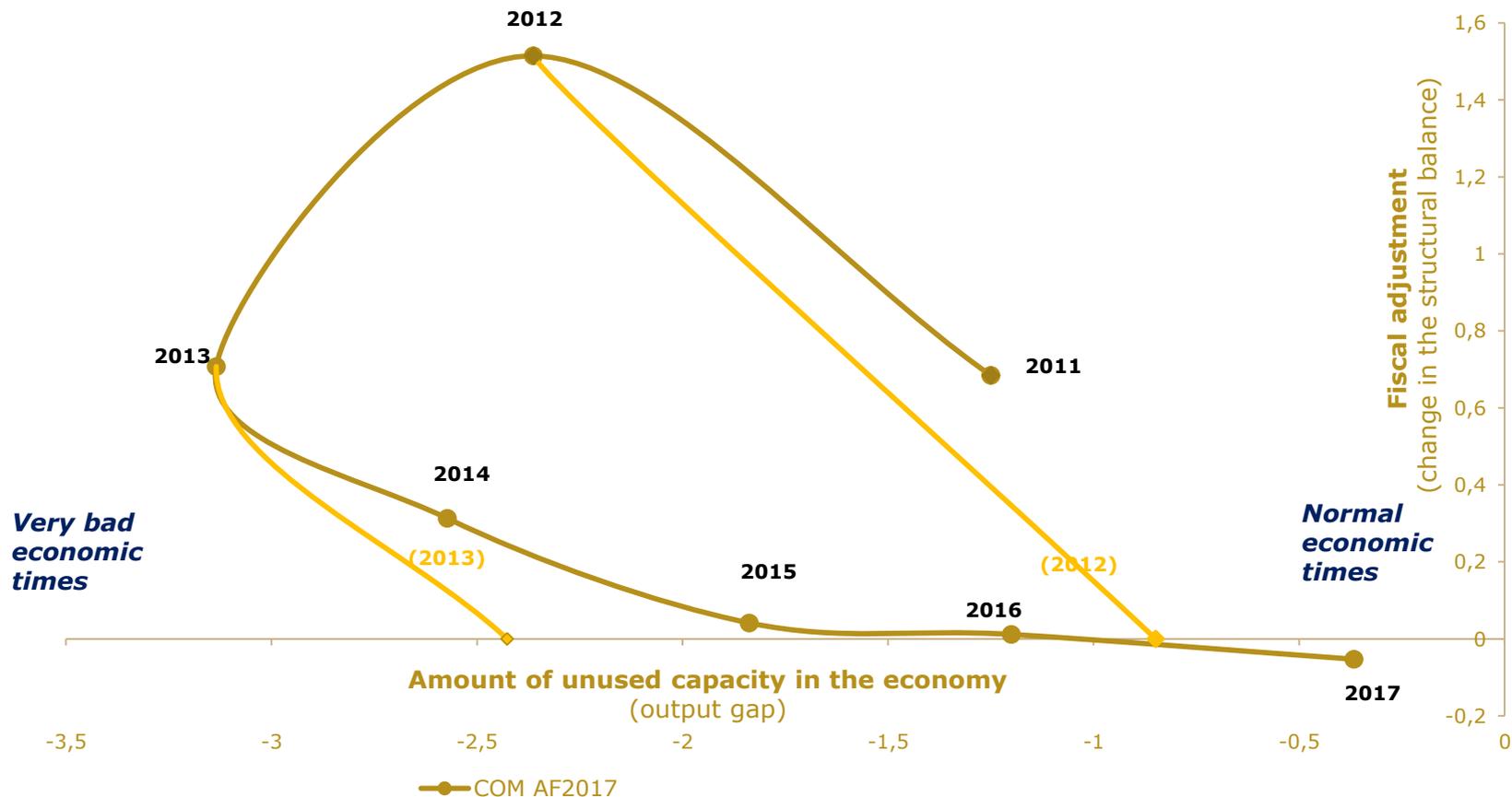


Source: Buti et al. (2016). Smoothing economic shocks in the Eurozone: The untapped potential of the financial union, VOX August.



Fiscal union

Benefits of a central stabilisation capacity



ARE FINANCIAL AND FISCAL UNION SUBSTITUTES OR COMPLEMENTS?

- Portfolio diversification and capital movement help absorb shocks in "normal" times but tend to be procyclical in "bad" times
- Central stabilisation can foster private risk-sharing (cross-border ownership of assets) by reducing country specific macro-risks (better smoothing of large asymmetric shocks and less need for state procyclical fiscal adjustment)
- Fiscal insurance to tackle and reduce shocks arising from the real economy before they reach the financial sector
- EMU financial union unlikely to look like in the US in the medium-period (some degree of home-bias will stay, financial system to remain bank-centred)



Next Steps: Financial Union

Advancing in parallel on risk-reduction and risk sharing

False dichotomy between risk-sharing and risk-reduction

Immediate priority

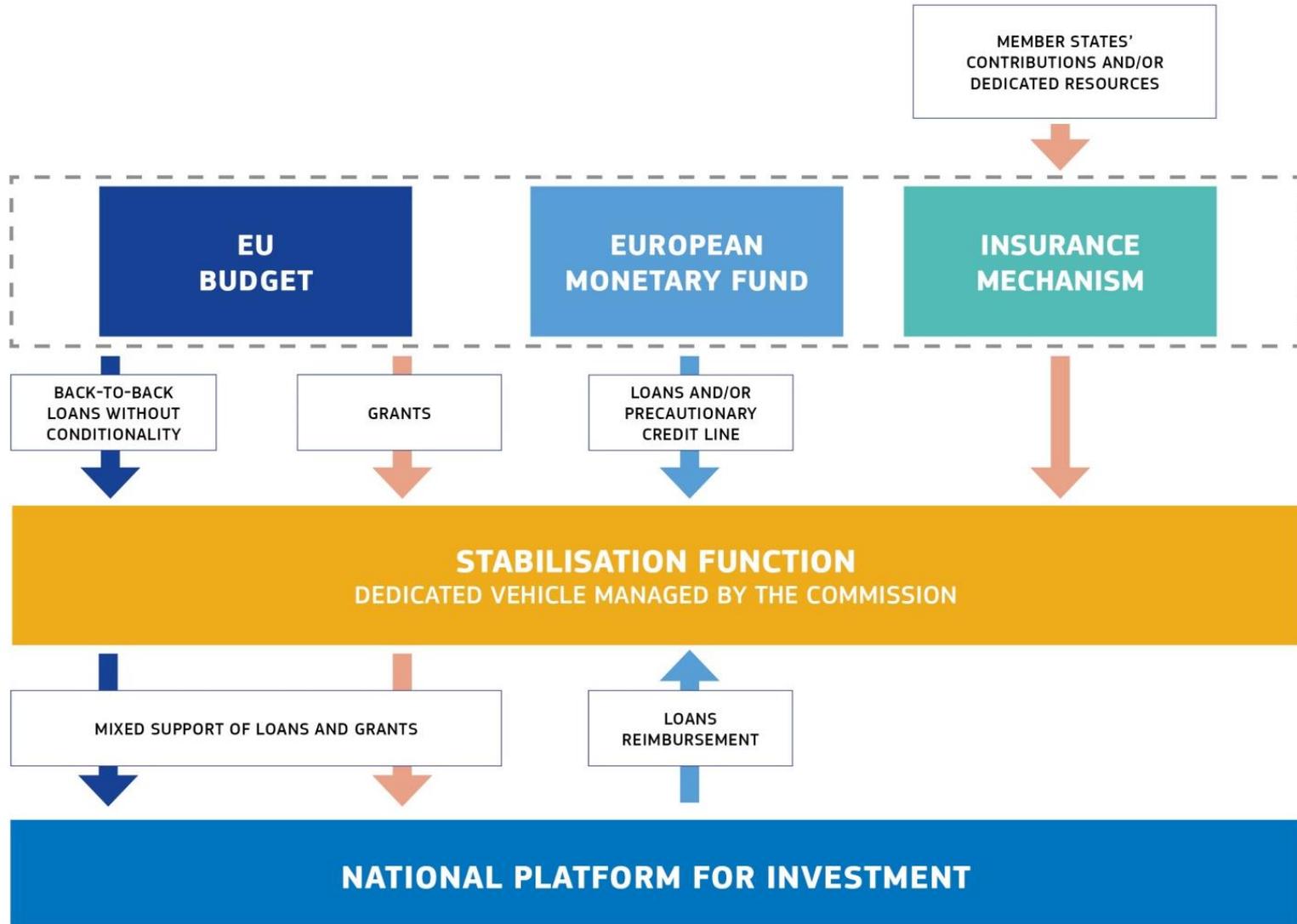
- Further reducing risks and building on banks' better capitalisation
- Setting up the backstop to the SRF
- Agree on EDIS
- Delivering on the Capital Markets Union (CMU)

Post-2019: possible additional successive measures

- European Safe Asset
- Regulatory treatment of sovereign bonds



Next Steps: A European stabilisation function to protect investment





Future of EU Fiscal Governance: Searching for the right balance

Elements of centralisation

Simplified fiscal rules

A common fiscal capacity

Last resort backstop to the banking union

Reinforced ability to intervene in case of gross errors

Elements of decentralisation

Operational national rules with links to the EU framework

More binding nature of medium-term fiscal planning at MS level

Empowered independent national fiscal institutions

Reinforced market discipline

Fiscal federalism by exception vs No bail out/market discipline



Thank you very much for your attention