

The European Financial Stability Framework: Recent Progress and Remaining Challenges



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Background: crisis has revealed gaps in European institutional frameworks



- **Coordination of structural reforms (least progress)**
 - Disappointing results of the Lisbon agenda
 - EC, Council and ECB proposals to introduce structural reform surveillance
- **Fiscal policy governance (some progress)**
 - EC, Council and ECB all support strengthening sanctions to ensure compliance with EDP and with requirements of SGP.
- **Financial stability framework (most progress)**
- **Monetary policy governance (?)**

New financial stability framework is taking shape



- **Financial integration outpaced the development of a common stability framework**
- **Following the collapse of Lehman, strong push for reform**
 - Financial supervision and rule-making (most progress)
 - Crisis prevention and macro-prudential policies (some progress)
 - Crisis management and resolution (least progress)

New supervisory and regulatory framework



- Formally established January 1, 2011
- Creation of European System of Financial Supervisors
 - Macro-prudential arm: European Systemic Risk Board (ESRB)
 - Micro-prudential arm: national supervisors + new sectoral European Supervisory Authorities (ESAs)+ cross-sectoral joint committee
- ESAs are expected to work toward establishing a single rulebook for the financial sector
- Efforts, led by the Commission, to achieve greater harmonization in existing and future legislation
- ESRB will operate with limited resources and without own policy tools

Crisis management and resolution



- **EC aims at harmonizing and improving national systems**
 - Early intervention tools
 - Bank resolution regimes
 - National resolution funds
 - Deposit guarantee schemes
- **Question of integrated frameworks to be revisited in 2014**
- **IMF staff has advocated the creation of a European Resolution Authority, supported by an industry-financed European Deposit Insurance and Resolution Fund and a fiscal backstop (see Fonteyne et al. 2010)**

Nordic-Baltic Agreement on Financial Stability, Crisis Management and Crisis Resolution



- MoU signed on August 17, 2010 establishes the Nordic-Baltic Stability Group.
- First cross-border financial stability group within Europe.
- Agreement has novel aspects:
 - Involves MoFs, central banks and supervisory agencies
 - Sets up permanent regional forum
 - Includes a preliminary ex ante burden-sharing formula
- Significant and meaningful step towards integration of cross-border crisis prevention and management

Some thoughts on the future of ECB governance



- **Stella and Vandenbussche (2010) discuss ECB governance and decision-making**
 - Issue of optimal size of Governing Council in light of past and future enlargement
 - Efficiency / legitimacy tradeoff
 - Different central bank functions may call for different governance structures or decision-making processes
 - ✦ E.g. conventional vs non-conventional operations
 - Experience of the US system of Federal Reserve Banks in the 1930's
 - ✦ Times of crisis often lead to greater centralization of power

References



- IMF, Regional Economic Outlook Europe, October 2010
- Fonteyne W. et al (2010), “Crisis Management and Resolution for a European Banking System”, IMF Working Paper 10/70
- Stella P. and J. Vandenbussche (2010), “Governance and Decision-Making at the ECB”, in “The ECB at Ten”, J. de Haan and H. Berger editors, Springer Verlag.