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***Ex post vs. ex ante* debt restructuring**

**Sovereign Debt Crises:
Prevention and Management
Rome, 10 December 2018**

Overview

- The aim of my intervention is to show that the EMU's most fragile countries (such as Italy) → an unfavorable bargain between two new roles of the ESM:
 - backstop in the 2nd pillar of the BU (by 2020), as stated by the Eurogroup (December 4th, 2018);
 - possibly, decision-maker of an *ex ante* public debt restructuring (SDRM).

Outline

- Three steps to pursue this aim:
 - (1) Short recall of the recent evolution in EU + EMU economic governance;
 - (2) Possible results of impending European meetings ← Eurogroup (December 4th, 2018);
 - (3) How Italy is hit by these results → active role to play.

1. Evolution of European governance

- From 5 Presidents' Report (mid-2015) to the election of Macron (mid-2017) = stalemate in EU and EMU's economic governance.
- Second half of 2017 = EC particularly active →
Completing the banking union (October)
Deepening Europe's Economic and Monetary Union (December).

1. Evolution of European governance

- EC + Euro-summit (end 2017):
 - completion of BU (backstop + EDIS) and progress in CMU;
 - stabilization and counter-cyclical tools to manage asymmetric shocks and to improve convergence;
 - creation of a euro-area budget;
 - transformation of ESM into EMF;
 - creation of a European Minister of Economy.

1. Evolution of European governance

- 2018 Euro-summit and Eurogroup meetings (March and June) attested a new stalemate in European economic governance.
- Evidence: Centeno's letter to Tusk (June) →
 - (i) new roadmap for the BU;
 - (ii) indicating possible tools for convergence;
 - (iii) fixing some aspects for the ESM's reform.
- (i) and (ii)-(iii) bring back the debate to: fall 2012 and mid-2017, respectively.

1. Evolution of European governance

- Eurogroup's last meeting (December 2018):
 - (a) ESM as a backstop (revolving credit line by 2020), subject to further risk reduction and with serious problems of implementation;
 - (b) no common view on ESM's instruments for fiscal stabilization and convergence (see *Term sheet on ESM reform*);
 - (c) no actual progress on euro-area budget;
 - (d) significant progress on ESM as decision-maker of an *ex ante* public debt restructuring.

2. Achievements of impending meetings

- (b) – (c) ← contrasting view between EMU's member states (mainly: Northern countries, Germany, and France) → open problem:
 - ESM can offer assistance without triggering a full aid program?
- ESM functions → beyond crisis management:
 - (i) mediation between creditors and member-states (even if voluntary and non-binding);
 - (ii) single-limb CACs for new issuances to prevent holdouts (by 2022).

2. Achievements of impending meetings

- Single-limb CACs = approval of a restructuring
← qualified majority for the whole set of bondholders.
Hence, the approval of a restructuring process on the whole stock of national public debt is easier.
- (i) and (ii) = first steps to endow ESM with the power of settling *ex ante* a (quasi-automatic) public debt restructuring (SDRM).

2. Achievements of impending meetings

- Hence, European Council + Euro-summit (December's meetings):
 - Launch of an inadequate backstop for the 2nd pillar of the BU (by 2020);
 - Approval of single-limb CACs (by 2022) + ESM's mediation role → a 'Trojan horse' to ease the implementation of *ex ante* quasi-automatic debt restructuring.

2. Achievements of impending meetings

- EC = has the power to check the sustainability of MS's balance sheets;
EC + ESM = already have the power to state that a country under a European aid program has an unsustainable public debt (*Agreement*, November 14th, 2018).
- This → *ex post* debt restructuring = unavoidable and efficient.
Single-limb CACs are necessary to limit the veto-power of an organized minority of investors.

3. Italy's recommended position

- ESM's new possible power to state the *ex ante* quasi-automatic debt restructuring → a dramatic change.
- The *ex ante* debt restructuring → perverse incentive schemes, triggering macroeconomic instability.
Hence: in this case, no single-limb CaCs.

3. Italy's recommended position

- Italy would have to remain compliant with European rules and save its reputation for several reasons.
- One of these reasons is, being the EMU's most important 'fragile' country, Italy would have to credibly state that:
 - (a) ESM as a backstop = immediately operative without further risk reduction: a 'vested' component of the BU.

3. Italy's recommended position

- (b) Restructuring of public debts would have to be carried out only *ex post* upon:
- assessment of debt unsustainability by EC and ESM;
 - request of the country in difficulty.

3. Italy's recommended position

(c) No form of *ex ante* quasi-automatism.

(d) Possible related application of any collective action clause would require that restructuring is not *ex ante* but only *ex post*.