

Tommaso Padoa-Schioppa says EU needs "big" bank bailout fund

Interview with Giselda Vagnoni and Gavin Jones

Reuters, 3 octobre 2008

- * Supervision must be reformed, co-ordinated more closely
- * EU budget deficit limits should take back seat during crisis
- * ECB should keep rate policy separate from crisis management

By ROME, Oct 3 (Reuters) - As Europe debates how to handle the growing financial crisis, a former European Central Bank board member and Italian finance minister said it must urgently set up a US-style bail-out fund and unify its supervisory mechanisms.

In an interview with Reuters, Tommaso Padoa-Schioppa said he hoped the leaders of Britain, France, Germany and Italy who meet in Paris on Saturday to discuss the crisis will take bold steps to head off a growing risk of financial contagion in Europe.

"(French) President Sarkozy is to be praised, and I am very hopeful the meeting will constitute the kernel of a European handling of the crisis," he said in the interview conducted late on Thursday.

Padoa-Schioppa, who was Italy's finance minister and head of the International Monetary Fund's steering committee until the fall of Romano Prodi's government in May, said Europe's fragmented regulatory structure made it highly vulnerable.

"Maybe Europe is in better shape than the United States in terms of risk and the structure of the financial system but it is in a much more difficult position in terms of supervision and policy instruments."

He strongly supported the setting up of a European fund to bail out banks in difficulty, a proposal reportedly aired by France but rejected by Germany and also shunned by Padoa-Schioppa's former boss, ECB President Jean-Claude Trichet.

"We have seen injections of capital by the public sector in the United States, Britain and in the Fortis crisis, but we need a system that can respond this way at the European or euro zone level," Padoa-Schioppa said.

"And it must be a European instrument, not a national one, otherwise it will create a scenario of conflict."

He declined to say how much public money should be poured into such a fund -- 3 percent of gross domestic product has been one suggestion -- but said it must be large to be effective.

"To overcome a crisis of confidence requires amounts that will reassure that there is no scarcity of money," he said.

A long-time advocate of fiscal rigour, Padoa-Schioppa said concerns about public finances had now become secondary and suggested that during the crisis the terms of the EU's Stability Pact on budgets could be effectively suspended.

"It would be much more dangerous for any stability, including budget stability, not to take extraordinary action to solve the crisis," he said, adding that Italy, which has the euro zone's largest debt pile, could also find the resources.

STATUS QUO "UNACCEPTABLE, DANGEROUS"

Padoa-Schioppa, who has also served as head of Italy's bourse watchdog, said a single Europe-wide banking supervisor was a desirable medium-term project, but much could be done immediately to improve co-ordination.

Europe's regulators should share key information, new directives should be translated into the same requirements in different countries and decisions should be made on the basis of collective assessments -- all lacking at present.

"The status quo is unacceptable, untenable and dangerous; there is no single rule for European banks," he said, noting the Basel 2 accord translated into completely different requirements in different countries.

"The French supervisor oversees French subsidiaries, the German supervisor oversees German subsidiaries and no-one has the full picture of the major EU-wide banking groups. This supervision is neither 'super' nor 'vision'".

Padoa-Schioppa said the Financial Stability Forum headed by Bank of Italy Governor Mario Draghi had produced some worthy proposals but was not the right venue to propose the reforms he was urging.

"If Europeans want to improve their cooperation that must be decided among Europeans and not in a more global forum like the FSF."

Padoa-Schioppa praised the way the ECB had supplied markets with huge liquidity injections while "holding the line" on monetary policy by not lowering interest rates in the face of high inflation.

This separation of policy was "very wise and probably shouldn't be abandoned," he said.

Trichet said after the ECB left rates on hold at 4.25 percent on Thursday that it had considered a rate cut, leading markets to price in monetary easing as early as next month.

(Editing by Ruth Pitchford)