German Finance Minister Wolfgang Schaeuble said that efforts to raise the euro-area’s financial backstop will succeed in tempering the debt crisis, as he urged Spain to press ahead with plans to reform its labor market.

Schaeuble, speaking in Copenhagen on the eve of a meeting of euro-area finance ministers today, said that governments are poised to agree on a firewall of about 800 billion euros ($1.1 trillion). That sum includes the 500 billion-euro permanent rescue fund plus bailouts already in place for Ireland, Portugal and Greece’s second rescue package, he said.

“We can be optimistic it will work,” Schaeuble said in a speech late yesterday in the Danish capital. He gave no indication of a timeframe for the firewall and neither did he refer to the 240 billion euros that remain in the temporary rescue fund, the European Financial Stability Facility.

European finance ministers gather in Copenhagen seeking to strike a balance between meeting international demands for a more powerful war chest and opposition in donor countries led by Germany to providing additional aid for underperforming economies on Europe’s fringes.

While ministers are nearing an agreement to raise the limit on rescue funds to 940 billion euros until mid-2013, the amount they will be able to deploy immediately to protect Spain and Italy will range between 340 billion euros and 640 billion euros.

**Political Cover**

The plan to temporarily increase the bailout-aid ceiling marks a compromise that gives German officials political cover at home while aiming to attract more outside help, four euro-area aides said.

“Given Germany’s resistance to a permanent increase in the euro zone’s firewall -- it is unwilling to put more taxpayers’ money on the line -- a quantum leap should not be expected,” said Carsten Brzeski, an economist at ING Group NV in Brussels.

An agreement taking shape involves running the 500 billion-euro permanent European Stability Mechanism alongside the 200 billion euros committed by the temporary fund to Greece, Ireland and Portugal, according to a draft statement prepared for the meeting.

Beyond that, the temporary fund’s unused 240 billion euros could be tapped until mid-2013 “in exceptional circumstances following a unanimous decision of euro-area heads of state or government notably in case the ESM capacity would prove insufficient,” according to the draft dated March 23 and obtained by Bloomberg News. Finance ministers may change the draft before issuing a final statement today.

**Spanish ‘Fragility’**

The strengthening of the defenses would come after Chancellor Angela Merkel of Germany, the dominant
power in two years of crisis fighting, this week warned of “fragility” in Portugal and Spain. It would also be
designed to lure the rest of the world into putting more money into the International Monetary Fund’s arsenal.

Schauble, who said that IMF assistance will be similar to the financial help the fund has given over the last
two years, called on countries to seek a balance between deficit reduction and structural reform to regain
“sustainable growth.” He cited Spain, saying it would benefit from “reforming the labor market.”

Spain’s government vowed to stick to its labor overhaul yesterday, defying union leaders who threatened
further unrest after staging the first general strike since Prime Minister Mariano Rajoy took office three months
ago. The government is due to present its budget today, and Rajoy has said the spending plan will be “very
austere” as Spain tries to slash its deficit by a third even as the economy contracts.

Draft Language

The language in the draft prepared for Copenhagen stresses the political hurdles to tapping the unused parts of
the temporary fund, the EFSF. Merkel or any other euro-area government leader could exercise a veto.

In a sign of the political sensitivities, the draft doesn’t spell out the 940 billion-euro figure. It puts the total
capacity at 700 billion euros from mid-2012 to mid-2013 and relegates the possible use of the EFSF’s
remaining 240 billion euros to a footnote. Merkel said March 26 that Germany accepted the 700 billion-euro
limit in the first indication that she was ready to allow an increase in the debt-crisis firewall.

The European Central Bank, which has battled the crisis by buying sovereign bonds and lending more than 1
trillion euros to banks, stepped up the pressure on governments to maximize their emergency aid resources.

‘Significant Increase’

The ECB urges leaders “to quickly agree on a significant increase of the resources of the ESM by combining the
lending capacity” of the two funds, ECB board member Peter Praet said in an article prepared for a seminar in
Copenhagen yesterday.

The increase in the aid ceiling mooted wouldn’t make the entire sum available upfront. It would require a
capital call in an emergency to mobilize the ESM’s entire 500 billion euros before mid-2014.

“The bottom line is that the ‘true’ firewall remains the European Central Bank,” said Thomas Costerg, a
European economist with Standard Chartered Bank in London. The ECB’s 1 trillion for banks is “the magic
number the market wanted to see.” With two rounds of loans committed already, “if the crisis escalates, we
think the ECB will have no other option but to provide another.”

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