Jean-Claude Trichet: Interview with *El País*

Interview with Mr Jean-Claude Trichet, President of the European Central Bank, conducted on 15 May and published on 16 May 2011.

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Question: How would you describe the situation of the euro?

Answer: We are in an economic and monetary union. From my point of view, Monetary Union has worked well: we have delivered price stability – fully in line with our definition of "below, but close to 2% – during the first 12 years of the euro, the euro is a solid and credible currency, and inflation expectations are solidly anchored over a horizon of five or ten years. The Economic Union, for its part, has shown its weaknesses during this global crisis and it has to improve very significantly. All pillars of the Economic Union have to be reinforced: first, we need a strengthened Stability and Growth Pact to ensure a rigorous surveillance of fiscal policies; second, we need a close surveillance of the competitiveness indicators and of the imbalances in the euro area, something that we have been calling for all over these last years, since 2005; third, we need to accelerate the implementation of structural reforms, which is an objective for the economic union (the "27") as a whole, as well as in the euro area (the "17"), in order to elevate the growth potential of European economies.

Q. What's behind the dissatisfaction that seems to be affecting the euro?

A. I think there is criticism of the behaviour of some governments regarding their own economic and fiscal policies, and also on others, because they did not exert appropriately the surveillance on their peers. . But I don't think the criticism concerns the single currency, which is a clear success. I have seen many surveys in different countries showing that citizens are supporting the euro. That is the case in Spain.

Q. Does rising debt indicate that the euro may be at risk?

A. As I said, the euro is a solid and credible currency. The economy of the euro area as a whole is in a better fiscal position than the US or Japan, with a likely deficit of 4.6% this year compared with around twice that figure in the US or Japan. Sovereign debt problems are global, not just a European problem. The paradox is that, while fiscal performance at the consolidated European level is relatively good, we have in the euro area some countries which are clearly in a difficult situation, and that require a major adjustment.

Q. Despite your rejection of a possible restructuring of Greek debt, markets are insisting that that is the only way out.

A. The ECB's position has been clear from the beginning. We have an adjustment plan set by the IMF and the Commission. What we are asking for is that the plan be implemented as strictly as possible, as it was negotiated, with rigorous efforts being made by Greece. The adjustment, engaged by this country is essential for its sustainable, medium term growth, job creation and the stability in the euro area. And there is no other way than the strict application of this adjustment plan.

Q. What can we expect from the summit in Brussels on Monday?

A. The Ecofin and the Eurogroup will have to examine a number of issues, including the programme for Portugal, which has been negotiated by the IMF and the Commission, in liaison with the ECB. The ECB attaches a great importance to the fact that this programme has been approved by various political sensitivities in Portugal.

Q. Has it been ruled out that a country could leave the euro?

A. I already said that I consider this an absurd hypothesis. But let me come back to the euro. If, in 1998, we had been told that for the 12 first years of the euro, we would have a single currency that keeps remarkably its value, with average inflation below 2%, a better result than in any Member State in the past 50 years, many people would probably have said that it was too good to be true. Today it's a reality and these achievements are documented.

Q. Is the standing of the ECB at risk because of the rating cuts for the countries from which you have collateral?

A. We are applying our own rules on the matter and are paying close attention to risk management. It is also useful to bear in mind that we are talking about three economies that account for around 6% of the GDP. The other 94% of the GDP of the EU are in a very different position.

Q. The ECB has embarked on debt purchasing but is doing it intermittently.

A. I've always said we are transparent in the management of this issue. I have no other comment.

Q. But that is a function that is not supposed to be performed by the ECB, it is not part of the mandate. Should another institution take on that task?

A. All these non-standard measures have been decided by the Governing Council to better transmit our monetary policy decisions, in times of financial crisis. It is fully in line with our mandate. These measures, including the full allotment of liquidity at fixed rate, are transitory by nature, as I say regularly in the name of the Governing Council.

Q. Three years after the start of the crisis, where are we now?

A. Since the recovery started in the third quarter of 2009, Europe's economy has experienced often upward revisions to previous projections of real growth. Quarter after quarter, the data has frequently exceeded expectations. This has been particularly evident in the first quarter of this year, with an increase of 0.8% more than projected, and several economies in the euro area with better results, even significantly better than expected. That includes Spain, which is growing a little bit better than anticipated. It is no time for complacency, we have to be very cautious and we do not declare victory, but I think that's encouraging. As for the role of the ECB, we are responsible for issuing the currency for 17 countries and 331 million citizens. That is a huge responsibility and it is normal that sometimes there are countries that go faster and others that go slower. What matters is that it's not always the same ones who go rapidly or slowly because that would be unsustainable. There was a time when Greece and Ireland were growing very rapidly and then it was Germany that was lagging. So it's good that there are now countries, including Germany, which are growing again fast and quickly recovering the ground they lost, while others need to undertake indispensable major adjustments. Again, what counts is that in the euro area as a whole the recovery is confirmed. But let us not be complacent, we have hard work ahead of us.

Q. Oil prices have fallen by more than USD 10 since the ECB decided to raise rates. How do you see price stability at the moment, with raw material prices so volatile?

A. The decline in oil prices is good news: it reduces both the inflationary impact and the depressive effect of high oil prices on the economy. That said, there is a high degree of volatility. The present price level is high; 2.8% in the euro area. We cannot do anything immediately to reduce the price of oil and raw material. We have to ensure that price setters and social partners fully understand that we are there to deliver price stability in the medium term at less than 2%, close to 2%. It would be for them a big mistake to think that the present hump in the CPI inflation signals the level of inflation in the medium term. Because we are there to take decisions that will prevent this. That's why there is an independent central bank – to ensure price stability over the medium term.

Q. Are you seeing excessive wage increases?

A. Let me say something to the people of Spain: we are providing price stability in line with our definition, an average of 1.97% in the first 12 years, we are credible for the future five to ten years, and that has to be accounted for in all decision-making within the euro area. If prices and costs in a particular economy are permanently above that level, with spiralling of nominal inflation and nominal wages, in particular there will be unavoidable losses in competitiveness and less growth and less job creation.

Q. Does that apply to Spain in particular?

A. To all countries, without exception, and of course to Spain also. This is a very important message.

Q. So those involved in wage negotiations should forget about national price data.

A. All price-setters, in particular the social partners, must be conscious that there is a benchmark for the euro area inflation as a whole, which is less than 2%, close to 2%. If the unit labour costs in particular are not in line with the evolution of the euro area as a whole, a loss of competitiveness of the economy will be unavoidable, with its consequences in terms of growth and jobs creation. Again, the worst that could happen in terms of growth, is a cost/price signalling over and above the average of the euro area.

Q. That is the conclusion that many people are drawing about the situation in Spain, do you share it?

A. Some of these phenomena happened in the past undoubtedly. It seems to me now that everybody understands that competitiveness of the productive sector is essential for the economy.

Q. It is doubtful that the citizens of southern Europe understand the rise in rates resulting from the threat of inflation.

A. I think they understand. Because if we were to lose credibility in price stability, then inflation expectations would not be anchored and all medium- and long-term market interest rates in Europe, would rise, driven by those higher inflation expectations. Then we would all, I insist, all without exceptions, be suffering the consequences of a less favourable financial environment and its impact on growth and job creation.

Q. This is very reminiscent of the situation in July 2008. Are you still defending that rise in interest rates?

A. Of course it was an appropriate decision. The collapse of Lehman Brothers came later and we took the right measures to cope with the dramatic crisis. We decided to raise rates to counter an unwelcome increase in inflation expectations. By taking that step we confirmed that we are extremely determined to anchor inflation expectations. It helped us considerably during the crisis in preserving us both from the materialisation of the risk of inflation as well as the materialisation of the risk of deflation – which was a very important element to surmount the crisis.

Q. Jürgen Stark has said that the debt crisis is our own Lehman Brothers.

A. We are experiencing at the global level a second episode of the crisis. After the private-sector crisis we are now seeing tensions in the public sector and amongst sovereign risks. This is a global phenomenon, observed in advanced economies. It's crucial to deal with these tensions correctly, especially in Europe.

Q. Let's turn to Spain. Don't the markets understand the reforms that have been made?

A. From our point of view, there are three key issues: fiscal policy, the financial sector and structural reforms. Spain is moving in these three areas, it has made decisions; it has set goals and has done a lot, and has still work ahead of it. I'd say that this is appreciated by external observers, who believe that the country is going in the right direction. But this is no time for complacency. On the fiscal side, the government has been convincing. That being said, measures have to be followed up and the deficit target of 3% in 2013 is essential for credibility. Regarding the financial sector, there is a huge difference in perception compared with a few months ago, but work has not been finished there yet. As for structural reforms, they are absolutely essential because it is through them that growth potential increases. There are reforms that need to be tackled, especially labour market reform, which is being discussed by the social partners. All this is true for Spain, but also for Europe, which has to push forward bolder structural reforms.

Q. Isn't fiscal orthodoxy, the surge of austerity, condemning Europe to slow growth for a long time?

A. On the contrary, fiscal soundness is essential for confidence, and confidence is the most important ingredient for sustainable growth. Financial soundness and structural reforms are also of essence. But speaking for the past, let me give you two or three figures. In the past 12 years, GDP per capita has grown in Europe at the same pace as in the US, around 1%. In the labour market, despite the years of crisis, the euro area has created around 14 million jobs since the birth of the euro: about 6 million more than in the US. This is again no time for complacency. And nobody can say that we are satisfied when unemployment is still so high.

Q. Is Spain the red line in the EU?

A. Spain in the past has shown a remarkable capacity for innovation, for creativity, growth and job creation. It is a very dynamic country. That makes me optimistic, provided Spain continues to implement very actively and convincingly its programme in three areas already mentioned: fiscal soundness, banks' reshaping, and structural reforms.

Q. And the savings banks are the red line in Spain?

A. In this sense, Spain has three main challenges. As regards the savings banks challenge, a lot of hard work has already been done and should continue to be very actively performed.

Q. Especially after the leaks in Germany, do you think all the European partners, especially the political leaders, are aware of the danger of the current fiscal situation?

A. I appeal to all governments to show a high sense of responsibility, both individually and collectively, and to keep a strong sense of direction.

Q. At first you didn't seem very happy about the IMF involvement in the bailouts. Some were even calling for a European Monetary Fund. Why did you change your point of view?

A. The worst thing would have been benign neglect by the Europeans, which was a big danger at the beginning. Having overcome this temptation, the rescue brought together the conditionality and the financial support from the IMF and the European partners, which was necessary.

Q. On the subject of eurobonds, Europe has no treasury, unlike the United States. Do you think that a step could be taken in that direction?

A. At the present stage of European integration, with the current institutional framework, we consider that a major improvement in governance, particularly in fiscal policy, is absolutely decisive. At this stage we are not in favour of euro bonds.

Q. What is your opinion of Zapatero?

A. It is not for the President of the ECB to judge or give good marks or bad marks to the prime ministers! We are fiercely independent from the executive branches and we are issuing the currency for all the people, all the 17 nations, and political sensitivities.

Q. What about Draghi?

A. The appointment of the President of the ECB is the responsibility of the Heads of State and Government, after having had the advice of the Parliament and the Governing Council of the ECB.

Q. Does he have the right profile?

A. We have a great Governing Council, with very wise and experienced colleagues. And I have to say that Miguel [Fernández Ordóñez], Mario [Draghi] and all others have the right team spirit. And it is this very good team spirit which counts.

Q. What will you do after 31 October?

A. We'll see. I have a very hard job ahead of me. There's no time for complacency in many ways. I still have five and a half month! I will be completely absorbed by my work until the end of October.

Q. In these eight years, what has been the worst moment? May 2010?

A. We have had major challenges from the start. Immediately after my arrival the largest countries in the euro area, Germany, France and Italy, were asking for an easing and even a dismantling of the Stability and Growth Pact. We had to fight that. And there were other big challenges afterwards; the crisis has certainly been one. This is the greatest crisis since the Second World War. It could have been even worse – the worst crisis since First World War – if we had not made the decisions we made. They were times that required a great deal of effort. It has been very rewarding to see the team spirit of the Governing Council and of the staff of the ECB and of the other central banks of the Eurosystem. There have been some intensely challenging moments, during which my greatest satisfaction has been to see a formidable dedication to the euro and to Europe, in serving our 331 million fellow citizens..

Q. What is your legacy?

A. It's not up to me to talk about that.