Mario Draghi: Interview in *Kathimerini*

Interview with Mr Mario Draghi, President of the European Central Bank, in *Kathimerini*, conducted by Alexis Papahelas, published on 11 October 2015.

* * *

How soon can the capital controls be lifted in your view?

The decision to impose capital controls, as well as the one to lift them, lies with the government of Greece. It is quite clear that its decision to put them in place was the result of a series of developments that saw the Greek banking system move into some very difficult terrain, with massive deposit outflows. Savers and depositors had lost their confidence in banks at that time. The bank holiday and the capital controls then decided upon by the Greek government were the only way to stabilise the banking system in the short run and, thus, to protect both depositors and borrowers. By the same token, the Greek government will decide to lift capital controls when it is convinced that confidence has returned.

As you know, there has been a lot of heated debate in Greece because, at some point, the government accused the ECB of imposing the capital controls as some sort of punishment for the policies it was implementing. What would be your response to that?

We face varying criticisms in different countries. Some have said that we were too lenient towards the Greek banking sector; others, that we were too harsh. One could say that this is the price we have to pay for our independence. But the truth is that the ECB is bound by the Treaty on the Functioning of the European Union, which prohibits monetary financing. There was no special treatment in favour of – or discrimination against – Greece. We have always made it clear that emergency liquidity assistance (ELA) could be neither unlimited nor unconditional. It could only be given to solvent banks and against sufficient collateral. As the quality of the collateral posted against ELA deteriorated and deposit withdrawals kept increasing, these limits became relevant. In this context, the capital controls were simply a measure taken by the Greek government in response to the huge deposit outflows caused by a lack of confidence. The focus now needs to be on the future and on normalising the situation in the best and quickest way possible.

Let me ask you a question here, because we know that at some point there was a bit of tension between our prime minister and yourself, especially in that famous meeting in Brussels. Is there still some tension in the air?

Let me be clear: the ECB is not driven by political considerations. It is the central bank of the 19 countries of the euro area, including Greece. Furthermore, the ECB cannot breach Article 123 of the Treaty, which prohibits monetary financing. May I also remind you that, at the time in question, the prospects for the Greek economy were quickly deteriorating. Since then, many things have taken a turn for the better in a very short period of time, and we have to give credit to the Greek prime minister, to the Greek government and really to the Greek people for that.

As you know, we have an important challenge ahead of us, namely the recapitalisation of the banks. One thing remains unclear to us and that is whether this is tied to the completion of the review.

The Eurogroup statement of 14 August is clear about the timeline and conditions for the recapitalisation of the banks. A first tranche of EUR 10 billion for possible bank recapitalisation and resolution needs has already been made available. A second tranche of up to an additional EUR 15 billion can be made available after the first review and no later than 15 November, subject to the completion of the planned Asset Quality Review and stress test and the implementation of the financial sector deliverables of the review.

Are you optimistic that the private sector and private funding will be able to participate in the recapitalisation, given what still overshadows Greece?

Private investors have participated in the last two recapitalisation rounds of the Greek banks. Whether this will also be the case in the upcoming exercise depends on the results of the comprehensive assessment and on the terms of the recapitalisation. We will soon have a better picture of banks' capital needs and of how private sector participation can be accommodated in the recapitalisation process. Obviously, the participation of private sector agents would be desirable from the point of view of minimising the use of public funds here. Private investors will certainly be more willing to commit funds to the Greek banking sector if they can be assured of successful programme implementation. Rapid progress towards the conclusion of the first review will contribute to this and is therefore in everyone's interest. Consequently, it is important that the government does its part by implementing the measures required for the first review. Together with the other institutions, we are making every effort to support the government in these efforts and to ensure a timely conclusion of the first review.

Greek banks currently seem to be operating like "zombies". Do you think this will change after the recapitalisation?

The key aim of the recapitalisation is to enable these banks to function normally and to be in a position to support the economic recovery in Greece by providing credit and other financial services. Robust capital and liquidity positions are necessary conditions for achieving this objective, which is why the process of bank recapitalisation and its smooth implementation are so important. Given that the upcoming recapitalisation will involve significant amounts of public money, it is critical that banks are controlled by highly professional boards complying with state-of-the-art governance standards. This will also ensure that the state funds used for recapitalising banks can be recouped via privatisation. Having said this, further measures are needed for banks to remain sustainable in the longer term. In particular, banks will have to intensify their efforts to resolve the high levels of bad or so-called non-performing loans and the relevant authorities will need to remove the remaining obstacles hampering progress in this area. Naturally, some other conditions are also important, for example, the lifting of capital controls and the country's renewed access to international financial markets. We are talking about a series of positive steps, including structural reforms, which are required for Greece to resume a path of sustainable growth and higher employment.

Is a bail-in of depositors completely off the table?

The ECB insisted that a bail-in of depositors should be excluded, as it deemed any such measure to be counterproductive for the economic recovery and harmful for the Greek economy. It would have had a very negative impact on the private sector. The Eurogroup accepted our viewpoint. It is essential that the Greek authorities move ahead swiftly with the implementation of the agreed financial sector measures so that the recapitalisation exercise can still be finalised this year. Its completion will be an important step in the effort to restore depositor and market confidence in Greek banks.

The prime minister, and also some ministers, have talked of trying to renegotiate part of the programme. Is there any scope for this or is this a move that could backfire?

The memorandum, which was supported by the Greek parliament, was agreed with the authorities in August. I believe it is in the interest of everyone that the focus should now be on quickly implementing the measures that were jointly agreed, in line with the set timeline. In other words, the key pillars and objectives of the programme must not be put into doubt. It is thus significant that the Greek prime minister said to the parliament last week that he intends to implement the bail-out agreement with no delays and to conclude the review successfully. The Greek government should show that it has taken ownership of the various programme deliverables and is determined to achieve them.

With the benefit of hindsight, how close were we to a "Grexit"? Is this scenario now off the table for good?

You know, I have been asked this question so many times, in press conferences, in the Eurogroup and in the European Council. My answer has invariably been that the ECB has always acted on the assumption that the current members of the European Monetary Union will stay members, Greece being one of them. It is not for the ECB to decide which country can be a member of the euro area. The ECB has acted and will continue to act on that basis.

Is it completely off the table though?

As far as the ECB is concerned, it was never on the table. I think we have demonstrated that consistently in the past, no matter what others have said or were said to have been saying.

Is debt relief important for Greece and, if so, when should it come?

Well, I believe that two elements will be important in the coming months. The first is the one that I have just mentioned: strong ownership of the programme and determination in its implementation. The second one is debt sustainability. We have expressed concerns about current debt sustainability. In our view, there will have to be an element of debt relief. However, debt relief would not be credible if it is not accompanied by the first element. It is crucial that the government, as well as the people, identify with the objectives of the programme, which are to bring back growth, fiscal and financial stability and social fairness to the Greek economy. For the government to present itself as being forced to do something by external powers would be self-defeating, as the people of Greece who are supposed to make some of the short-term sacrifices will then ask their government "Why?" – "Why should we do this, if you yourself are not convinced?" Incidentally, this has been a long-standing challenge regarding programmes that have been designed and negotiated with international institutions. So, I would like to reiterate that ownership is important. Ownership and compliance will give credibility to debt relief, especially given the economic developments of the last ten to 12 months.

Wouldn't it have made sense to have had this kind of debt relief at the beginning of the programme or when the primary surplus was achieved?

There are two answers to this. First – and I have been asked this question in respect of other programme countries that have faced similar situations in the past – it is very difficult to look at a reality that existed four, five or six years ago with today's eyes. At the time in question, circumstances were very different: for example, there was no crisis management framework, there was no banking union and the ECB shields were not in place. Second, until a year ago, the rate of growth of the Greek economy was such that debt sustainability was not completely out of the question. Since then, things have changed; some for the better and some for the worse – including the policy slippages and the resulting deterioration in the country's economic outlook.

How can Greece return to growth? Can we compare Greece with Ireland?

Greece will return to a growth path if it undertakes all of the structural reforms that have been discussed. I think that is the key point. When we speak of structural reforms, we are referring to a change in the structure of the economy that will make it more competitive. And more competitive does not necessarily mean just in terms of exports. It means that people who want to open up a new business should be free to do so, and without any problems. It means much greater competition in the product and services markets. It means perhaps a more flexible, more open and more competitive labour market. In a sense, that is the message from countries like Spain and Ireland. Both countries have shown that, with the right reforms, it is possible for the economy to bounce back rapidly. So the bottom line is: yes, it is doable.

So, do you think that Greece could return to growth in 2016?

Remember that, in 2014, growth was positive and that, in the first half of 2015, the Greek economy showed strong resilience to worsening business sentiment. This was partly a result of robust growth in the tourism sector and partly because of one-off factors. For 2015 as a whole, the outlook is less favourable and more uncertain. But I am quite confident that, if there is strong commitment to the programme, which aims at ensuring economic growth, fiscal sustainability and financial stability while safeguarding social fairness, there is a good chance that this could happen.

Some people think that this programme is not sustainable because there is an element of overtaxation of the private sector. Are you worried about that – that people will not be able to pay their taxes again?

Achieving a sustainable, strong recovery requires fiscal sustainability, in a growth-friendly manner. This should come through reductions in unproductive government spending and through shifting the tax burden away from labour to taxes which are less detrimental to growth, such as those on consumption or property. That is what both the theory and evidence suggest. Indeed, the fiscal consolidation strategy foreseen in the third programme relies heavily on measures which are less detrimental to growth, such as a reform of the country's valued added tax system and a reduction in military spending and subsidies. An important issue is how Greece will cope with curbing tax evasion. In this regard, property taxes (if designed not to be regressive, for example, they exclude low-income housing) are more equitable, also because they are more difficult to evade. In contrast, taxes on labour should be reduced. This is where incentives should be allowed to play freely. In other words, people should be able to find jobs and entrepreneurs should be able to hire people. Well-designed taxes can actually support employment, particularly youth employment. This would, in turn, have a positive effect on confidence and therefore on consumption and investment.

The Governor of the Bank of Greece has been the target of many political attacks in the last few months. Were you worried about the independence of the Bank of Greece at any point?

Well, we have had similar situations in other parts of the euro area. As a member of the Eurosystem, the Bank of Greece must be independent from any political influence and pressure, and its actions should not be guided by political considerations. In this regard, Yannis Stournaras has managed to protect the authority, the independence and the status of his institution amid very challenging conditions. My understanding is that there is now smooth cooperation between the Greek authorities and the Bank of Greece on several issues of mutual interest.

Did you feel at any point that, as regards Greece, the political leaders handed you a hot potato?

No. However, what the whole experience shows is that our Union is still imperfect and needs to become a "more perfect union", to borrow a phrase from the constitutional tradition in the United States. A union where the central bank is called upon by certain politicians to decide on the membership of certain states cannot be right. The central bank should just do the work of a central bank, i.e. maintain price stability over the medium term, and should not be called upon to take such decisions. That is why we have to move towards greater political integration. Certainly, we have been criticised for making allegedly political decisions. Those on one side say that we should have cut ELA to the Greek banking sector much earlier – not only frozen, but cut it, and cut it to zero – and those on the other side say that we should have extended ELA further, unconditionally, even if that would be a violation of the Treaty. All in all, given these extreme criticisms, I think we have acted in an independent and balanced way.

Do you think any mistakes were made in terms of how Greece was handled during the last few years?

Well, I can only speak for the ECB and, obviously, I am a biased observer. The very nature of any crisis is that you are working under intense pressure to come up with a solution. What I can say with confidence is that the ECB has always acted within its mandate and outside of politics.

And what's your main message for the Greek government right now? It is a very critical moment – we have just had an election and the review lies ahead.

My message is one of hope and determination. Greece has been through a very rough period in which the economic and living conditions of the Greek people have worsened considerably. The cost for the country, the economy and society alike, has been high. But recently, with enormous determination, the Greek people and the Greek government have re-established political and economic stability. My message is: build on this and do not let a sense of desperation take over again. Fight to maintain the stability that you have rebuilt at great cost, and very soon you will see the benefits. That is the message I want to send and, frankly, the message that I would listen to, if I were in that situation.

Let me ask you now about non-Greek issues. There is also discussion, as you know, about the debt crisis and at some point there was a real fear that it was going to hit Spain, Italy and France. Does that still worry you, or do you think that it is completely off the table and, if so, why?

Over the past few years, several euro area countries have taken important steps to improve the sustainability of public finances and the resilience of their economies to adverse shocks. Market sentiment has normalised, also in response to the strong resolve shown by euro area governments to put the euro project on a more solid foundation. Looking ahead, however, it is important that, at the national level, countries continue to pursue sound economic and fiscal policies, and that, at the supranational level, integration continues to make progress.

Are you satisfied with the results of quantitative easing (QE), or do you think that you overestimated its impact?

We are satisfied with QE, as it has met and even surpassed our initial expectations. Both the financial markets and the banking sector are giving indications that QE is working. Actually, this was first seen in the financial markets. Interest rates at all maturities went down to historically low levels. QE has had a favourable impact on the cost and availability of credit for firms and households. The volume of credit is now expanding, and what is interesting is that it is also expanding in the so-called stressed countries. The overall cost of lending by banks to the private sector has decreased by something like 80 basis points since we announced the measures, and by much more for the "stressed countries". The spreads between large enterprises and small and medium-sized enterprises (SMEs) lending costs have also gone down, which is an important element.

Finally, let me add that, in some of our regular surveys (e.g. the bank lending survey), banks' responses indicate that lending is positive and that the macro risk and the lack of liquidity which were previously deterring lending are no longer a prime concern. Also, in other surveys, fewer and fewer SMEs report that credit has been a limiting factor for their business. The number has substantially diminished and now, for the first time since 2009, those SMEs that signal an improvement in the availability of bank loans outnumber those that see a deterioration, and by a wide margin. In most countries, we are currently seeing the return of growth and higher employment. This recovery is primarily led by consumption, supported by the lower oil prices and by our monetary policy.

There seems to be a "theological debate" regarding austerity and a fear of inflation, as you know. What's your position on this?

If we look at any measure of inflation, we see that it takes quite an effort to raise inflation expectations and actual inflation to the levels that are consistent with our objective of "below, but close to 2%" in the medium term. In March, when we started purchasing assets at a pace of EUR 60 billion per month, we were forecasting that inflation would be back to 1.8% by 2017. Now, largely because of the lower oil prices, but also because the global growth outlook has weakened, these projections have been revised downwards to 1.7% by 2017. Therefore, it presently appears that it will take somewhat longer than previously anticipated for inflation to come back to, and stabilise around, levels that we consider sufficiently close to 2%.

And, finally, let me ask you about the refugee crisis. In your opinion, what will be its impact on Europe?

The human tragedy of this crisis demands that we all participate actively in responding to it. The sheer scale of what is happening will change Europe forever. Indifference or hostility to change are not options. Our elected leaders are already working on a common response. As we have seen repeatedly over the financial crisis, agreement on major issues of significance can take time and patience, and is sometimes difficult to achieve in an acute situation. The generous response by some citizens in some countries, such as Germany, could be an example for others. As Europeans, we should – and I think we will – be able to find the necessary resources to deal with this challenge together.