# Mario Draghi: Participation of the President in the Portuguese Council of State

Introductory remarks by Mr Mario Draghi, President of the European Central Bank, at the Portuguese Council of State, Lisbon, 7 April 2016.

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President of the Republic,

President of the Assembly of the Republic,

Prime Minister,

President of the Constitutional Court,

Honourable Members of the Council of State,

I am grateful for the opportunity to discuss with you today the state of the euro area and the changes that still lie ahead of us and I would like to thank the President of the Republic for inviting me.

On my way here I passed by the Tejo river and the tower of Belém. The place where five centuries ago the first maritime explorers set sail for often uncharted waters, looking for new opportunities.

Portugal and its people have also been going through uncharted waters and facing important challenges in recent years, as has the rest of Europe. During the past couple of years, economic headwinds have swept through Portugal and the euro area at large. However, we are seeing signs of recovery.

Nevertheless, important challenges remain as the euro area continues to be weighed down by low potential growth and high structural unemployment. In my remarks today, I will consider the state of the euro area recovery, the role of monetary policy and finally the steps needed to strengthen the euro area and the EU.

### The state of the euro area

The euro area recovery is currently proceeding at a moderate pace. It is supported by our monetary policy measures and their impact on financial market conditions, as well as by the low price of energy. Yet, investment across the continent remains weak, as heightened uncertainties about the global economy and broader geopolitical risks are weighing on investor sentiment.

The recovery is also taking hold in Portugal: its economy is currently growing at the same pace as the euro area as a whole and unemployment is on a clear downward trend.

Yet, the signs of the euro area and Portuguese economic recovery should not be an indication that we can rest on our laurels. The euro area as a whole only just managed last year to return to the levels of economic activity seen before the crisis and some countries, among them Portugal, are still not there. And our economies are still marked by significant vulnerabilities which need to be swiftly addressed. One key issue in this respect is youth unemployment, as it prevents young people from playing a full and meaningful part in society. Indeed, despite being the best-educated generation ever, today's young are paying a high price for the crisis. In Portugal, still now, around one-third of the young workforce is without job. This seriously harms the economy, because these people who are willing but unable to work are being prevented from developing their skills. To avoid creating a "lost generation" we need to act quickly.

Issues such as this illustrate clearly that the current economic recovery needs to be further supported by policymakers taking decisive action. In this respect, all actors need to play their role and European institutions must do so as well by delivering on the objectives that have been assigned to them as part of their mandates.

The ECB did not hesitate to act in this regard. To preserve price stability, we have adopted an accommodative monetary policy stance without precedent and the ECB has and will continue to do whatever is needed to comply with its mandate. We have solid evidence that the monetary policy measures that we have taken since mid-2014 are being effective in delivering their intended impact. We are finding that our policy measures have been instrumental in providing better financing conditions and addressing financial fragmentation across euro area countries. From May 2014 to February 2016, interest rates on loans declined significantly inside the euro area, when considering the average: by 92 basis points for non-financial corporations and by 72 basis points for households. The effect has been even stronger in Portugal, with bank lending rates for non-financial firms falling by nearly 200 basis points over the same horizon. For households rates came down by 125 basis points. The improved funding conditions for both firms and households are supporting the current recovery, facilitating job creation and affecting the inflation outlook.

However, our decisions have also helped to maintain trust in the single currency in times of financial instability and high uncertainty, as, among others, public confidence shows. According to Eurobarometer data, trust in the euro is virtually unchanged compared to its pre-crisis level. While doubts increased in Portugal at the beginning of the crisis, we even see a solid strengthening of trust in our common currency in the last couple of years, again suggesting that our monetary policy measures have been effective.

The measures we announced on 10 March 2016 will further contribute to achieving our aim of price stability. Of course, it will take time for these latest measures to start working their way through the economy and delivering their full benefits. Nevertheless, they constitute a substantial package which gives priority to loans for households and businesses, thus further supporting economic activity in the euro area. They underline our determination to fulfil the mandate entrusted to us, namely to bring inflation back to below, but close to, 2%. These measures also show we have no shortage of tools available.

However, the ECB cannot single-handedly create the conditions for a sustainable recovery in growth. Our policies can support a cyclical recovery, but they cannot by themselves remove structural impediments to growth. This requires a concerted effort in terms of economic and fiscal policies. In many countries of the euro area, current fiscal space to support growth is limited. We should avoid the fiscal rules being stretched to a point where they lose credibility. In the case of Portugal, we welcome the fact that the Commission found that the 2016 draft budgetary plan was not in particularly serious non-compliance with the provisions of the Stability and Growth Pact. And we welcome the commitments of the Portuguese authorities to prepare additional measures which could be implemented when needed to ensure compliance.

There is however scope for all countries to step up the efforts to make the composition of their tax structure and spending more growth-friendly and, among other things, to redirect public spending towards investment, research and education.

Regarding economic policies, without the active role of national governments and parliaments to steadily improve the competitiveness of the euro area economy, we will not be able to raise potential growth and reduce structural unemployment. And I would add that the conditions in recent years were never as supportive as they are today for jump-starting structural reforms that ease the way firms do business, improve productivity and lay the foundations for a more sustainable recovery.

All Member States of the euro area have already been working hard to reform their economies in the past few years. Portugal's reform efforts were in this regard both remarkable and necessary. We now see clear signs that these remarkable efforts are paying off here and elsewhere. Just to name a few examples: buoyant employment growth since 2014 suggests that labour market reforms are making the economy more adaptable. The improved conditions for doing business or the reduced port operating costs are two out of a long list of measures which have enhanced the competitiveness of this country. Moreover, educational reforms are bearing fruit as well, with the rate of early school leavers having almost halved since 2009. However, all reforms take time to yield results. This is true for Member States across the Union, large and small.

There is no case for unravelling past reforms. In addition to upholding past achievements, further reform efforts are needed across the euro area, as outlined in the 2015 country-specific recommendations, which each year identify key objectives in tackling remaining vulnerabilities and rigidities. It is only through such reforms that we can avoid a build-up of new imbalances and bring growth rates back to levels that ensure prosperity and allow households and Member States to grow out of their debt.

Improving the functioning of the labour market remains key in this respect, with a view to ensuring a rapid adaptation to shocks or structural change. This area remains an important challenge in Portugal, as also mentioned in the 2015 country-specific recommendations. Taking further action is all the more important, with high unemployment, according to the latest Eurobarometer, being considered the main concern to the people of Portugal. But we also need reforms that encourage firms to invest. Investment raises both supply tomorrow and demand today. Such reforms include measures that further improve the business environment. However, investment could also be helped by addressing the corporate debt overhang. For instance, increasing the efficiency of debt restructuring tools could disburden still viable companies and thereby facilitate their investment plans.

The European Semester, in which these country-specific recommendations have been issued, should be a good framework to push for such a new effort. However, the country-specific reform recommendations, as just indicated by the Commission, have so far hardly or not at all been acted upon by Member States. Stepping up the reform momentum is therefore essential. In this respect, I have noted with great interest that you will be discussing the National Reform Programme later today. Indeed, greater ownership not only by national governments, but also by parliaments and bodies such as this one would be crucial for the European Semester to gain more traction and yield better results.

**Making economic and monetary union work in the long run**

These are efforts that should be undertaken by countries individually. But there is also work to be done collectively. Most importantly, governments should work towards completing Economic and Monetary Union (EMU). EMU remains an incomplete construction. And while steps have been taken to strengthen the economic governance framework and to make our financial markets safer, this incompleteness amplified the effects of policy mistakes in the run-up to the crisis and continues to leave EMU fragile and its Member States vulnerable to shocks.

In principle, we know where the weak spots in our construction are. The Five Presidents' Report provides a road map on how to correct them by way of risk reduction *and* risk sharing, both as regards the financial sector and as regards economic and fiscal policies.

It is now up to political leaders to fill this road map with life. I am aware that at the moment much of the political attention lies elsewhere. But we should not forget that a stable and sound economy is a vital precondition to be able to tackle challenges in all other policy areas; therefore, making EMU function in the long run is not a luxury – it is a necessity for Europe to flourish.

Thank you for your attention; I am now looking forward to our debate.