

Mario Draghi: Interview in *Die Zeit*

Interview with Mr Mario Draghi, President of the European Central Bank, in *Die Zeit*, conducted by Mr Giovanni di Lorenzo on 17 December 2014, published on 15 January 2015.

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You have a clear-cut reputation. Luca di Montezemolo, the former CEO of FIAT and Ferrari who attended the same school as you in Rome, said that you were always the most competent and serious one – Mario, the prize pupil.

He exaggerates. I've never regarded myself as the best. Most certainly not. I went to school because I was sent there.

But you may have felt the burden of responsibility more than others: you lost your father at the age of fifteen, and your mother passed away only a little later. You were suddenly a very young head of family.

I can remember when, as a 16-year-old, I came back from holidays at the sea with a friend. He went home and could do what he liked. I, by contrast, was confronted with a stack of letters that I had to deal with, bills that had to be paid. But young people do not reflect on what they have to deal with and how they should do so. They simply get on with it. That is important, that is what prevents them from becoming depressed even in adverse circumstances.

They perhaps also understand at an early stage what they must do to survive, for example, work hard.

Belief in hard work was something that my parents taught us. My father used to say that work is the most important element in any person's life.

That sounds very much like a German virtue.

There are lots of people who work hard everywhere in the world. But possibly he might have been influenced by his knowledge of German culture. His German was almost as good as his Italian. In the 1930s, while responsible for the financing of energy projects at the Institute for Industrial Reconstruction (IRI), he travelled a great deal to Germany to see what was being done there in this field. In fact it was not uncommon at that time – he was born in 1895 and married late, aged 52 – even for middle class families to be educated with the sense of belonging to a European culture that would extend beyond the national borders.

What else did he leave you?

The importance of following your convictions with consistent action and with courage if need be. He once told me that there was a monument in a city square in Germany with an inscription that read more or less as follows: if you have lost money, you have lost nothing, for you can get it back with a good business deal. If you have lost your honour, you have lost much, but you can regain it through a heroic deed. If you have lost courage, however, you have lost everything.

You were born in 1947. Were you ever tempted to join the protest movement of 1968?

I had sympathy for some of issues raised, I shared the critical stance towards a culture that we regarded at the time as obsolete, but I was a marginal participant to the protest movement. Typical of that generation was a mixture of criticism and self-confidence, given that the world was experiencing growth...

...there were many opportunities available to you...

... Indeed. I can remember that most of my university classmates and I got many job offers after graduation. They were forwarded to us directly from the university secretariat. At the

same time, we were angry that our institutions, our universities and our country were unable to function better, to address inequalities, to satisfy our desire for change.

Did you sympathise with any political grouping?

No. My convictions were along what you would call today ideas of liberal socialism, not really suited for extremist groups.

No open rebellion, no long hair?

My hair was quite long, but not very long. And, that aside, I did not have parents whom I might have rebelled against.

People close to you say that the period that really shaped Mario Draghi was that as from 1971, the five years he spent in the United States. Is that so?

That is correct. You asked me earlier whether there was a specific moment when I realised what work meant. Well, in the United States, I learnt what hard work is and how much there is to do.

Namely?

Initially I was admitted at MIT as a special student, that is on a temporary basis. To become a regular student, I had to convince my professors I was worth keeping. There I learned that incentives can work wonders. My scholarship covered the rental costs and tuition fees for only the first two years. I had to work to pay for everything else. Fortunately MIT helped by giving its students teaching assignments and paying for them. Later, when my daughter was born, I got a job with a computer company some 40 miles from Boston. The typical day was made up of attending classes, studying for exams and later writing the dissertation, fulfilling teaching assignments and working at the computer company. It was not impossible but it was a very long day, sometimes as long as 18 hours. That would have taught anybody what hard work is.

Looking back, this institute has become something of a legend. You studied together with Paul Krugman, a subsequent winner of the Nobel Prize, and Ben Bernanke, President of the US central bank until early 2014. And then there are the renowned professors ...

... I once counted them – there are five Nobel laureates among my professors: Paul Samuelson, Bob Solow ...

... who also supervised your doctoral thesis ...

... yes, as well as Franco Modigliani, and then there are Peter Diamond and Bob Engle.

Were you aware of the fact that you were part of an elite group?

Oh yes. MIT accepted only very few students, 20 to 25 per year. But it was a very special elite, one in which you had to earn a place every day.

Would you say that you also gained something of an American mindset there?

Of course such an intense and extraordinary experience leaves a legacy that helped to forge my personality today – as a true European.

But what was it like at the time?

Well, during those years I felt like I was maturing professionally in a very open environment, one in which you are assessed in terms of your capabilities – a place where you are what you do.

Thus nobody ever asked about your origins.

Nobody, and in the United States, that, generally, remains the case to this day.

Did you ever feel homesick?

I certainly did miss Italy a little, but the 1970s were not really pleasant in my country. There was terrorism, an inflation rate that reached 20% ...

Didn't that inflation erode what your father left as inheritance?

What we inherited was not very large, but enough for his three children to study. The first time I returned to Italy in 1976 I found that the equivalent of a few hundred euros was all that remained of our inheritance. This was because the family court judge had instructed the guardian of my two younger siblings to invest the money in fixed-interest Treasury bills. And that made all the money disappear into thin air.

So you should actually understand why people in Germany are so afraid of inflation.

That is precisely the point: in Germany, some people say of me – ah, that Italian, he is sure to fuel inflation in the German economy! And I explain to them that their experience of inflation dates back to the 1920s, while mine is far more recent. Those were difficult years. When we returned to Italy we went to Trento because it was there that I found my first university teaching post.

Trento was a political hotspot at the time, a stronghold of the extreme left.

It certainly was a very left wing university, to the extent that a small number of students from there later became violent terrorists. I was supposed to teach students how a capitalist economy works, which was what I learned at MIT.

How did you do that?

Certainly it was not easy but for a teacher it was also rewarding.

Did those students of sociology ever protest against you?

No, but there is a story in this context that is quite amusing. I held a seminar on a text written, I believe, by Paul Samuelson, on capitalism, and explaining some of the differences to Marxist economics. When the time for the exams approached, students came to me with the following suggestion: "Professor, we want to take a group examination." I asked them what that was. I didn't have a clue, given that I had been in the United States for years. "Well, it works like this," they told me, "You ask us a question and one of us will answer it for the whole group." So I looked at them and said, "Okay, we'll do it like this: if that student answers the question correctly, the whole group will pass the examination. But if he can't, the whole group fails." The student who was asked did not come up with the correct answer, so the whole group failed. The same thing then happened a few more times, with the group involved becoming smaller each time and the students finally deciding to sit the examinations as individuals.

When you explained the capitalist system to your students, you presumably tried to highlight the advantages that this system has, and probably did so out of conviction ...

... yes, indeed!

Has this conviction diminished over the past years and decades?

I share a view of society in which individual incentives are regarded as important and rules are deemed to be indispensable for a proper functioning of markets. That is my cultural background, so to speak, and my views on these issues have never changed.

What has proved to be most disappointing to you about the capitalist system since your student days?

Well, quite a number of issues can be mentioned in this respect. One of the disappointments is the latest financial crisis.

The crisis of 2008?

Yes, indeed. And then there is, how shall I put it, that predatory instability ...

What do you understand by predatory?

You know the saying “the winner takes it all.” I do not regard that as being always right and proper especially in environments where social mobility is limited – often the winners who take it all are the same people. Beyond any ethical consideration, this is bound to generate instability.

And the 2008 crisis what does the former Goldman Sachs top manager say: couldn't the experts have predicted it?

Yes, pretty much, though of course neither precisely nor in its devastating extent. It could have been foreseen a few years before it happened, and it was foreseen by some economists like Bob Shiller, the 2013 Nobel Prize Winner, or Ragu Rajan, the current governor of the Reserve Bank of India. The protagonists themselves knew that things couldn't go on like they were. The financial sector overshot the mark. There was a reduction in the quality of loans, just think of subprime lending in the US, in standards, checks, oversight of lending – there were enough signs. Furthermore, in the early 2000s several rules which certainly would have been helpful in mitigating the crisis were revoked. Since then, a lot has been done to reinforce those rules and regulations.

Do you sometimes think that you are the public person that in Germany is the least understood?

I think that's true...

Whose fault is this lack of understanding: Germany's or Mario Draghi's?

My position is actually quite simple: we have the mandate to guarantee price stability. The ECB was established in the tradition of the Bundesbank. But there is a big difference, as the ECB is not responsible for just one country, but 19. The instruments that it has to fulfil this mandate are different. That is, I would say, the message that some in Germany must understand. The mandate hasn't changed, but time and circumstances have. That's important. And yes, you are probably right: some people do not want to understand me on that.

People here in Germany wonder how the countries that have not budgeted well and have for decades failed to reform can be rewarded with loans and low interest rates. And are thus getting the countries that have worked hard and made sacrifices to pay for it?

It's not true. So far, thanks also to the strict monitoring by the governments of these hard-working countries, they have not paid much if anything. But also the European institutions played a role. The ECB has thus far not made any losses and each year, it distributes billions in profits to its members and among them to the Bundesbank, which passes these profits on to the Ministry of Finance, and so to the people of Germany. What is more, they benefit from the fact that public and private credit are unusually cheap. And consider also the TARGET 2 balances ...

... i.e. the claims and liabilities that the national central banks in the euro area have vis-à-vis the European Central Bank and which indicate the extent to which lending via the ECB is being taken up ...

... and which some people claim is money for which Germans would be liable in the event of losses. People who make much of this argument forget to say that these TARGET 2 balances have fallen by half since July 2012. What does this mean? It means that less is being borrowed from the central bank, it means that confidence is growing in the system. Private money is coming into circulation again, and it is being invested in other countries.

The lesson is clear. Anything that strengthens confidence in the euro is also beneficial for the German tax payer.

But the most pain is caused by the low interest rates, which you said in Handelsblatt two weeks ago will stay low.

One must make a distinction here: there are interest rates that we set with our monetary policy, and there are interest rates on long-term securities set by the markets. The latter are more directly relevant for savers. The fact that our key policy rates are low and expected to stay low for quite some time surely has an impact on long-term interest rates. But there are two more fundamental reasons why those rates are low: first, because the whole world and above all the euro area is bringing its money to Germany and investing it in these securities so interest rates fall. Germany acts as a safe haven in times of crisis. As confidence returns, this should be less the case. And second, because expected inflation and the long-term growth forecast for the economy are both unfortunately very low. As our policy brings back inflation to close to 2% and growth picks up, more normal levels of interest rates will return.

This explanation lets the ECB off the hook.

Draghi: Let me be clear: central bank policy is not about punishing German savers, and it is not about rewarding weak countries. The European Central Bank's mandate is to achieve an inflation rate of just below 2% for the euro area as a whole. To fulfil that at this time, it must keep interest rates low and must work towards an expansionary monetary policy which accompanies growth. That's the point, not punishment or rewards. But sometimes it is hard to explain this to everyone in Germany, including in discussions with some politicians...

What are they saying to you?

They say: in that way you are removing their incentive to push through reforms.

And isn't that true? Italy and France are two examples.

Our job is not and cannot consist of taking on the reform tasks of individual governments – not least since we lack the democratic mandate to do so. Do you believe then that it would be better for German savers if we tried to raise interest rates?

If you put it that way, the answer is obvious.

The answer is no!

Why?

Because we would then create deflation and recession. Anybody can see that the current economic situation calls for an expansionary monetary policy. If monetary policy was restrictive, even more companies would go bankrupt. And then long-term interest rates – the interest rates that affect the savings of Germans and other Europeans – would fall further.

But when the interest rate is near to zero and you want inflation at 2%, then this will consume even more of the assets that Germans want to save for their old age.

But this reasoning is wrong! If inflation were to rise, we would have to raise rates again.

Why do we need inflation anyway, even if it is very low?

Yes, why? We've learnt this lesson from Japan. In Japan there wasn't this 2% objective, and in the 1990s prices began to fall. The problem was not that prices were falling, but that people thought that they would never rise again, they would keep falling further and further. So they stopped buying things, because they thought they could get them even more cheaply at a later date. Production fell, so prices fell even further, and so the economy became slower and slower. We are not in that situation, yet.

That's what we call deflation.

Yes, what I described is a negative deflationary spiral. The only thing that counters this is the credibility of our inflation objective – the attainment of which requires the continuation of our expansionary monetary policy.

But you have already given us this expansionary monetary policy!

Our expansionary monetary policy has already contributed to a turnaround in the growth of loans to firms. But that is not enough. If firms don't increase productivity, they will not be competitive.

That means that countries and firms must introduce reforms.

Right! Productivity must increase particularly in the so-called southern countries. There even before the crisis, many companies were no longer productive partly because they had not invested in new technology, partly because the countries as a whole were no longer competitive. For many years easy credit conditions allowed them to import from the rest of the euro area while increasing their debt, both public and private. The crisis made it clear that growth is sustainable only if it is not accompanied by unsustainable debt levels. When this condition is not satisfied brief periods of growth are followed by deep recessions, as the recent history of the U.S. and of some euro area countries shows. That is why our expansionary monetary policy must be accompanied by higher productivity. Those countries need to make structural reforms to make investment profitable. I have been saying this for years now: We are pulling our weight but the governments also have to do their bit.

Are you telling me that is where your sphere of influence stops?

Exactly, we can only provide access to funding, we can only remove one of the obstacles, and nothing else.

So we now have credit with an interest rate close to zero. In addition to that, we now have the unbelievable blessing of falling oil prices that many countries are enjoying, which is not down to you though. Despite all this, the crisis countries are only making slow progress, if at all. Do you not sometimes have your own doubts as to whether your measures are truly working?

You see, the falling oil prices are a good thing but to the extent that they have a negative impact on people's inflation expectations not a good thing at all. The danger is that people may start believing that we will not go back to an inflation rate of 2% very soon, not even in five years and this by itself would have a recessionary effect. Shall I show you what the expectations' curve for the inflation rate looks like? It is actually astonishing.

Yes, please do.

Look at this (he holds out a piece of paper): The average annual inflation rate expected during the course of the following year used to stand at around 1.77% in the past; in 2013 it stood at 1.08% and now it is only 0.37%.

In Germany?

In Europe. Now, the figures for the future five-year period. In the past, the average inflation expected for the next five years was 2.31% and today it stands at 1.68%. Looking at a ten-year period, it stood at 2.09% in the past and today it stands at 1.15%. That's how it goes!

And what does this mean, do you think?

It means that the risk of deflation is still low but it is definitely higher than it was a year ago.

You are more concerned about deflation than inflation then?

Both are undesirable. But from a central banker's perspective, inflation is easier to tackle than deflation. Why? When there is inflation, you raise the interest rates. In this way, the price of money increases, the volume of cash in the economy shrinks and the pressure on

prices and wages recedes. With deflation it is harder. We are now in a situation in which we should reduce the interest rate further, but that is no longer possible. At this point, we need to take recourse to unconventional measures, meaning we need to change the size and the composition of the European Central Bank's balance sheet

Are you talking about the thousand billion that you want to spend over the next few years, predominantly by purchasing government bonds, and which is to be decided upon at the ECB over the next week.

I never said "thousand", but as guidance, I mentioned the balance sheet size of the European Central Bank at the beginning of 2012.

There is huge criticism in Germany of the large-scale purchase of government bonds, also from political parties. Is it the worst response that you have had thus far as President of the central bank?

Possibly the three months after my speech in London were similar. (*What is meant is Draghi's commitment at an investors' conference in July 2012, in which he said that he would "do whatever it takes" within the mandate in order to keep the euro, which led to a lot of protest in Germany.*)

And what do you think, will the majority be in favour of your plan?

All members of the Governing Council of the ECB are fully committed to comply with our mandate. Of course there are differences on how it should be done, but it isn't as if we had an endless number of options.

Germany is the biggest lender of all the euro area countries, whilst Italy and the United States are amongst those countries in the world with the largest debt. Is that the reason for the differences, for the completely different opinions on monetary policy?

It is a complex question better answered in an essay rather than in an interview. There are many reasons for these differences. Some of them are cultural and find their roots in the different histories of economic thought. Part of the explanation resides in the spectacular success that the Bundesbank's monetary policy had in the 70s. And another main reason is that such policy is the perfect complement to the fiscal discipline and the culture based on stability which are an integral part of the socio-economic foundations of this country.

Many Germans fear, in particular, that the debtor countries will be unable to redeem their loans. The options available in such cases are indeed frightening: state bankruptcy, the national central banks continue to print money, loans are prolonged in perpetuity, debt that we are burdening future generations with...

In our currency union, such fears and the ensuing pressure are actually a further stimulus for debtor countries to undertake the structural reforms needed for growth and eventually pay back their loans. But be it should be clear that a break-up of the Union would not be in the interest of Germany.

Which law states that all countries must remain in the euro area at any price? Is there really "no alternative", as Angela Merkel claims?

"No alternative"?

That has become a dictum in Germany: in the discussions on whether to help Greece or not, Ms Merkel said that she had "no alternative" but to save the euro. This remark also then gave rise to the name of the "Alternative für Deutschland" movement.

Our countries wanted the euro as a fundamental step of a process that should lead to greater and more significant unity in Europe. The euro is irreversible.

What would be so bad about Greece, a country where so many don't want the euro, simply exiting? Would the EU not be able to cope with that quite well?

Please understand that I would not like to comment as any statement could be used politically. To speculate about possible outcomes at this stage is pointless.

That is less of an economic reasoning, and more of a political reasoning.

It is both political and economic reasoning. You are asking me why I consider the euro to be irreversible? It is part of the Treaty. But, just imagine what would happen if the euro were to disappear, which was already a matter of speculation in 2012. If all countries were to start devaluing, prices would no longer be stable. Would the countries where complaints about reforms and fiscal consolidation are the loudest be better off exiting the euro area? They would still have to continue with their reforms! You cannot simply keep on devaluing a currency forever: It would simply lead to higher prices.

You are considered in this country as someone who has a particular understanding of southern Europe. Do you sometimes find yourself having to defend Germany to the Italians?

There is an equally large, equally irrational prejudice towards Germany as there is in Germany towards Italy. It is the task of all of us, of all the European citizens to fight these prejudices and to behave so as not justify them.

The prejudice is that Germany wants to bring Europe to heel?

In Italy, but for this matter this happens in many other countries in the euro area, there is often a failure to understand that, within a currency union our policy decisions affect the other members, and we can no longer behave as though we were alone in the world.

So what are you trying to explain to the Italians and other southern Europeans?

We have given ourselves some common rules. They must be respected. If the rules are not respected, there is no trust. And without trust, people call into question the foundations for the common currency.

Are you offended by the charge of being an agent of the southern countries?

Yes.

Have you come to accept this label? What are you doing to counter it?

I don't accept any labels, but I present facts. We are responsible for price stability. We are not there to provide advantages for one country or another, or even to punish German savers. I keep saying this, but ...

... the message is difficult to get across?

I can but quote Paul Krugman: "*When faith meets evidence, evidence doesn't stand a chance*". This is everything other than helpful. The simplification of the discussion you see in many places is in fact just simplistic and leads to wrong conclusions. A great German economist, Rudi Dornbusch, used to say: "*Complicated questions have easy, wrong, answers.*"

Would you describe Angela Merkel as a friend?

"Friend" is not the right word in this context but I have a good working relationship with her as with other European leaders.

Are you constantly in contact with her?

Draghi: Insofar as this is compatible with the ECB's independence.

Finance Minister Schäuble has said that cheap money should not be allowed to dent the reform zeal.

I am pretty confident that we will manage to do what has to be done within the limits of our mandate.

What about the reports speculating that you could become Italian President? Maybe this speculation has also to do with the reports that you are not so happy to be in Frankfurt. Your predecessor, Jean-Claude Trichet, was almost always here and took care personally of every detail.

Frankfurt has become the best site one can imagine from which to run the monetary policy for 19 countries, and now with the establishment of the single supervisory mechanism, can well be named the monetary and financial policy centre of Europe. The members of the ECB's Executive Board are responsible for the areas of competence that I have assigned to them. My management style is based on delegation but also on control which I do both personally and collegially with the Executive Board. I find that works well.

At any rate, people say that you are in Italy as much as possible, or somewhere else ...

I like to go to Italy, when the work in Frankfurt is done, and I must go everywhere else where my presence is needed. The ECB, as the name says, is a European institution, and it is the second largest central bank in the world. You cannot lead it solely out of Frankfurt. But the nickname "Mr Somewhere Else" has pursued me for 20 years!

Since your time at the Italian Treasury?

Yes, I had a thousand things to do. Sometimes people tried to find me and could not so. They said: "Draghi is never there, he's somewhere else!"

What is actually so bad about being touted as the President of Italy?

I do not wish to support any – I repeat, *any* – speculation of that nature. It is of course a great honour to be mentioned, but it is not my job. What is important is the job I am doing at the moment. I am happy to be able to do this job and I will continue to pursue it.

Do you sometimes have the feeling that you are being used as a scapegoat – by both sides?

If this is the price to be paid for a job well done, I am happy to pay it. But what is certain is that no one in Europe has ever won an election by invoking my name.