

Jean-Claude Trichet: Joint interview with Corriere della Sera, Helsingin Sanomat, De Volkskrant, Diário de Notícias

A joint interview of Mr Jean-Claude Trichet, President of the European Central Bank, conducted on 19 June 2006 by Ms Marika de Feo, Corriere della Sera, Mr Juhana Rossi, Helsingin Sanomat, Mr Olav Velthuis, De Volkskrant, Mr Sergio Anibal, Diário de Notícias, published on 27 June 2006.

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1) Mr Prodi, Mrs Merkel and Mr Chirac think that an alliance between Euronext and Deutsche Boerse, instead of a merger with the New York Stock Exchange, is necessary in order to strengthen financial markets in Europe. Do you agree?

Answer: As you know we have no say and we do not participate in the decision, which has to be prepared by the appropriate boards of directors and shareholders.

2) Why do you prefer the European solution?

Answer: All things being equal, a personal preference coming from me for a European solution would appear natural, wouldn't it? That being said, we are not protectionist, the European economy is and must be an open economy.

3) There seems to be no evidence now of a stronger synchronisation of the 12 euro area economies when it comes to growth.

Answer: As far as the business cycle is concerned, the level of synchronisation has improved over the last 20 years, and recent analysis suggests that this level has never been that high for the euro area economies. Furthermore, dispersion of growth in the euro area is not different from the magnitude of equivalent dispersion between growth in the various States in the United States. So it seems to be characteristic of very large economies. But we have persistent differences in the long-term trend growth and in the growth potential of the various euro area economies, which can be explained by factors such as the level of structural reforms and demographic developments. It is this persistence of trend growth differences which seems to be the characteristic of Europe.

Let me also stress that price stability is not only our primary goal but also a mean to attain sustainable growth and job creation.

4) Is this also true also as far as inflation is concerned?

Answer: We also have a level of dispersion of inflation from country to country which is similar to that seen in the United States. But again it is the persistence of these differences which is the European characteristic. That is the reason why when we observe a) that unit labour costs – which is the major cost parameter for inflation – are augmenting in a country, year after year, and that they are above the average of the euro area, and b) that the level of cost competitiveness of the economy concerned is starting to create difficulties, for instance that the external account is deteriorating vis-à-vis the average of the euro area, then it is time, in our opinion, to take appropriate measures to bring the unit labour costs below the average and catch up on the lost competitiveness.

5) At Governing Council meetings, have you discussed the situation in countries like Portugal and Italy – with high levels of debt and very low growth – or the Netherlands and Finland – with low inflation?

Answer: Just like the Federal Reserve, we have to look at the average of our vast continent. And we are responsible for price stability in the euro area in terms of the average inflation for our 313 million fellow citizens of the euro area. But the countries concerned are responsible for the differential between their country's inflation and the average. And we examine as carefully as possible the evolutions and relationships inside the euro area.

6) Which measures would improve competitiveness in the euro area, and specifically in Italy and Portugal? Maybe, for instance, cuts in labour and/or administrative costs?

Answer: It is important, not only for Italy and Portugal, but for all economies of the euro area, to have a good understanding and a very attentive examination of the evolution of their own cost competitiveness, of their labour costs including their labour productivity progress, in order to be able to take if and where necessary the appropriate measures to regain lost competitiveness if there is a documented loss of it. Structural reforms are equally of the essence to foster competitiveness.

7) How do you permit unit labour costs to move at a speed which will make it possible to catch up on lost competitiveness?

Answer: Labour productivity is certainly decisive. In this domain structural reforms make it possible to extract improvements from new technologies and processes. It is equally important to improve unit labour costs through moderation in nominal wages.

8) The German Chancellor Angela Merkel has dealt with the budget deficit through tax increases. Should other countries follow suit?

Answer: What counts is the final goal, which is the rigorous implementation of the Stability and Growth Pact. If and when it is necessary to redress the situation, it is pure arithmetic that you have first to reduce spending and, if a gap remains, increase tax receipts. We would certainly recommend cutting the level of public spending in economies that have a high level of public spending in proportion to GDP. But we can not rule out the possibility of increasing taxes.

9) Even if it happens at the expense of growth?

Answer: In the opinion of the Governing Council, which includes also Mario Draghi (Banca d'Italia), Nout Wellink (De Nederlandsche Bank), Vitor Constancio (Banco de Portugal) and Erkki Liikanen (Suomen Pankki), sound fiscal policies are not hampering growth but fostering growth. We believe that, if the Stability and Growth Pact is not respected, what we would lose in terms of the confidence of households, entrepreneurs and the economy in general would decrease growth more than the illusory expansive impact of a fiscal deficit.

10) And would you agree with a country, for instance Italy, raising taxes but putting off cutting labour costs?

Answer: We have two different questions there. One is if an economy has lost a certain degree of cost competitiveness and has to regain it. And to regain it at the level of enterprises and of the productive sector, it is decisive to rely upon unit labour costs that would augment less than the average of the euro area in order to regain cost competitiveness. That is the first remark, which is always true in any circumstances. Regardless of whether you have budget problems or not, you have to be sure that you are progressively regaining an appropriate level of cost competitiveness.

11) What about the second question?

Answer: Then you have the second question associated with the budget situation: the goal is very clearly the rigorous implementation of the Stability and Growth Pact. And the way you do it logically is by reducing public spending as a priority and then by increasing taxes if and when needed.

12) Are you concerned that Italy and other countries with difficult deficit and debt positions may put the euro at risk?

Answer: No. The euro is a very solid currency of which we are ourselves the guardians. But good policies at national levels would augment growth, prosperity and job creation.

13) Are you concerned that, now that growth is picking up, some countries have budget deficits exceeding the 3% limit?

Answer: We should not repeat the mistakes of the past, when, even in good periods, insufficient attention was paid to budgetary soundness, and thus a very high price was paid when we were back in a more difficult period in the business cycle. That is the reason why we call for a rigorous implementation of the Pact and encourage the European Commission in its efforts.

14) In the past, you have been quite critical about a lack of compliance with the Stability and Growth Pact. Do you think that these fears still arise?

Answer: We have said very clearly in the past that we would not recommend changing the corrective arm of the Pact. After the unanimous decision of the executive branches to agree on a new wording of the Pact, we said that "we call on the Commission and the governments to implement it rigorously."

15) Recently equity markets in many euro area countries have seen their value diminish by around 10%. How is this phenomenon related to the interest rate hikes? And do you expect this to have an impact on consumer demand?

Answer: I will not comment on the daily ups and downs of the stock markets. That is like looking at the sea and commenting on the waves and the tide. If you consider the picture in the context of a longer

period, then the situation is very different. What we do in the Governing Council is to ensure price stability in the medium and long term, which is also a prerequisite for financial stability.

16) So the influence of future rate hikes might have on equity markets is not a concern at all when you make a decision?

Answer: Price stability is our primary goal as you know and also fosters financial stability.

17) In the last stability report the ECB wrote that hedge funds increasingly present a risk to the stability of the economy. Can you elaborate on that?

Answer: Hedge funds have expanded considerably rapidly in the most recent period of time. When we look at them from the financial stability standpoint, we think it is important to have a full understanding of the main reasons behind this extraordinarily rapid expansion, and to handle appropriately the risks involved with hedge funds. This handling is operated through the counterparties of the hedge funds, namely banks, which are themselves under the surveillance of the banking authorities. It is through this cautious monitoring by the banks of their risks with hedge funds that we expect them to be disciplined. We have to check permanently whether this channel of introducing discipline in the hedge funds is functioning correctly or not. In this respect, we still have a lot of work to do within the ECB and the Eurosystem, and certainly at the global level. As you know, it is also one of the major issues which is examined by the Financial Stability Forum at a global level.

18) To what extent does this risk influence your rate decisions?

Answer: Again, our responsibility is price stability which is itself a precondition for financial stability.

19) Do you expect further regulation of hedge funds to be necessary?

Answer: I think that more work has to be done, but what we do need, directly or indirectly is more transparency. But any decision in this domain has to be made at global level.

20) The Bank for International Settlements (BIS) published its annual report yesterday. In its conclusion, the report says that “it could be that monetary policy should have been tightened more, and earlier”. So basically the BIS is saying that the ECB, together with the other central banks, started its tightening cycle too late and has been too modest with its interest rate hikes. How would you assess this implied criticism of being too accommodative in monetary policy?

Answer: To say that the ECB has been too complacent would be very paradoxical! We resisted a lot of advices, which we were given both by academics and executive branches. In 2004 I had calls during the same week from the heads of three important countries, economically speaking, in Europe, calling for rate decreases. As you know, we did not act on that. We maintained our rates at 2% because we concluded that it was necessary to ensure price stability and be faithful to our mandate.

21) So you are saying that the ECB did not start too late and has not been too modest in its current tightening cycle?

Answer: We certainly resisted a lot of pressures in 2004 and, when we decided to increase rates, we did that very much against a number of advices we were receiving from various circles, as well as from a number of international institutions, such as the OECD and the IMF. We raised rates at the right moment and we took the right decisions without complacency against a lot of advice to the contrary.

22) Moving on to the second part of the analysis by the BIS. The report says that now that the central banks have been too slow to act, continued tightening of monetary policy could harm the economy and could, to quote, “have negative effects on global growth and employment”. Will the ECB do as the BIS suggests and give, to quote, “a more measured monetary response”?

Answer: The BIS is merely reflecting the debate, particularly the academic debate. Ex ante you are called on not to increase rates. Ex post you are reproached for not having done that earlier. So, again, we will continue to do what is necessary. Our responsibility is very clear: to ensure price stability and be credible in ensuring price stability. It is what the Treaty itself and I would add that it is what our 313 million fellow citizens as well as investors and savers in Europe and in the rest of the world are expecting from us.

23) So you are continuously as vigilant as a hawk seeking its prey?

Answer: I leave the responsibility for this metaphor to you. I would say the Governing Council is permanently alert. We have to be. In several speeches I have mentioned the concept of “credible

alertness". It is the mark of our institution to be constantly alert. We, as you might have noted, never pre-commit ourselves unconditionally to any particular course of action, whatever happens. We do what is necessary when it is necessary.

24) Does the unwinding of the global imbalances such as the deficit on the US current account argue for a more measured monetary response?

Answer: The possible disorderly unwinding of global imbalances is calling for all partners concerned to do their homework. And that homework has been very well documented, particularly at the global level, at G7 meetings.

25) What can Europe and the United States do?

Answer: Europe should implement structural reforms to elevate the level of its growth potential. The continent has a lot to gain in doing that, growth, more prosperity and more job creation. The United States has to address its fiscal imbalances and deal with the issue of the low level of savings in the overall US economy, which is a major issue. And it is also true for Japan and the rest of the world: we all have homework to do in order for the global imbalances to unwind in an orderly way. I think we have done a very good job in the past, and we will continue to do so.

26) Has the risk of a disorderly global unwinding increased or decreased?

Answer: There has been and there is an important risk for a number of years. That is absolutely clear. Our working assumption is that there will be an orderly unwinding, because we trust that homework which has to be done will be done. And we call on all partners to be responsible and consistent.

27) One specific imbalance is the housing market bubble. Do you think that the situation has improved or worsened in the last few months?

Answer: It is clear that this is a domain in which there is undoubtedly a lot of diversity in the euro area, as is also the case in the United States. For example, you might have real estate dynamism in Florida, whereas in Massachusetts things are not going that fast. We have to accept that a very vast continental economy might have different features. That being said, at the aggregated level of the euro area it is clear that we have dynamism in outstanding credit for housing, and dynamic price increases in various available real estate figures, which are a cause of tension and that we are monitoring carefully.

28) How is this influencing your monetary policy decisions?

Answer: I have mentioned several times that, in the Governing Council's decision-making, we have paid particular attention to real estate developments and we were impressed by the dynamism of the counterpart of the monetary aggregates which is the financing of housing. This was one among many other elements that we took into consideration when we increased rates.

29) You mentioned the advices that you got from executive branches and the IMF. To follow-up on that, two months ago you were sent a letter by Mr Juncker asking for more contact with the ECB. You have already said in the press conference that there is enough contact. The executive branches kept asking for rate decreases and now they are asking you to pay attention to the euro exchange rate? Do you think that the executive branches pay enough attention and respect to the central bank's independence?

Answer: First, let me tell you that I have great esteem for Jean-Claude Juncker, who has a very important responsibility in chairing the Eurogroup. Second, central bank independence is guaranteed by the Treaty. In that respect, independence is guaranteed more nowadays than it was before under national legislation. I do not see any dispute on that. I trust that because the entire world, Europe and European households know and see that we are independent. We have a very high level of credibility. That, I have to say, explains to a large extent why we are anchoring solidly inflation expectations. I would say the sequence is: independence, which is crystal clear and undisputed, triggers credibility, which in turn triggers the solid anchoring of inflationary expectations and permits us to deliver price stability. That is why we are so profoundly attached to independence.

30) Mr Juncker rebuffed you very strongly last week when he said "I am Mr Euro for my competencies", leaving you saying you are Mr Euro for your competencies. Do we have two Mr Euros in Europe?

Answer: You are not at all quoting him exactly and I do not share your appreciation of what he said. The euro is a currency which is issued by central banks. The Eurogroup is the college of Ministers of

Finance. Presiding over all Ministers of Finance of the euro area is a considerable responsibility. As far as I am concerned, on behalf of the Governing Council, I sign the euro banknotes.

31) But he said that he had responsibility as far as the competence of the finance ministers goes.

Answer: Of course and it is an extremely important responsibility.

32) So we have two Mr Euros?

Answer: No. I have already responded to that question at the last press conference.

33) Is the fact that stock markets heavily adjusted downwards recently a signal that economic growth is not doing well?

Answer: I would say that, on growth, as you know, we in the Governing Council extract from all information and signals that we are receiving what we would call the trend growth as we see it. That trend growth that we are extracting from those signals indicates that we are around potential in the euro area. This analysis was made at the end of 2005. We increased our rates in December 2005 on the basis of our economic and monetary analyses. In the economic analysis, it was clear for us that growth was reaccelerating and going progressively around potential. We maintained this analysis when we had somewhat disappointing information on growth in the last quarter of 2005, which we attributed to short-term volatility on a quarter-on-quarter basis.

34) Did you maintain this sentiment also at the most recent Governing Council meeting in Madrid?

Answer: We maintained this sentiment in Madrid. We consider, again, that all the information we have from both surveys and from all other figures have to be replaced in a medium-term context and that they confirmed that we were around trend potential.

35) Now that Jürgen Stark has taken over from Otmar Issing, the fears of smaller Member States that the larger ones would claim their own seats in the ECB's Executive Board seem to be confirmed. Do you think this fear is justified?

Answer: This is the responsibility of the executive branches. I will ship that back to the Council. What we call for ourselves is full and appropriate implementation of the Treaty, which calls for persons of exceptional quality in the field of monetary and financial matters. And I have to say that my colleagues in the Executive Board are all of exceptional quality as it has been recognised by the European Parliament.

36) In your prepared statement after the last monetary policy decision, you dropped the word "vigilance" in characterising inflation risks. The markets have interpreted this as a signal that interest rates will not be raised in July, but maybe at the beginning or end of August.

Answer: I will stick to what I said on behalf of the Governing Council in the last press conference in Madrid as well as in my hearing at the European Parliament last Wednesday.

37) The Finnish banker Bjorn Wahlroos suggested in an opinion article published in the Financial Times on 6 June that Turkey and other EU candidate countries be allowed to join the single currency. Can you comment on the specific arguments expressed in this article? And in more general terms, has the euro become strong enough to unilaterally replace the national currencies of weak economies, in the same way that the US dollar has replaced the national currency in some poor countries?

Answer: If a particular country wants to unilaterally adopt the euro, it is up to that particular country. It would be the same with the US dollar or any other currency. But the Governing Council of the ECB is not committed; we do not do anything ex ante to facilitate this decision. It is really the responsibility and risk of that particular country. And this country has to realise that this would not be a way to bypass the Maastricht Treaty. If a country is a Member State of the European Union and wants to enter in the euro area then this country has to prove the stability of its national currency through the participation in the Exchange Rate Mechanism II.

38) Could you tell us the individual salaries of the Executive Board members of the ECB?

Answer: The total amount for the Executive Board was EUR 2.1 million in 2005. There are six of us on the Executive Board.

39) Why only the aggregate figure? Why not the individual figures?

Answer: Because a decision has been taken on this by the Executive Board and the Governing Council, and we are sticking to that.

40) Do you think you will at some point publish the minutes of the Council meetings, maybe without the names of the governors?

Answer: It was our decision – and we are very proud of that – to introduce for the first time in the world the display of the “Introductory Statement”, which is an overall diagnosis of the situation as viewed by the Governing Council. It is presented immediately after the monetary policy decision. This was a first. No other central bank had done that before. We also have a press conference, which is proof of our full transparency, which remains exceptional among the major central banks of the world. We consider that what we are producing in the Introductory Statement and in the questions and answers in the press conference delivers immediate transparency. Until now, the Governing Council has not wanted to publish the individual votes of its various members. We consider that we are responsible for the single currency in 12 – and in the immediate future 13 – sovereign states. That leads us to think that what we have to display is the unity of the collège, the unity of the Governing Council, which is characterised by a very strong sense of team spirit. As you know, we all stick to the position which is taken by the Governing Council. We are very committed to the decision taken. I have explained that to the European Parliament and, through you, to the people. I think this is becoming more and more understood.

41) Would you consider in the future publishing the minutes even without the names?

Answer: The publication of the Introductory Statement immediately after the Governing Council gives the information that you are looking for. This is the reason why a priori we don't envisage publishing the minutes.