

## Jean-Claude Trichet: Interview with the *Financial Times*

Interview with Mr Jean-Claude Trichet, President of the European Central Bank, in the *Financial Times*, conducted by Messrs Lionel Barber and Ralph Atkins on 8 September 2010 and published on 10 September 2010.

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***Financial Times:*** After the events of the past few years, are you confident that the euro can survive, and if so, why?

***Jean-Claude Trichet:*** Yes, I am confident, of course! You know how much scepticism there was in the run-up to the setting-up of the euro. The best way to measure how much has been done is to conduct a thought experiment and place ourselves at the beginning of 1998 or, perhaps even more boldly, in 1994, and imagine hearing somebody say the euro would be launched on time in January 1999, that it would start with 11 countries, that very rapidly there would be 16 countries. And that after 11 ½ years, for these 16 countries and more than 330m people, not only would the stability of the euro be in line with our definition of price stability – below but close to 2 per cent – but that the level of price stability would be better than that obtained in the previous 50 years by major currencies before the euro. Over the 11 ½ years, euro area inflation has averaged 1.97 per cent.

That would certainly have been considered much too bold, much too optimistic, perhaps totally unrealistic – but that is what we've been doing. So “yes, sir”, the euro is there. The euro area faces a lot of challenges, as is the case for all major advanced economies. All their central banks have a lot of challenges today, and this is no time for complacency for any of us, but the success of the euro, measured as I just suggested, is obvious.

***Financial Times:*** What would you describe as the main challenges facing the euro today?

***Jean-Claude Trichet:*** I would say that we have all the challenges of major central banks in the advanced world. There is the challenge of coping, in terms of our own responsibility, with the “turbulent episode” in which we find ourselves since three years. We have to cope with the challenge of globalisation. We have to cope with the challenges of science and technology, which is developing so rapidly that it creates for the central bankers a lot of additional challenges, in particular in terms of assessing correctly productivity and the impact of IT on the financial sector. Population ageing is also a big challenge for all central banks.

We have two other challenges that other major central banks do not have. One is the deepening and overall implementation of the single market with a single currency, which has been Europe's ambition since the very beginning. We are the only central bank which is transforming, by virtue of its own activity, the economy under its jurisdiction.

The second challenge is enlargement. We were 11 countries at the beginning. Next January we will be 17, with Estonia joining. This highlights the challenge of permanently strengthening and deepening the governance of the euro area, with new economies coming in.

***Financial Times:*** Before we talk about governance, let me ask you some specific questions about the crisis management measures. How are you going to reduce the dependence of the likes of Greece, Portugal, Spain, Ireland on extra liquidity provided by the ECB?

***Jean-Claude Trichet:*** As you know, the European economy relies very much in terms of financing on commercial banks. So it's not surprising that our own “non-standard measures” concentrate much more on bank refinancing than on intervening in markets, in comparison with the Fed. As markets gradually stabilise, our non-standard measures, which are fully consistent with our mandate and, by construction, temporary in nature, will continue to be

progressively phased out. So we are accompanying the market as it progressively goes back to normal. But, as I said already, it is a process which takes time.

**Financial Times:** Do you have in mind, though, a need to phase out “non-standard” refinancing and do you have a sort of time horizon for this?

**Jean-Claude Trichet:** We of course have to consider all those measures as transitory. They are there to cope with a situation which is abnormal – to help correct those markets that are dysfunctional and thereby help restore a more normal transmission mechanism for our monetary policy.

We have eliminated one-year liquidity, and we have also phased out six-months liquidity. The decisions we took last week take precisely into account, through three fine tuning operations in the last quarter, this progressive phasing out and its impact on liquidity.

**Financial Times:** Where do you think we are in this crisis? It’s a difficult question. I mean, if I’d asked Roosevelt in 1935 he would have had a hard time answering the question too...

**Jean-Claude Trichet:** I guess so, yes. I would say that the correct response is that we are in a situation where central banks in particular, and also other authorities, have to remain alert and have to know that we are in an uncertain universe. We always have to be prepared for new challenges that can not necessarily be foreseen and that might be in some respect unpredictable. We have permanently to be in a state which I call credible alertness.

**Financial Times:** How close did the euro area come to disaster in May?

**Jean-Claude Trichet:** No, I don’t think that the euro area was close to disaster at all – seen from inside. I know how Europe functions. I know how the constellation of authorities functions, at the level of the various nations and at the level of the European institutions,. Seen from the outside, I would say that it’s always difficult for external observers to judge and analyse correctly the capacity of Europe to face up to exceptional difficulties. There is no other model to which we can refer – either in history or in a fully fledged political federation such as the US, and certainly not in comparison with centralised states such as Japan or the UK. But I’m always confident. In May we had additional proof of the capacity of Europe to cope with new challenges.

**Financial Times:** Can you explain why [in May] the ECB changed its mind on government bond purchases? There was a lot of criticism in Germany especially.

**Jean-Claude Trichet:** When I talk of “credible alertness” I really mean it. When we decided on 9 August 2007 that it was appropriate to embark in an unlimited supply of liquidity in our own money market, and we supplied 95 billion euros for 24 hours, that was not a decision that was in the textbooks. We were criticised a little bit at the time, and then, after a while, it was recognised that this decision had been wise and lucid.

So in May this year I would say that we were in a situation where it was considered appropriate by the governing council of the ECB to take the decision, as I said earlier, to help restore a more normal functioning of our own monetary policy transmission mechanism. We had previously purchased covered bonds and we had not excluded intervening in other markets.

**Financial Times:** What lessons do you draw in terms of euro governance from this crisis to date?

**Jean-Claude Trichet:** First of all, we are on the record as having always asked for full and decisive implementation of the governance measures that already exist. We combated very fiercely the position of the heads of government of the three major countries in the euro area when they wanted to weaken formidably the stability and growth pact, back in 2004 and 2005. It was a very, very fierce battle. They wanted to really unravel the pact.

What I would sum up as our position today is very simple. We call for “a quantum leap” in the reinforcement of fiscal surveillance, with, in particular, what I would call the reversal of the

burden of the proof. We have called for the “quasi-automaticity” of procedures and sanctions. We have called for a reinforced independent way of assessing the fiscal situation and we have also called for a quantum leap as regard the surveillance of competitiveness and imbalances in euro area member countries. And, finally, we have called for decisive measures to enhance the quality of statistics.

As regards the methodology, we consider that a change of the treaty would be appropriate, but we accept that this would involve a long or very long procedure at the level of 27 EU countries. That’s why we have called for the maximum use of secondary legislation as a first step, to exploit all the possibilities that secondary legislation can offer to go in the direction of the necessary goals. That’s the idea.

**Financial Times:** And what about temporary suspension of membership or even expulsion of a member that is systematically breaching this...?

**Jean-Claude Trichet:** No, I don’t call for expelling members, but a temporary suspension of voting rights is something that should be explored.

**Financial Times:** In retrospect, shouldn’t Europe have undertaken bank stress test earlier?

**Jean-Claude Trichet:** I think so. The ECB and the Bank of England were very much in favour of this stress test. Of course, we have a very complex institutional environment, involving cooperation in real time among 27 EU capitals. It was really essential to have this exercise undertaken on a unified basis, simultaneously. You know that we particularly welcomed the detailed publication of the results for the 91 banks involved.

**Financial Times:** Are you worried about deflation in Europe?

**Jean-Claude Trichet:** No, I do not see the materialisation of a risk of deflation, or either of inflation, at present. We went through the heat of the crisis without any materialisation of deflationary risks. Our successful and solid anchoring of inflation expectations has protected us, I trust, very well against the materialisation of inflation risks – but also against the materialisation of deflation risks.

**Financial Times:** And what about deflation in the United States, is that different?

**Jean-Claude Trichet:** I fully rely upon the analysis of the Federal Reserve.

**Financial Times:** But how serious do you think is the present weakness of the American economy?

**Jean-Claude Trichet:** I would say, again, that I rely very much upon the Fed’s analysis, which I have to say over the crisis has been wise and pertinent. There was a level of hype at certain moments, when we were getting out of the crisis, which perhaps did not fully reflect the situation of the real economy. And now there is a mood which seems to me too negative. That’s my own personal feeling.

**Financial Times:** Let’s talk about the pace of financial reform, regulation. Why were the reforms as proposed under Basel III watered down?

**Jean-Claude Trichet:** I do not want to prejudge in any respect the upcoming meeting we have on this issue. I will only say that we need the same rules at the global level, a level playing field globally. And now at the global level we have the full participation of the emerging world, which, by the way, is one of the major structural transformations of global governance over the last three years. The G20 has substituted for the G7 as the premier forum for international economic cooperation. We have also profoundly transformed the global governance of central bank cooperation with full ownership by the central banks from emerging economies. That is something which I would call a “silent revolution” in global governance.

One thing is certain – and I’m sure that all my colleagues share this view: We cannot again in the next years be put in a situation where the financial sector is about to collapse in the

advanced economies and at the global level, or a situation in which it is necessary on both sides of the Atlantic, for taxpayers to put approximately 27 per cent of GDP on the table to stabilise the system and avoid a major global depression. We cannot do that twice. The people in our democracies would not accept that.

This is not, of course, to say that the 27 per cent of GDP was spent or lost, but that was the level of additional taxpayer risk that had to be put on the table, on both sides of the Atlantic.

**Financial Times:** You said, when we saw you in December 2008, that the airbags had been taken out of the financial system. This was just after Lehman collapsed. Do you think the airbags are now being put back in the system ?

**Jean-Claude Trichet:** I would say it remains a good metaphor for what we are trying to work out, by consensus, among the G20 countries.

**Financial Times:** You've done a number of jobs which have been at the heart of the construction of the euro, and you've just been through the worst financial crisis in 60 years, where as you say, the financial system almost collapsed. What do you think are the qualities that a central banker needs today?

**Jean-Claude Trichet:** It seems to me that in periods that are marked by turbulence, unexpected events, a high level of uncertainty – and I'm afraid that a large part of the reasons for this are structural – central banks are the institutions that have a mandate for price stability, a sense of direction, a stake in overall stability in a medium and long term perspective. They are independent. They can be precisely those anchors of stability that I would say an economy and society need even more in times that are very demanding and very turbulent. That would perhaps be the best way to sum up the responsibility of central banks.

**Financial Times:** Are you concerned, in the wake of this crisis that there's been any weakening of support for the concept of central bank independence?

**Jean-Claude Trichet:** If I take a global perspective, it seems to me that one of the lessons that has been drawn from the crisis, or taken into account, is that the concept of independent central banks having a stake in stability, and a medium to long term perspective, has been recognised as the right concept.

**Financial Times:** Very soon, you're going to be chairing the new European Systemic Risk Board, which will take an EU view, so you will actually be including the United Kingdom in your work, your daily outlook, I suppose. To what extent do you think the UK should fear or embrace this process?

**Jean-Claude Trichet:** I expect that the cooperation with the UK authorities, particularly with the Bank of England, and for me personally with its governor, will be extraordinarily close. It's a job at the level of the EU 27 where you will need a very close cooperation between Mervyn King and all of us, and I expect that this is the way we are all looking at it.