

## Jean-Claude Trichet: La gouvernance de la zone euro

Speech by Mr Jean-Claude Trichet, President of the European Central Bank, at the Notre Europe Séminaire en Hommage à Tommaso Padoa-Schioppa, in the session “Quel bilan pour l’Union Economique et Monétaire”, Brussels, 4 April 2011.

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Ladies and gentlemen,

Let me begin by thanking Notre Europe and the Egmont Institute for the invitation to this conference today in honour of Tommaso Padoa-Schioppa.

Tommaso was a man of culture, a man of vision and a man of action. I had the privilege, during a great number of years, to work close to him in different positions and then to work with him in the Executive Board of the European Central Bank. In the Executive Board he did marvels, particularly in the area of international relations where his tireless activity permitted many advances, in the domain of payment systems in which he had acquired in Basel the best global expertise, and in the crucial dimension of financial stability where his diagnosis on our global and European institutional weaknesses proved unfortunately to be prophetic.

But, overall, Tommaso was a European, a militant of the European Union’s historical endeavour. And although it is with a heavy heart, it is inspiring to speak on a subject that was so dear to him and so central to his life’s work.

Let me also remind us that I am in the purdah period, and nothing I will say can be interpreted in terms of future monetary policy.

We all know that the Chinese leader Zhou Enlai, when asked in 1971 about the impact of the French revolution, famously replied that it was “too early to tell”.

What Zhou Enlai confirmed in this comment is the difficulty of making assessments of historical processes at a particular point in time. There is always a risk of being too influenced by the circumstances of the present. This can lead to judgments that lack an appropriate, encompassing perspective.

The same remarks apply when assessing EMU at a particular point in time.

To avoid the trap of being over-influenced by the present, a broader framework for assessing EMU is needed. To this end, I would like to draw on a framework put forward by French historian Fernand Braudel.

In his seminal study of the development of social structures in Europe, Braudel identified three levels of time which are necessary to understand historical change. The first level was the *longue durée*: the deep processes over long periods that shape the structures of economy and society. Such a long term perspective is important to assess EMU because a key objective is to further the historic project of European integration.

The second level of time was the *époque*: the trends that define a particular period of history. This medium-term perspective is also relevant because the Treaty has set aims for EMU which are best assessed over the medium-term – most notably ensuring price stability.

The third level was *l’histoire événementielle*: the events of the day that shaped the course of current affairs. This near term perspective is significant because the litmus test of any union is how it responds to unforeseen stresses and challenges – and EMU has experienced just such circumstances together with all advanced economies since 2007.

Such a textured approach may give a more comprehensive picture of Economic and Monetary Union. I will discuss each level in turn.

## The *longue durée*

Let me start with the long-term perspective, the *longue durée*. For Braudel the *longue durée* concerned the slow and subtle effects of deep social and economic changes. It is an important perspective because EMU is part of a historical process to deepen economic integration in Europe, and thereby, as Montesquieu famously argued, to make the countries of Europe “*reciprocally dependent; and their union is founded on mutual necessities.*”

It would be fair to say that this ambitious aim has been achieved. The ideas for the start of a European Community, presented as early as in the speech of Robert Schumann in 1950, for an economic and monetary union laid out in the Werner Report in 1971 and then in the Delors Report in 1988 have become reality. Going further back, a single market with a single currency represents – to various degrees – the fulfillment of the visions of thinkers like Victor Hugo in the 19th century, Immanuel Kant in the 18th century, Hugo Grotius in the 17th century, and Erasmus in the 16th century. EMU has brought economic gains and thereby help lay the foundations for “perpetual peace” in Europe.

This wish for deeper integration is not only a philosophical pretension but also evident in the attitudes of European citizens. Surveys indicate that, on average in euro area countries, more than 80 per cent of euro area citizens are in favour of greater policy coordination between countries to overcome the crisis. This suggests that European integration has led Europe’s citizens to fundamentally reappraise the value of cooperation in difficult times. Economic and Monetary Union constitutes the *avant garde* of this long term historical process.

It is important to keep in mind this long term perspective, looking beyond the ongoing economic and financial challenges in the euro area. EMU is an unprecedented achievement in history of sovereign nations. Euro area countries have voluntarily chosen to share sovereignty for the sake of common goals.

## The “*époque*”

Let me now turn to the *epochal* view. The *epoch* in Braudel’s view is a period of time over which medium term trends can be meaningfully assessed. The medium term for central banks, as regards the definition of price stability, is a duration of several years. Therefore the 12 years since the launch of EMU is an appropriate length of time to allow for a review of whether medium term goals have been met.

As regards Monetary Union the first aim is price stability, the primary mandate of the ECB. The ECB Governing Council has defined price stability as an annual increase in consumer prices of below 2%, but close to 2%, over the medium term. Since the launch of EMU the average annual inflation rate in the euro area has been 1.97%. This is a better performance than any large European economy over the last 50 years. It has also helped the euro establish itself as the second-most important international reserve and transaction currency, trusted by financial markets.

This has been possible because the ECB’s actions were enshrined in a medium-term oriented monetary policy strategy. Our definition of price stability is the needle in our compass and has guided the steady course of monetary policy over the last 12 years.

On a consolidated basis the euro area performed well in terms of growth and employment, also in an international comparison. Adjusted for differences in population growth, per capita GDP growth in the euro area over the last decade has been almost the same as in the United States, at about 1% per year. As regards the dispersion of real GDP growth rates across euro area countries, they are comparable to the equivalent dispersion between the states of the U.S. On employment, the euro area made significant progress as well, with overall employment increasing by 14 million during the first twelve years, compared with a

rise in employment of about 8 million in the United States. And the overall yearly public finance deficit is presently about half of that in the U.S. or in Japan.

However, the crisis has revealed that not all of these gains in all countries were sustainable or balanced. Some euro area countries did not follow rules for the conduct of national economic policies. Between 1999 and 2008 significant fiscal and broader macroeconomic imbalances appeared.

In a stability-orientated economic and monetary union, countries have to keep their fiscal house in order. Fiscal and broader macroeconomic policies have to keep domestic demand in line with rates of sustainable growth and price stability. Otherwise the result will be escalating unit labour costs, increases in public and private debt and losses in competitiveness.

So if I sum up the “*époque*” from the start of the euro until the global crisis, during the first nine years of the euro I would say that we could observe a remarkable success of monetary union as a whole and a much less flattering behaviour of the economic union, both because a number of countries were not respecting individually the rules of the Stability and Growth Pact, and also because all member countries collectively did not exert the surveillance, which was commanded by the Pact.

In that sense, the global crisis, which intensified in 2008, has acted as revelatory. It marks the end of the first “*époque*”.

More than before, from now on it appears absolutely essential that all euro area countries adhere to the ambitious fiscal consolidation plans to which they have committed in front of their peers and restore the confidence of firms, households and investors in the soundness of public finances. Fiscal consolidation is an essential first step on the path back to sustainable and balanced growth in the countries concerned, and ultimately to achieve the objectives of the Treaty and the expectations of European citizens. It is equally essential that all euro area countries create a strong surveillance of their competitiveness indicators and of their imbalances as a second “*pillar*” of their governance.

### **L’histoire événementielle**

Now let me turn to the near-term perspective, *l’histoire événementielle*. For Braudel this period of time concerned “events, politics and people” and how their real time activities shaped the course of history. This is a significant perspective because EMU is a “community of destiny” that is responsible for taking measures to ensure the best interests of its citizens. Thus an assessment of EMU has to take into account how it responds to and manages challenges.

The severe challenges since 2007 and, more particularly, since the intensification of the crisis, in September 2008, have provided EMU, as well as all advanced economies, with the toughest global test since at least 65 years.

EU policy makers have so far responded to these testing times effectively.

The ECB has been fully faithful to its primary mandate, price stability, in deciding on interest rates, its standard policy measures. And, taking into account that the financial crisis was hampering the normal transmission of its monetary policy, it has decided a number of non-standard measures to help restore a more normal function of this transmission.

Member States also took important measures. No systemically important financial institution in the euro area was allowed to fail. All euro area countries undertook ambitious fiscal consolidation. Two stability facilities with a total volume of €500bn were established.

And these achievements have to be set in context. Observers often compare EMU with a unitary state like the U.S. and Japan and expect similar policy responses. Yet EMU remains a union of sovereign states that has its own logic for addressing challenges. This leads to

outcomes that are not always linear. Seen in this light, EMU's response seems all the more impressive.

Indeed, one should not exaggerate the differences, as regards diversity of economic behaviour of member economies, between a full fledged political federation like the US and the Euro area. As I mentioned before, the difference between the fastest and slowest-growing U.S. states is not of a different order of magnitude as that between euro area countries. For instance, between Oklahoma and Nevada there was a 13% difference in growth in 2009; between Slovakia and Ireland the difference, which was the highest that year, was around 9% in 2008. The same is true of employment. In 2009 the largest difference in unemployment in the euro area was between Spain, with 18%, and the Netherlands, with 3.7%; for the U.S. between Michigan, with 13.6%, and North Dakota, with 4.3%.

But, that being said, if a lot has been done in Europe a lot remains to be done in the domain of economic governance. The problems with the economic pillar of EMU that I described above result from weak governance. The solution to these problems involves resolutely strengthening economic union by a major change in its governance. As I said, we need to make a "quantum leap" by both reinforcing the fiscal pillar of governance, which is the Stability and Growth Pact, and by creating a new pillar of governance, namely a strong surveillance of competitiveness indicators and imbalances. There is a third pillar of governance of the Economic Union in the EMU, which is as important for the European Union as a whole as it is for EMU: the structural reforms embedded in the "Europe 2020" strategy. These structural reforms are essential to elevate the growth potential of the single market of Europe as well as of the single market with a single currency.

The Council has recognised the need for stronger rules for fiscal policy and the necessity of a new surveillance framework for macroeconomic imbalances. But in my view, it does not go far enough.

The proposals currently on the table should be strengthened to reach this very significant jump towards closer economic union that is required. The ECB strongly believes that more ambitious reforms are needed for the euro area and it is convinced that the *Triologue* between the Council, the Commission and the Parliament will permit the Parliament to significantly improve the texts that were presented to it.

This is much more than a simple procedural concern. Stronger economic governance is essential to support the fundamental construction of EMU. A union with a centralised monetary policy but decentralised economic policies needs appropriate mechanisms to balance the independence of countries and their economic interdependence.

## Conclusion

It is essential when discussing Economic and Monetary Union to take an appropriately broad view. EMU is a major step in a major long historical process that cannot be judged solely on the basis of passing events, of *l'histoire événementielle*.

That said, how the euro area responds to the challenges of the "époque" it is currently facing together with all other advanced economies, will influence the historical trajectory of Europe. The key question is whether governments can put in place a very significantly reinforced governance of their economic union in order to reap the full benefits of the single currency. This will determine whether the new "époque" which is ahead of us after the crisis is a time of economic and financial stability, of sustained growth and of sustained job creation. It will also be decisive in giving a direction to the historical evolution of Europe in the perspective of the "longue durée".

The historical stakes are important. Either we prove that we are able to find the new strong reinforced governance concept, which will fit with a constellation of sovereign states and

permit the European Union to face up with the new globalised world. Or, we do not convincingly succeed into this direction, and then a new jump in the institutional framework of Europe toward a political federation will appear necessary.

It is often said that Europe has demonstrated the capacity to make progress when it has to draw lessons from its own difficulties. I find this notion in Jean Monnet's remarks, immediately after the conference of the "six" on 23 July 1952, on the E.C.S.C., almost 60 years ago. At the end of Chapter 14 of his mémoires, he writes: "Je dis à François Fontaine: Nous avons quelques heures pour nous reposer, et quelques mois pour réussir. Ensuite... Ensuite – poursuivit Fontaine en souriant, nous rencontrerons de grandes difficultés dont nous nous servirons pour avancer à nouveau. – C'est bien cela, n'est-ce pas ? – C'est cela même. Vous avez tout compris sur l'Europe."

"I told François Fontaine : We have a few hours to rest, and a few months to succeed. Then... Then said a smiling Fontaine, we will meet great difficulties which we will use to advance further. Is it the right way to look at it ? It is exactly the right way. You have understood everything about Europe!"

Tommaso was often mentioning this remark of Jean Monnet when we were discussing together the future of Europe.

More than ever, Europe, coping with the present challenges, needs to demonstrate its sense of direction. This is no time for fatigue. This is no time for complacency.

Thank you for your attention.