

Jean-Claude Trichet: Interview with Helsingin Sanomat and Kauppalehti

Interview with Mr Jean-Claude Trichet, President of the European Central Bank, conducted on 20 April 2011 by Mr Jorma Pöysä (Kauppalehti) and Mr Juhana Rossi (Helsingin Sanomat), published on 26 April 2011.

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Question: As you may know, a populist and euro-hostile party called True Finns won the general election in Finland last weekend, obtaining almost one-fifth of the votes. Are you worried that this anti-euro sentiment will grow in other euro area countries? Could it dampen the willingness of triple A countries to accept new rescue arrangements and therefore slow the gradual recovery from the recession and the debt/banking crisis?

As a central bank we issue a currency for absolutely all political sensitivities. We are the guardian of a public good – a credible and stable currency – and that public good is for the service of all our fellow citizens. We are, by construction, a multi-partisan and multinational institution. I will not comment on the functioning of our democracies. We fully respect the functioning of our democracies in which we have the fortune to live in Europe.

Question: But what is the atmosphere in Europe? Do you think there are worrying phenomena?

In a democracy all opinions are expressed. I have observed that there was always a very strong European drive in Finland, and I am very happy with that. As I said, the euro was created on the basis of a multi-partisan and multinational vision to deepen European construction and to reinforce solidarity between Europeans. Taking into account the historical challenge, which Finland perhaps knows better than other European countries over the last 60 years, it seems to me that all the reasons why the “founding fathers” had this vision of European unity are still there and they are even stronger now. When we look at the changes all over the world, the extraordinary growth of the emerging economies, such as India, China, Brazil, Mexico, Russia, and the remarkable development of Latin America and Africa, we see that European unity is more important than ever.

Question: The level of the ECB’s refinancing rate is still unusually low. Also the non-standard measures are in use, and banks have access to ample liquidity. At the same time global price pressures in energy and food are elevated, and headline inflation exceeds the ECB’s definition of price stability. With this frame of reference, is the Governing Council engaged in very close monitoring of price developments in the euro zone?

As I said after the Governing Council’s last decision, we judged it necessary to increase rates by 0.25 percentage point in order to deliver price stability in the medium term. For us it is extremely important to prevent second-round effects after the “hump” in the headline inflation rate. Some price-setters and social partners might be tempted to view this hump not only as a transitory phenomenon, due to a shock in the price of energy and commodities, but as something more permanent. Such a perception is not acceptable for the ECB’s Governing Council, which is responsible for price stability in the medium term. That is the reason why we increased rates.

We are proud of the fact that during the first 12 years of the euro we have delivered price stability, in line with our definition, namely “below 2%, but close to, 2%”. To be precise, we have delivered an average yearly price increase to our 331 million fellow citizens of 1.97%.

And it is extremely important to continue solidly anchoring inflation expectations in a period which is marked by uncertainties and turbulences.

Question: Do you see second-round effects caused or any signs of second-round effects anywhere in the euro area?

We have risks of second-round effects here and there. We have to be very alert that they do not materialise.

At the moment I do not see any significant materialising of second-round effects and I do not see un-anchoring of inflation expectations. But this is no time for complacency. We have to be permanently alert to avoid the materialisation of such risks.

Question: To what extent is the ECB's freedom of action limited by the poor condition of some of the euro zone banks?

We have to deliver price stability to the whole of the euro area – which means 17 countries and 331 million people – just like the Federal Reserve has to deliver a single monetary policy to all the states of the United States of America, and not one policy for particular states that are growing rapidly and another one for states that are in difficulties. Our mandate is very clear, and it addresses the euro area as a whole.

From the very beginning of the financial turmoil we set up a strict separation principle between our standard measures, namely the interest rate decisions, which are designed to deliver price stability, and the non-standard measures, which are designed to help restore a better transmission of our monetary policy, taking into account the abnormal functioning of some markets.

Question: How is the ECB's room for manoeuvre influenced by the poor condition of public finances in euro zone countries, and especially in the countries with acute crisis?

As I said, we are not compromising on our primary goal of maintaining price stability, and our interest rate decisions are designed to fulfil that aim. Any other approach would be unthinkable. And one should never forget that price stability is a precondition for sustainable growth and job creation.

Question: There are some heavily indebted nations within the euro area, most prominently Greece. Yesterday (Tuesday, 19 April) the news agency Reuters reported that Clemens Fuest, who chairs the German Finance Ministry's Technical Advisory Committee, said Greece's extremely weak balance sheet meant a restructuring of the Greek sovereign debt was inevitable. He said that: "One must recognise the realities – I am expecting a haircut". Do you agree with Mr Fuest and other prominent economists and policy-makers who have expressed similar views?

There is an important adjustment plan which has been adopted by the Greek government to reform its fiscal and structural policies. This plan has been approved by the IMF, by the international community and by the European Commission in liaison with the ECB. This plan is being applied.

Question: How worried should we be about credit rating agency S&P's negative outlook for the AAA rating of US debt? Is there a rising risk of higher long-term interest rates worldwide?

The ECB has always thought and said that it was important for all advanced economies, without exception, in Europe and the rest of the world, to be very keen on the sustainability of their long-term fiscal policies. It is extremely important that the authority of the signatures of the advanced economies is unchallengeable. I personally have full trust in the United States for preserving its creditworthiness and the authority of its signature.

Question: The ECB has postponed its exit from the non-standard measures on several occasions. Can the non-standard measures de facto co-exist with any level of interest rates?

Yes, indeed, the "separation principle" that we apply permits us always to have the right level of interest rates, even when markets are still not functioning perfectly. As I said, we set interest rates at the right level to deliver price stability. This is independent from the decisions

we take regarding the non-standard measures, which have to be commensurate with the situation in the markets and the need for a proper transmission of monetary policy.

You have seen an example this spring. Following the March meeting of the ECB's Governing Council we pre-announced that there was a possibility that the Governing Council would increase interest rates. That was of course a very important message that the Governing Council was sending as regards the "standard measures".

At the same time we decided to maintain the "non-standard measures" for the second quarter of this year, particularly the policy of full allotment and a fixed rate for the supply of liquidity with a duration of three months.

Non-standard measures are temporary by nature. I do not imagine that we would have them permanently, because that would be relevant only in a permanent situation of dysfunctional markets, which is of course not our working assumption.

Question: The ECB began purchasing government bonds from the secondary market (i.e. the Securities Markets Programme or SMP) in May 2010. Is there a limit to the size of this programme?

This is one of the non-standard measures we have taken. I have nothing further to add to what I have already said on that.

Question: When will this programme be terminated?

I have nothing to add.

Question: The yields on the stressed euro area government debt securities in some maturities are now much higher than on several occasions in the past during the SMP. Yet the ECB has not particularly actively purchased securities from the markets during recent weeks and months. Why?

We take the decisions that we consider appropriate in the circumstances.

Question: Do you consider the outgoing president of the Deutsche Bundesbank, Axel Weber, a constructive and discrete member of the Governing Council of the ECB?

Axel Weber has been an important member of the Governing Council and his contribution has been appreciated during the entire period of his membership of the Governing Council.

Question: In a recent interview in the Der Spiegel magazine Mr Weber made the following statement: "There are minutes of meetings of the American Federal Reserve Bank and the Bank of England in which divergent opinions are documented. I think that's exemplary. I had already told my colleagues ahead of time that we weren't with a routine decision, but an important change in direction, and that I could not keep my opinion to myself on such a fundamental issue." Was Mr Weber correct when called the launching of the SMP an "important change in direction" for the ECB?

We are, in the European framework, in a unique situation. We have a single currency, a single monetary policy and a single system of central banks for the euro area, the "Eurosystem", comprising the euro area national central banks and the ECB. We issue the single currency for 17 sovereign nations and for 331 million fellow citizens. That explains why we have features ourselves that are not the same as in a fully-fledged federation. In particular it explains why we have a principle of speaking with one voice.

Question: Why could the majority of the Governing Council accept the decision to launch the SMP, but not Mr Weber? What is your explanation for this divergence of opinions?

I have no comment.

Question: How do you explain the SMP to ordinary citizens who fear that the ECB is engaged in the monetisation of debt and creation of inflation?

As you know, securities are purchased by the Eurosystem in the secondary market, after they have been issued and found a first buyer. And we always withdraw all the liquidity which has been injected with the SMP, so that we do not practise quantitative easing, which has been used in other economies. The SMP is one of the non-standard measures, which are transitory, we deemed necessary in view of the abnormal situation in markets, to help restore a normal transmission of monetary policy. Another example of important non-standard measures was the full allotment at a fixed interest rate for liquidity with a duration of six months, even up to a full year. This programme of liquidity provision with exceptionally long maturities has been phased out. We also had a programme in which we purchased covered bonds. That has also expired.

Question: In your opinion, should an ordinary euro area citizen take a fixed-rate mortgage or a variable rate mortgage? By a variable rate mortgage I mean a bank loan with one of the EURIBORs as its reference rate.

[Laughter] Do not count on me to take the job of the investment advisors. I would only say to my fellow citizens that they can rely on us to be an anchor of stability at the level of the entire euro area. Since the euro was set up we have had challenges within Europe and challenges coming from the outside. Citizens can count on us to deliver price stability in the future as we have done over the past 12 years. This is important in terms of confidence, and confidence is the most precious ingredient for consolidating the economic recovery.

Question: Stable and predictable inflation is one important issue when companies make investment decisions. Recently there has been prominent volatility in headline inflation rates. What is your message to entrepreneurs: how they can trust you to deliver what you have promised?

We delivered price stability over the first 12 years of the euro. The performance was better than what had been achieved in the countries of the euro area over any 12-year period since World War II. That is a remarkable record of price stability. These are deeds, not only words or promises. It is something we have done in the past. In a number of cases, decisions we took were criticised out of short-term considerations. We had the medium and long term in mind. All observers can look at our track record. Inflation expectations are well-anchored for the next five and ten years, based on our credibility. But this is no time for complacency. And this is why we took our last decision on interest rates.

Question: There is a relatively large number of medium-sized saw mills in Finland which are dependent on the export markets. When the euro is strong, they soon lose market share to their Swedish and Russian competitors. This makes them lose money and forces them to put their staff on furlough. What would be your advice to these entrepreneurs?

I would tell them that we have been living in a universe of floating exchange rates between the major currencies for the last 40 years. As regards the relationship between the euro and the US dollar, I will stress the statements made by the United States Secretary of the Treasury and the Chairman of the Federal Reserve: that a strong dollar vis-à-vis other major floating currencies is in the interest of the United States. I entirely share this view. I will also say to all economies in the euro area – and not only to Finland – that keeping a lid on costs, in particular by increasing productivity as much as possible, is essential to be competitive.

Question: The ECB decided recently to suspend the application of the minimum credit rating threshold in the collateral for the debt instruments issued or guaranteed by the Irish government – as you did previously with Greece. Why did you do this? Can the same procedure be applied later possibly to Portuguese debt instruments?

In these two cases the Governing Council of the ECB has taken into account the programmes the governments in these countries have set up with the IMF – namely by the international community – and the European Commission in liaison with the ECB. The

programmes have been approved by the IMF and the European institutions, and they incorporate strict conditionality. We took our decision on the basis of this strict conditionality.

Question: Now markets know that the ECB will accept junk bonds as collateral. Likewise, euro area governments have one incentive less to maintain an investment grade credit rating because they now know that the ECB will accept in an extreme situation their bonds regardless of their quality. Did this softening of collateral requirements set a dangerous precedent?

I repeat: the decision of the Governing Council was made on the basis of very strong conditionality of the international community. No government takes lightly the fact that it has negotiated a programme that implies very strong conditionality with the international community and the European institutions.

Question: Once the sovereign debt crisis has been resolved, it may well take years before Greece and possibly Ireland have regained solid investment grade credit ratings. How is the ECB planning to exit from this softening of collateral requirements?

Again, strong conditionality and strict implementation of the adjustment programme. It is the sine qua non. At the end of the road stands the return to normal financing with market access. That is always the goal.

Question: You have a lot of experience of central banking within the European context. You first led the Banque de France for ten years and now you are approaching the end of your eight-year term at the helm of the ECB. Based on your experiences, what skills and abilities are an absolute must for your successor?

I never comment on my succession. One has to consider what a central bank is. A central bank is an institution that is there to be an anchor for stability and to have a sense of medium and long-term direction. It should not depend on an individual. Jean Monnet said: “*Nothing is possible without individuals; but nothing is lasting without institutions.*” We are an anchor for stability in Europe. What counts is the institution and the team. I have had the fantastic privilege of being part of a fantastic team. I like to use the metaphor of a football team: you have all the players on the field and among them is a captain, which is undoubtedly an inspiring responsibility. What counts is to have a good team spirit, a solid institution and all the wisdom of collegial decision-making.

Question: Is the President of the ECB more of an academic/technocrat or a diplomat/politician? Should the President of the ECB be a career central banker with impeccable academic credentials, such as Athanasios Orphanides of the Central Bank of Cyprus? Or should the President of the ECB have a background in high-level national and European politics and multinational institutions with extensive personal networks, such as Erkki Liikanen of the Bank of Finland?

I have no comment on the decision which will be taken by the heads of state and government. I will only say that, of course, all members of the Governing Council have a solid academic background. That being said, all kinds of experience can be important and useful. And again: what is decisive is the team spirit.

Question: Based on your experience, is central banking more art than science?

Central banks need formidable analytical capacities and skills. You need both state-of-the-art analytical work, as deep and robust as possible, and you need judgement, based on experience and a solid capacity to synthesise all pertinent analyses. That is true in absolutely all circumstances, and particularly in times of crisis.

Question: Professor Barry Eichengreen of the University of California, Berkeley, recently published a book about the US dollar entitled Exorbitant Privilege. In the book Prof. Eichengreen makes the following assessment when he analyses the strengths and weaknesses of the major currencies.

“If a first-class international currency needs a first-class central bank, then this, too, is something the euro possesses. The ECB has shown itself to be extraordinarily serious about the maintenance of price stability. Although it was roundly criticized for its exceptional purchases of government bonds in the spring of 2010, it continues to take its price-stability mandate seriously. It shows absolutely no inclination to embark on reckless inflationary policies.”

First of all, do you agree with this assessment? Secondly, is the perception that the ECB is extraordinarily serious about the maintenance of price stability something that you would like to see as your personal legacy as a central banker?

I did not know that you would quote Barry Eichengreen. But yes, you can see that we consider price stability to be fundamental. It is our primary mandate and we are faithful to our primary mandate. We trust that fulfilling this primary mandate is a precondition for delivering sustainable growth and sustainable job creation. In the first years of the euro a great number of new jobs were created in Europe: around 14 million. That is not to say that we are satisfied. We cannot be complacent in any respect and structural reforms are still necessary to combat unemployment. Let me add that delivering price stability is a strong request we get from all our fellow citizens.

Question: When an economic historian looks back at the economic history of Europe 30 years from now, would you, on a personal level, like to see Jean-Claude Trichet remembered, both as head of the Banque de France and the ECB, as a central banker for whom the most important mandate was the maintenance of price stability?

It is not for me to make a judgement. But to the extent that I was called on to pursue price stability as the primary mandate it goes without saying that I hope I can be remembered for this, together with all my colleagues of the Executive Board and the Governing Council. That has also indeed been the mandate of the Banque de France since 1 January 1994, when the Banque de France became fully independent. It is also what we are asked to do at the ECB, But again, it is not for me to judge. It is for external observers to make the judgement.

Question: Do you have any memories of your visits to Finland or your work within the Eurosystem with your Finnish colleagues?

Already before I was President of the ECB I had a relationship with the Finnish central bank and Finnish society in general. I had a very good professional relationship with Sirkka [Sirkka Hämäläinen, a member of the Executive Board of the ECB from 1998 to 2003]. I have to say it is always moving to be in Finland for many reasons, including the very special situation of Finland after World War II. Finland experienced directly some of the tensions that unfortunately marked the post-war period. I was also close to Matti [Matti Vanhala, the late Governor of the Bank of Finland]; in meetings of the Governing Council we sat next to each other and often exchanged views. I also have a close relationship with Erkki [Erkki Liikanen, the current Governor of the Bank of Finland] for a host of reasons, including that not only do we speak English together but we also speak French together from time to time. He has a wealth of experience and vision. In all my meetings with Finnish people I have always observed that Finland has a culture of soundness and wisdom.

Question: You visited Finland in 2007. You attended a concert in the Pori Jazz Festival and stayed overnight in the Villa Mairea, an architectural masterpiece of Alvar Aalto. What impression did you gain of Finnish nightlife and architecture?

[Laughter] It was not nightlife, it was “day”-life. The jazz was excellent and the festival remarkable. We were lucky to have such exceptional weather and were treated to excellent music.

Question: Your term of office expires at the end of October. Would you like to conclude your career as a central banker with a rate hike in the October monetary policy meeting of the Governing Council?

[Laughter] No comment.

Question: You have a smart phone and a tablet computer on the table in front of you. I take it that you use them actively in your work. How do you find the user experience?

I am absolutely fascinated by the scientific and technological progress we are presently experiencing. I sometimes have the feeling that I am myself in a science fiction novel, because of the new marvels that technology displays every other year. You see new possibilities, but at the same it creates challenges. When you make jumps in science and technology, it transforms society. If I have a message to my own sons and granddaughters, it is: be prepared. We all have a tendency to underestimate the pace of change in our society and in the globally integrated economy.