

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

Interview with Mr Jean-Claude Trichet, President of the European Central Bank, and the Financial Times, conducted by Lionel Barber and Ralph Atkins, London, 12 October 2011.

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### ***Financial Times: What needs to be done to contain and bring the eurozone crisis to a close?***

Jean-Claude Trichet: We have to be lucid, recognising the acuteness of the situation. Noting that there is an interplay between the sovereign risk crisis and the banking sector, and that we have to act both at a global level and at a European level. In such situations being ahead of the curve is of the essence. We have to take the right decisions in reinforcing the balance sheets of the banking sector on the one hand and, on the other hand, doing what is necessary to restore as completely as possible the credibility of the sovereign signature. Europeans have a special responsibility because they are the epicentre of these tensions which are of a global nature.

### ***What do European leaders need to do to restore the credibility of sovereign debt, or government bonds?***

European governments need to be crystal clear they are doing all they can, individually and collectively, to honour their signature. It is what the Heads said on 21 July 2011 in their communiqué: "All other euro area countries solemnly reaffirm their inflexible determination to honour fully their own individual sovereign signature and all their commitments to sustainable fiscal conditions and structural reforms. The euro area Heads of State or Government fully support this determination, as the credibility of all their sovereign signatures is a decisive element for financial stability in the euro area as a whole." This declaration is, in my view, extremely important.

### ***What are the risks in the discussions over Greece?***

The ECB has a clear position. Governments should avoid a credit event and avoid a compulsory solution [on involving the private sector]. We ourselves, in the July 21 [eurozone leaders'] agreement, called for the appropriate enhancement of our own collateral.

### ***So it is absolutely essential to prevent contagion from Greece?***

Yes.

### ***David Cameron in his Financial Times interview talked of having a firewall. How do governments make sure that firewall is credible and that contagion can be prevented?***

They have an instrument, which is the EFSF. The appropriate way of having an appropriate firewall would be to leverage the EFSF capital, which is what is being discussed now by Treasuries.

### ***Some believe that preventing contagion from Greece also requires a clear statement from governments that bond holders of other countries will not suffer haircuts or debt write-downs?***

The Heads of State or Government have said very clearly that Greece is a special case and that, as I just quoted, as regards all other countries they reaffirm their inflexible determination to honour fully their own individual sovereign signature. I would say it was important to avoid any ambiguity in this respect.

### ***Can you explain how you would leverage the EFSF?***

There are various means to do that and I don't want to embark into technicalities because it's really the responsibility of the treasuries. But there are several ways to leverage the EFSF.

***Do you think the ECB's role in providing unlimited liquidity prevented an intensification of the global financial crisis and a depression in Europe?***

I think the governing council of the ECB has demonstrated a capacity to be lucid in diagnosing the gravity of the situation since the start of the crisis in August 2007. So I would certainly echo what you say.

We have had two categories of monetary policy measures in this crisis. One has been the decisions on interest rates – what I would call the standard measures – which are designed to deliver price stability over the medium term and be sure that inflation expectations are solidly anchored.

On the other hand, in periods of abnormal tensions in financial markets, we have helped restored a better transmission of our monetary policy – of our interest rates – by other, non-standard measures.

The most important of our non-standard measures is full allotment at fixed rates, which we used as early as August 2007 and which is now a generalised concept. Other non-standard measures have included intervention in the covered bond market and in treasuries.

After almost 13 years of the euro we have delivered for 332 million fellow citizens 2.0 per cent average annual inflation. This is better than over the past 50 years for the main euro area countries, and we can see from information we extract from financial markets that we are credible to deliver price stability for the next 10 years, in line with our definition.

So this is a level of credibility, after four years of crisis, which demonstrates the effectiveness of our so-called separation principle between the standard measures and the non-standard measures.

As it is obvious, the euro as a currency is credible and solid. The challenges in the euro area are related to fiscal credibility and financial stability.

***What needs to be done today, tomorrow and perhaps in the more distant future to make sure that the governance systems for the eurozone are actually credible and work properly?***

The crisis revealed – like an X-ray picture – the weaknesses of many advanced economies – weaknesses in the US and in Japan as well as in Europe. In Europe it has revealed a big weakness in terms of governance – abnormal behaviour of individual countries and absence of effective surveillance of the policies pursued by the various countries. The ECB called a long time ago not only for a strict respect of the Stability and Growth Pact but also for a surveillance of competitive indicators and imbalances inside the euro area. This new pillar of surveillance is now part of the enhanced governance just decided by the European Parliament and Council.

Because of the hard lessons various countries have learnt during this crisis, I assume they will stick not only to the letter but also to the spirit of this new governance structure. It is of the essence.

Beyond this I think we have to reflect on a treaty change that would permit more than surveillance, with recommendations and appropriate sanctions. When recommendations are not followed and sanctions prove ineffective, European institutions should have the capacity to impose the necessary decisions on a particular country.

***...and this is where your idea of a minister of finance comes in....***

I said in my (Charlemagne award) speech in Aachen that, for the “day after tomorrow”, within the framework of an effective European executive branch, we could have a minister of finance with, in particular, three major responsibilities. He or she would have responsibility for surveillance of fiscal and macro-economic policies – including the capacity to impose decisions when necessary. And as far as the executive branch responsibility is concerned, the minister would be responsible for the financial sector of Europe, so that the financial

sector could be decoupled from the various sovereign signatures in order to have an achieved single market of financial services, including in crisis periods. And the minister would have also the responsibility of representing Europe in international institutions, vis-à-vis the rest of the world.

***Would this just be for the eurozone or for the 27 European Union countries?***

The working assumption of European treaty is that at a certain moment in time, all 27 would be in the euro. But of course the possibility of imposing decisions would not apply outside the euro area – that goes without saying.

***Do you think the appetite for that amount of economic integration is there now in Europe, among the new generation of leaders?***

There are more reasons today for the Europeans to unite in economic, financial and monetary fields than there were at the beginning of the 1950s, at the time of the first speech of Robert Schuman. I really think that the structural transformation of the world, the formidable economic success of the emerging countries, of China, of India, of all emerging Asia, of Latin America, calls for the Europeans to unite very significantly. One of the main lessons of the crisis is precisely that Europe needs more unity. In my opinion, this is not necessarily perceived spontaneously or communicated appropriately to the public, but I think these are truths that are there. This necessity for Europe to unite is recognised more and more in the business sector, by all those who have a direct connection with the rest of the world.

I think we had, recently, several examples of European democracies where it was said it was impossible to take some difficult decisions. But after discussions and due reflection, the decision was finally taken in the direction of reinforcing European unity. We are presently experiencing history in the making in Europe. All what I know makes me think that no leader, no individual and no country will take the responsibility of going backwards. That's the reason why I'm confident in the future of Europe. But it calls for a strong sense of direction and for hard work.

***Even those countries where there are deep political reservations, deep political doubts?***

I'm confident for all countries without any exception.

***How do you respond to those leaders who say "we're elected, we're not going to be pushed around by markets"?***

I think we are proud to live in market economies because they have proved the right way of producing wealth, and all other experiments have proved catastrophic. That said, market economies have to be disciplined. You must have rules. You cannot rely too naively on the spontaneous functioning of markets. Central banks were created when it became apparent that it was necessary from time to time to exert some discipline in the market.

***Was not part of the problem leading up to the current crisis that there was almost an irrational belief in the perfect nature of markets and in, for example, efficient market theory?***

Yes. In this respect I have to say that the immediate lessons drawn from the crash of the dotcom bubble were unfortunate. The idea was that financial markets were extraordinarily resilient – which was plain wrong. I must say, I never shared the view that we were in a world where there was no risk.

That being said, when the first diagnosis was made at a global level with China, India, Brazil, Russia around the table, as well as of course Japan, the US and the Europeans, we didn't challenge the fact that a market economy was the best recipe for producing growth.

***In Germany there's a very strong belief in the market, which is why German conservatives opposed crisis measures taken by the ECB. We've had two resignations by Germans – Axel Weber and Jürgen Stark – from the governing council. If you're talking about further steps towards European integration, are you in danger of losing the Germans?***

First of all, I don't know what "The Germans" means, I don't know what "The English" means, I don't know what "The French" means. We are living in cultures that are very deep, very profound and very complex, obviously, and where fortunately you have a lot of different opinions.

We have a legitimate debate – in Europe as well as in the US and in Japan – about whether the central bank is doing well on this, well on that. The Governing Council of the ECB did all what was necessary to be faithful to its primary mandate and to take into account, in transmitting our decisions on interest rates, that we were in the worst crisis since 66 years, a crisis which was disrupting some markets.

Jürgen Stark has been a very close friend for 18 years. He has worked for Europe for the past 18 years. I have great esteem for Jürgen and all that he has done and is doing.

***If you look back on all the years that you've been involved in European construction, is this the most serious crisis that you've had to deal with?***

I was involved in many crises: the real economy crisis after the first oil shock, the sovereign risk crises of the 1980s, the crisis of the exchange rate mechanism in 1992 and 1993, the Asian crisis in particular. But what we are experiencing presently is bigger and has hit directly in at the heart of the advanced economies. So it is undoubtedly an historical event of the first magnitude, the worst financial crisis since the Second World War. It could have produced a great depression had appropriate decisions not been taken at the appropriate.

***This is also the moment of maximum peril for Europe's most important political and economic project and if this were to fail, it would have the gravest consequences for Europe, never mind the rest of the world?***

All advanced economies are being X-rayed by the present crisis and revealing their skeletons and the weaknesses in their skeletons. It's true for all of us – for Japan, for the US, for Europeans. Europe's skeleton of Europe is weak because the institutional framework is weak.

I would confirm that is a major challenge and that it puts into question the strategy of all major advanced economies, including Europe and its institutional framework. At the same time, I could say, that it has positive aspects, now what are our major weaknesses. We had a period of benign neglect, at the global and European levels which was shared by financial markets, by the mainstream of economic analysis and by executive branches. As regards financial markets, before the crisis, for instance, Greece's government was borrowing at the same interest rate as the German treasury!

***Can we carry on with a situation where every country has to sign up to the slightest change and we can be held hostage, if you like, by a country like Slovakia?***

I think that the complexity of the European decision-making process in a crisis situation that requires for major decisions 17 democratic decisions is obviously one of the weaknesses of the present institutional framework.

***Are you confident that in the end will get a suitable rescue package agreed by European leaders at their meetings over the next two to three weeks?***

All that I know makes me think that it is the clear will of the European governments. I would add that I see nobody taking the responsibility of a failure.

***A lot of people think the ECB should be acting as lender of last resort to governments and that ultimately this crisis could only be resolved when the ECB says “we are the ultimate backstop” Why is the ECB not prepared to be that ultimate backstop?***

I think that the ECB has done all it could to be up to its responsibilities in exceptional circumstances. I explain tirelessly what we have been doing to those who are uneasy with some of the decisions we have taken. Keeping inflexibly our sense of direction – price stability – and being up to the challenges of the worst crisis since 66 years.

The ultimate backstop is, of course, the governments. To do anything that would let government off their own responsibilities would be a recipe for failure.

***Are banks still being irresponsible when it comes to pay and bonuses?***

I think we have a real problem here. It is a question of values. Our democracies do not understand some behaviour. It's a very grave issue for all the democracies in the advanced economies.

***You will be succeeded by a very experienced technocrat and somebody who's also spent years on Europe's construction. But he's Italian and in some quarters, in the press and the media, this is seen as a potential problem. What is your response to that?***

First, nationalities do not count. He is a very knowledgeable true European. And do not forget, he took all the decisions of the Governing Council as member of the college. Our decisions are collegiate decisions. So I have absolutely full confidence in what he will do, together with all our colleagues.

***What do you plan to do after you leave the ECB on October 31?***

I have not reflected yet on what I will do afterwards because I have to say that, even in the three weeks which I still have, there are a lot of things to do – 24 hours a day. I'm sure that I will read much more than I do today. I will certainly continue to meditate on the historical future of Europe and I will give more time to my four granddaughters.