

Erkki Liikanen: Interview in *Süddeutsche Zeitung*

Interview (edited script) with Mr Erkki Liikanen, Governor of the Bank of Finland, in *Süddeutsche Zeitung*, conducted by Mr Markus Zydra and published on 7 February 2015.

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Süddeutsche Zeitung:

Mr Liikanen, why did the ECB Council decide to cut Greek banks off from ECB credit?

Liikanen: Greek banks have a counterparty status with the Eurosystem. In January, we communicated that the collateral waiver based on which the Greek government bonds qualify as eligible collateral to Eurosystem refinancing assumes a successful conclusion of a programme review. This could no longer be assumed. So this was a very logical decision, as we have to follow our rules.

But the ECB kept Greece in the emergency liquidity programme via the Bank of Greece?

Liikanen: Every case will be treated according to ELA rules and procedures. Every bank that receives ELA must be solvent.

The ECB wants to help the euro zone to recover economically. That is why the ECB decided to buy government bonds for 1,1 trillion euro? Many Germans resent the decision. What do you tell them?

Liikanen: This was a decision to deliver on our mandate which is price stability. When inflation and as well as inflation expectations drop clearly below our definition for price stability, and the ECB runs out of traditional monetary policy measures like lowering interest rates, then non-standard measures, such as large scale asset purchases, are needed to maintain our policy target. By the way, the arguments in favor of the decision were also shared by most economists at home.

And you have to do it rather sooner than later because if you get in a deflation spiral, it becomes very difficult to get out. Of course I understand the German discussion. By the way in Finland for example, there is also criticism that we acted too late.

The decision was disputed – not only by the German members. How has this dispute changed the working atmosphere in the Council?

Liikanen: There were different opinions among the members of the Governing Council about the timing. It is a non-standard monetary policy measure, we all agree. The working atmosphere is and has been professional and full of substance. You can justify both, doing it now or buying bonds later, but based among the best information we had, I came to the conclusion that risks for price stability were so high that we needed to act.

Have Jens Weidmann and Sabine Lautenschläger been all too relentless in their criticism?

Liikanen: No, it's been professional. Nobody can claim for not having been heard in the Governing Council. History will tell whether our timing was right. I hope the economy in the euro area will turn for the better.

The Germans admire the Bundesbank. The blueprint in the creation of the ECB was meant to be the Bundesbank – now there seems to be not much left of it.

Liikanen: I admire the Bundesbank too. We all learned the value of monetary policy independence by studying the history of the Bundesbank. That is what the ECB fights for. The spirit is there. When inflation rates were too high, I have been one of the first to support higher interest rates. But if interest rates are close to zero, and we have protracted low inflation and deflationary risks, that requires early action. You have to act while you can.

The Bundesbank thinks the ECB is going too far.

Liikanen: There is a new question for central bankers: If our inflation is too low should you react with the same vigor as when it is too high?

Should you?

Liikanen: I am a hawk in both directions, fighting inflation and preventing deflation. There are people who say zero inflation is fine. I think zero inflation makes the economy vulnerable without any buffers. The ECB objective of below but close to 2 percent in the medium term is safer. We haven't had this kind of a problem before, in the postwar period. Rather, inflation was the problem, and the Bundesbank has a great record there.

Now we talk about the prospect of too low inflation for too long. We have to go far back in history to the 1930's to understand the dangers of deflation. You would not believe how often the history books are being quoted among central bankers in various discussions.

But buying government bonds always has the odor of financing government deficits? Don't you agree?

Liikanen: No, not when we are doing it the way we decided to do it. We only buy bonds on the secondary market, we buy according to the capital keys of the Eurosystem members, we buy maximum 25 percent of each issuance and maximum 33 percent of each issuer's debt. And it is done for monetary policy purposes. If you take all this into account you will see there is not that problem to this respect.

The programme bolsters the creation of a bubble. Investors are forced to buy stocks, since bonds become all too expensive due to the ECB.

Liikanen: That's a fair point. We must monitor the side effects including in the real estate market. In member countries macroprudential tools are in place to combat these risks.

Will the 1,1 trillion programme do the job and bring back growth and inflation?

Liikanen: The programme is scheduled until September 2016. Then we look at the situation. If inflation has not reached the target of close to 2 percent, we will continue our efforts to reach our target.

What do think about the growing power of central banks who seem to rule the world economy?

Liikanen: I think we would be happy to do less in the future, but it was important that we acted in the crisis, we ensured sufficient liquidity in the market and we cut interest rates. That was the lesson learned from the depression of the 1930ties.

The German saver wants higher interest rates.

Liikanen: Well, that is going to take some time. All savers will also benefit from the recovery in the euro area. Stability of the economy is good for all. We have seen how the situation for example in Spain, Ireland and Portugal has improved, we have better budget rules, we have a Single Supervisory mechanism in Europe – all that is good for all in Europe, Germany as well.

When will the ECB exit and drop their emergency measures?

Liikanen: I am a marathon runner. We must keep cool and moving and finish the job. When the time comes, we decide about the exit on the basis of the analysis based on our strategy.