François Villeroy de Galhau: Present challenges for France's central bank

Hearing of Mr François Villeroy de Galhau, Governor of the Bank of France, by the Senate Finance Committee, Paris, 30 March 2016.

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Madam President, General Rapporteur, Senators,

Thank you for receiving me this morning, just a few months after your vote of confidence. I attach great importance to these regular exchanges in order to inform you of matters essential to the Banque de France.

In 2016, the world in general, and Europe in particular, are experiencing a period of uncertainty: uncertainties relating to our security, with the threat of terrorist attacks still real; political uncertainties, with the risk of "Brexit" and the refugee crisis; as well as economic uncertainties, with lower economic growth in emerging economies, including China, and excess market volatility in January and February.

Faced with this turmoil, the Eurosystem, of which the Banque de France is a member, is acting decisively. Its monetary policy is supporting the economy and creating a favourable environment for taking all the other actions necessary to return to strong, sustainable and job-creating growth: France, and Europe, must seize this opportunity to regain confidence.

1. Monetary policy, first of all, is doing its fair share of the work.

The Eurosystem is determined to fight the low inflation that we are facing today and thus underpin economic activity. This is our mandate and we are striving vigorously to achieve it. The new comprehensive package of measures that we adopted on 10 March 2016 reflects two main objectives: first, to return to inflation rates below, but close to, 2% over the medium term. This is not the case at present since inflation stood at –0.2% in the euro area in February, taking account of the sharp decline in oil prices, but it should return to positive territory in the second half of 2016.

The other objective is to bolster the financing of the real economy and to protect it from the pressures related to market volatility. The new series of targeted refinancing operations extension of the asset purchase programme, for its part, will be of particular benefit to large French corporations.

We are convinced that these additional measures will deliver concrete results, as did the successive measures we have implemented since June 2014. The latter have indeed boosted lending to businesses, while lowering the cost of credit, and made a 0.3% contribution to French growth in 2015, or even 0.4% according to INSEE. This represents about 80,000 additional jobs for the economy.

We are therefore consistent in our objective, and ready to act using the right instruments. But we also remain vigilant as to the possible risks that our monetary policy could generate. Today, there are no signs of a financial bubble, but we are ready to act, if necessary, by implementing macroprudential measures, in the framework notably of the Haut conseil de stabilité financière (High Council for Financial Stability – HCSF) that you created via the Banking Act of 2013. For instance, at our eighth meeting held on 15 March 2016, we issued a warning about the office sector in the Paris area.

2. Monetary policy thus contributes greatly to our economy, but it can't do everything.

It cannot be the only game in town. ***It is vital that Europe and France seize this opportunity now***. In France, growth is expected to be both robust and inadequate: Robust, as it should remain in 2016 at least at the 1.2 percent level observed last year. But inadequate, as it will probably linger a little below the euro area average of 1.4–1.5 percent. For growth and employment, three essential actions are necessary: reforms in France; private and public investment; the coordination of economic policies in Europe.

First, in France, orderly and sustained ***reforms*** are needed to rebuild confidence. Keeping our public deficit and our debt under control is a contributing factor: the good figures published on Friday (deficit reduced to 3.5% in 2015) are another reason to strictly respect our European commitments by bringing it below the 3% limit in 2017. We must stick to the reforms that work, in particular the tax credit for competitiveness and investment (CICE) and the Responsibility and Solidarity Pact (RSP), and we need to go further still. The unemployed and youth cannot afford to wait. There are at least four reforms that are a priority, because our neighbours successfully implemented them and they are fully compatible with the European social model that we share: the large-scale development of apprenticeships; simplifications, starting with labour law; the decentralisation of social dialogue to the company level, i.e. as close as possible to the economic and human reality; and lastly, the development of entrepreneurship.

Second, we need to mobilise both public and private ***investment*** in order to take advantage of the exceptional financing conditions created by our monetary policy. To do so, we need to put the Juncker Plan back on the table. The Juncker Plan has yielded results, but they are insufficient. To support the revival of this Plan, I have proposed the creation of a true European "Financing and Investment Union". To achieve this, we must combine the Juncker Plan, the European Commission's plan for a Capital Markets Union, and the Banking Union. The aim is to create synergies in order to achieve three ambitious goals: better channel euro area household savings to productive investment and equity; better pool risks across countries; and thus better finance innovation and the networks our economy needs. This is the direction we should take now.

Lastly, we need to make progress towards an ***economic governance*** of the euro area; in France, we spoke of "economic government". This progress is essential, regardless of whether or not the United Kingdom remains in the European Union; naturally, I would like it to stay in. This is not a purely institutional question; it is not about "more Brussels" but very concretely about more growth and employment. Indeed, economists estimate that the current lack of coordination of national economic policies has cost Europeans between two and five percentage points of GDP since 2011. Naturally, contrary to the case of monetary policy, the aim is not to fully integrate all of our economic policies at the European level, but to achieve a "full coordination" of fiscal and structural policies. For this, we need to have shared economic goals, and a true "collective strategy" for the euro area, in which each country has a role to play to improve everyone's situation. This requires trust, in particular between France and Germany, based on a clear pact: national reforms and (not or) European coordination. This full coordination also rests on the setting up of a strong and legitimate European institution: a euro area Finance Minister backed by a European Treasury system and subject to greater democratic accountability. This Finance Minister would be charged with defining the collective strategy, supervising its decentralised implementation by Member States and managing crisis management tools. Going forward, he/she could also be in charge of a common budget. For the euro area and for the confidence of its citizens, 2016–2017 is the crucial time to act: I had the opportunity to discuss these proposals in greater depth a few days ago, and I hope that our exchange will further this debate.

I will finish with a few words about the ***Banque de France*** itself. When you heard me in September, I presented my view of the three main tasks of the Banque de France: monetary strategy, financial stability, economic service, via its branch network. With the staff of the Banque de France, we firmly believe in these tasks and in their future, and that is why our ambition is to be an exemplary public service, even more efficient, more innovative, and more visible in France and Europe.