Peter Praet: Interview in Die Zeit

Interview with Mr Peter Praet, Member of the Executive Board of the European Central Bank, in Die Zeit, conducted by Ms Lisa Nienhaus and Mr Mark Schieritz on 12 December, and published on 14 December 2016.

*   *   *

Mr Praet, you are a member of the Executive Board of the ECB and thus part of an international elite that is really hated by the new right-wing political movements. Do you feel threatened by that?

Peter Praet: No, but I am worried. As a European institution, we look at how much people trust us. People like the euro, but the latest Eurobarometer survey shows that trust in the European institutions has strongly declined in recent years. This is true for the whole of Europe as well as for national institutions, not only for the ECB. But for us too.

No wonder, when savers no longer get any interest!

That is not the reason. In recent years, i.e. during the period of low interest rates, the approval ratings have not changed significantly. The strong downturn came in 2008 as a result of the financial crisis. That is when trust plummeted. The reasons were, above all, economic. Before 2008 we, and most economists, predicted that the euro area would carry on growing continuously. But then came the recession following the financial crisis and we never reached the predicted economic strength. Shortly afterwards came the sovereign debt crisis, the second recession and the rescue programmes with their cutbacks. So expectations were raised much too high and could not be fulfilled. That is a great disappointment for many people.

So everything is the fault of the financial crisis. The ECB itself has nothing to do with it?

Central banks didn't see the crisis coming at an early stage either. In the years before the financial crisis, credit growth was very high, not only in Europe, benefiting from relatively low interest rates in some countries. We gave several warnings at the time about the excessive liquidity in the markets. When the crisis then erupted, people realised that Europe was not properly prepared for a situation like this.

What was missing?

The toolkit was insufficient to respond to critical developments. There was no common banking supervision, there were no institutions for the stabilisation or resolution of banks, and there were no macroprudential instruments. That increased the effects of the crisis. Central banks have just one instrument to achieve price stability – the interest rate. It is difficult to counter a complex situation with this instrument alone. However, we have made good progress in stabilising the foundations of Monetary Union.

The European elites did that too. But the people are clearly not happy with that. Ultimately, it comes down to the euro, without which there would be no problems. Was the euro itself a mistake?

No. The crisis only illustrated that the euro had been created within an incomplete institutional framework. However, we should not forget what we owe to the euro. Before Monetary Union there were repeated economic shocks owing to strong fluctuations in exchange rates. That created trade barriers. In addition, you must always consider the alternative. Take Germany, for example: without the euro, the currency would have risen very strongly in value during the financial crisis. For a country that exports a lot, that is a problem. I rather doubt that the country would have been better off than it is now – and it is likely that interest rates would have been pushed down very strongly in this case too.

At present everyone is saying that the elites have lived too long in their filter bubbles and did not notice the rise in populism. Does that apply to you too? Do you live in the ECB bubble?

For us, diversity in opinions and views is an important basis for good decisions. On the ECB's Governing Council, we have the 19 governors of the national central banks who are there in a personal capacity and not as representatives of their countries. That enriches the debate and our perspective on the world. And, conversely, they are also able to explain our decisions in their countries. We ourselves regularly go to the European Parliament, and occasionally national parliaments.

For example, Mario Draghi spoke at the German Bundestag a few weeks ago.

And you?

I try to exchange views with different people as often as I can. For example, I've been to events for German small and medium-sized enterprises, and I take part in a lot of panels. Just recently I met the President of the Bavarian building societies, among others, in this way. Both sides learn from such events. The Germans are critical, but they are always polite, I find. Most people understand me better after such events. But usually they still don't think that what we are doing is good.

Do you sometimes meet tough critics? For example, members of Alternative for Germany (AfD), a party that came into being quite specifically as a protest against the euro rescue policy?

We are open to dialogue with our critics. And we also engage in such dialogue on a regular basis, not least in the European Parliament.

At the moment, interest rates are rising all around the world. Only the ECB is resisting the trend and is leaving interest rates low. Are you losing touch?

The picture is not at all as uniform as you describe. In the United States, for example, the economic recovery is far more advanced than in the euro area, unemployment is lower and the rate of inflation is higher. That is why the US economy can cope with higher interest rates. We have not got that far yet.

Why not? Unemployment is falling in Europe too, and there is growth – and the oil price is rising.

It is true that the recovery is firming. However, the speed is still moderate and inflation is still some distance from a sustainable path back to the target value. That is why we have decided to extend our government bond purchase programme until the end of next year. We have, however, reduced the scale of the monthly purchases by €20 billion as of April.

Is that the beginning of the exit from the trillion euro programme?

No. We want to continue the level of monetary policy support that we have been administering to the European economy so far.

So, what would have to happen for you to be prepared to exit?

It would have to be apparent that there was a sustained convergence in the rate of inflation towards our objective of below, but close to, 2% over the medium term.

That can change quickly. In the financial markets it is expected that the US economy will receive a boost because Donald Trump wants to reduce taxes and increase public spending. Europe would also profit from that if we could export more.

There are signs of a looser fiscal policy in the United States in future, which is expected to lead to higher growth rates. But that alone will not be enough. The important thing is to make the economy more productive. Another outstanding question is protectionism, which would of course be damaging, including for Europe. Trump is not President yet. We do not know exactly what he is planning, and we should therefore be cautious.

So you want to continue flooding the world with money. You have already purchased bonds for over a trillion euro. At the end of the programme planned so far, it will be €2.3 trillion.

We are not flooding anyone. People only ever talk about the billions of additional central bank money that we are making available. But hardly anyone mentions the fact that money and credit growth are fairly moderate. Our measures are thus aimed at stimulating this weak money and credit growth.

How can that be explained to someone who is not a central banker?

Both central banks and banks can create money through lending to the economy. If the banks are only doing so hesitantly, we can make financing conditions more attractive and so create incentives for more generous lending. As long as the overall money supply is not growing very quickly, that is not a cause for concern and does not lead to excessive inflationary pressures.

That means you are doing everything right, but no one understands?

I didn't say that, but when interest rates reach zero, monetary policy becomes very complicated to explain. The central banks have not exhausted their options, but they have to resort to unconventional means, such as the purchase of government bonds.

Here in Frankfurt, property prices have risen by 20% in one year. That is not very hard to understand. Is that the next crisis in the making?

We follow developments in the financial markets very closely. In some regions we are indeed seeing a strong rise in property prices, but it is still not a Europe-wide phenomenon. Moreover, such a boom is only really dangerous when it is financed on credit. However, the issuance of building loans is only growing very slowly.

In the event of a crisis, are you capable at all of responding in time? After all, countries like Italy are so highly indebted that they might not be able to cope with higher interest rates.

I can take this worry off your shoulders. When the time for higher interest rates comes, then we will increase interest rates. The countries would also be able to cope with that. Many of them have used the period of lower interest rates to extend the maturities of their loans. When interest rates rise, that will not therefore lead immediately to a significant rise in the cost of servicing the debt. That does not mean that high debt levels are not a problem, but they do not restrict the ECB's room for manoeuvre.

Italy is already causing us concern today. The big problem is the ailing banks. The new Government is considering State aid. Does that make sense?

The European rules permit that. Even Germany put public money into the banks at the height of the crisis. At that time, Italy did not. In my view, much more important than the question of where the money comes from is that there is a clear-out in the banking sector. There are too many banks in Italy and they are not profitable enough.