

DEBATE

Thierry DE MONTBRIAL, President and Founder of the World Policy Conference

Thank you very much. Tomorrow we will have a debriefing of the European Council. As of today, I would like to ask you two questions. It seems to me that the threat to the Euro can be analysed both from a short-term viewpoint and a longer term one. In the short term, we ask, 'Is there still a risk that speculation will destroy the Euro?' The very possibility of blowing up the Euro has now become a reality in psychological terms. That is the short term. The question of course is whether or not the measures that are being taken by the European Council will be enough for this very short-term issue.

Now, assuming the short-term issue is fixed, what about the long term? It seems to me that there is an issue of differential competitiveness, but there is also a debate. In the long term, is it possible to maintain a European Union if some countries lag behind others in terms of competitiveness? This is a much more structural issue.

Peter PRAET, Member of the ECB's Executive Board

I have been a Central Banker now for 10 or 11 years. I spent part of my career dealing with big infrastructures, such as payment systems. It is true that when it comes to infrastructure, we are used to the doomsday scenarios. At one point, I was in a workshop with the Federal Reserve in Washington. We talked about how the payment system in the US would continue if there was a nuclear attack on Washington. I am not making doomsday predictions about this.

Policy makers and politicians are wondering about doomsday scenarios and what would happen because the stakes are extremely high. I think what is happening is an understanding of what that would mean. I was very happy to see that some analysts some months ago said, 'It is sufficient. If you do not like it, delete it.' That would be an easy solution to the other problem that you mentioned. I was very happy to hear these people say, 'What would that mean?'

We are together here to discuss this issue beyond Europe. When the cooperative solution breaks down, which is at hand, that will have extremely damaging consequences for everybody. I think this is what is being understood. Now, of course, politicians say, 'These are very complex issues and we need more time.' Who will provide this time? How will it happen? I am not going to comment on this discussion, but it is what you often hear.

On the objective and the firm willingness to continue and keep it, I think this is understood, even saying, 'It would be so easy if one or the other.' We know what it would really mean. It is very important for people in all situations to understand that. It is collective interest.

The other question is very simple, actually. Is the monetary union sustainable? I am getting old and when I look back, I see all these currency or money creations, which very often provided a solution to gain time and so on. Devaluation of the currency would be the same. If you have problems with your labour markets or you have rigidities, you postpone the problem and find the funding for a while. There is a confidence trust and then you devalue the currency. You could say, 'Fine, I get 30% devaluation and then I can start again.'

With all the experience we had, starting from the 1930s and the currency story then, I thought that we had learned from that. In Europe where we have a single market and where a number of countries had the experience of 1992 and 1993, the risk we had in the internal markets related to the currency problems we had. Now, of course, I can also admit that some countries can have an independent monetary policy and exchange rate, such as Sweden. I understand that and I



do not see any problem, but the question is, 'Do you think that the rigidities that you have in a number of countries that led to the problem will be addressed?'

You could have a monetary solution to that, but it is not a monetary solution that will fix it. Because of the stress that these assumptions would imply, I do not think anyone envisages that. It is going to be tough for some countries. Think about Germany after reunification. That was a huge, huge effort. When people say that it is difficult to understand, my mother was from West Germany and told me about reunification. There have been huge efforts over all these years and this shows that these things are really possible, once there is a will. It is hard, but it is feasible.

Participant

Mr De Montbrial asked if speculators could ruin the Euro. How can we allow speculation? When will Europe take measures to reduce the power of these speculators?

Peter PRAET, Member of the ECB's Executive Board

What is a speculator? Who is selling Italian bonds and things like that? When you look at who the speculators are, very often you will see long-term investors, pension funds and insurance companies. It is not necessarily hedge funds that are really speculating. When the question of trust about policy comes up, it is very simple. As you said, we need good governance. Of course, speculators can destabilise faster because financial markets can move very quickly and brutally. This is absolutely true, but basically your fundamentals must be right. That is the first part of the answer.

The second part of the answer is not to make too many assumptions. Those who you call speculators are very often conservative or balanced investment managers who say, 'I do not know what could happen, but maybe I will sell this position or sell these bonds and buy something else.' If everybody does this, then you get a situation where you call them speculators. It could be many institutional investors, for example, who wanted to try to save their customers' money.

Of course, financial markets can be very brutal because there are very limited transaction costs and a lot of information and a lot of noise coming in, but we try to develop a level. I prepared a speech for Mario Draghi and it will be distributed at the end of this conference today. We took a number of initiatives before the crisis, which unfortunately were not sufficient. Mario and the Financial Stability Board under the umbrella of the G20 have a huge agenda of reforms. I think a lot of things are being done. It is a big story because we have to redesign our financial infrastructure.

In my job, I work to make the system more resilient. You probably think about derivative markets, which very quickly lower market participation to short with very low transaction cost for a country or a corporation or a bank. As you know, there are plans and projects to deal with this, but these are things you cannot change in one day, unfortunately. For example, the G20 put the derivatives market on organised exchanges and projects in the US and Europe. These are some of the things going on.

We have a very difficult agenda for the end of 2012 and I am working on these issues, but it is going to be tight. Fundamentally, never forget that when trust is lost, it is not only that. We have seen that those who are selling are very often institutional investors or Japanese long-term investors. The response is what Thierry talked about. You need to be serious in your governance. You have to identify the problems and act. It is true that they have been slow to act and have underestimated the problem and the depression of the financial markets. There was some noise about the ECB creating money to help, but that was not done.

I think now politicians understand what is going on. It is not yet finished. I fully agree. It is still tight. I think that good results take a bit of historical distance, but we are on the way.

Participant

It seems to me that there is some kind of confusion between the tasks of central banks and the tasks of governments. From my point of view, I think governments are supposed to take steps to correct the economic situation in different countries, and usually government do this the easy way. Look at the United States. President Obama gives hundreds of billions of dollars to the banks. Now, sometimes banks only have the task of managing the money and do not really have to draw up economic policies.

Where is your input in the discussion today in Europe about what will happen to the Euro? What is the input of the Central Bank in those negotiations between the prime ministers and the president of Germany, France and so on?

Peter PRAET, Member of the ECB's Executive Board

I have to be extremely brief now. I go along with the first part of your comments. I think they have taken the easy answer in relation to money creation. I think we have to think a bit more deeply than that. We are going to see what happens in other constituencies. I sense that is the first part. For example, Mario Draghi used the term 'fiscal compact' in one of his first speeches. Long before the crisis, there was signalling of the weaknesses in the economic part of the EMU. I can remind you of all the speeches. Jean-Claude has been extremely vocal for years about this.

The Central Bankers, as you know, have a very strong worldwide network internationally. That is why we are usually well informed and we see these weaknesses of governance and we are quite involved. Some politicians do not like it, but these things have been flat. We have our mandate, which is well defined, especially here, and I think it has to be like this. There is temptation to go the easy way and give the illusion that you will not have to address these fundamental problems that have often been ignored for many years. Now they are back forcefully and I understand that this is not pleasant. I fully agree that it is difficult, but we have heard these stories about needing more time for so long now.

I think now there is pressure. Unfortunately it is not optimal, but it is happening. There are some very good measures being taken all over the place. Take a little bit of perspective. We will see.