Christine Lagarde: Interview with Le Monde

INTERVIEW

Interview with Christine Lagarde, President of the ECB, conducted by Marie Charrel and Eric Albert and published on 19 October 2020

19 October 2020

With the pandemic getting worse, many countries are introducing new restrictions. Against this backdrop, what are your fears for the European economy?

The second wave of the pandemic in Europe, notably in France, and the resulting new restrictions are adding to the uncertainty and weighing on the recovery. Since the rebound we saw over the summer, the recovery has been uneven, uncertain and incomplete and now risks losing momentum. We will keep a close watch on indicators throughout the autumn. Our central scenario foresees euro area GDP declining by an average of 8% in 2020 and assumes partial and localised containment measures. If the situation deteriorates, our projections, which we will revise in December, will obviously be gloomier.

Back in March, some people were hoping that the pandemic would be a short-lived shock. That is not the case. What long-term scars might this crisis leave behind?

Job losses are the most serious. They pose a risk for the social fabric, household income, demand and growth. Governments in the euro area need to be extremely mindful of this. We think it’s essential that the fiscal safety nets that governments put in place during this crisis are not withdrawn too soon.

In response to the slowdown in activity, the ECB launched asset purchases amounting to more than €1.5 trillion, which is unprecedented. If the crisis gets worse, what more will it be able to do?

The options in our toolbox have not been exhausted. If more has to be done, we will do more. On taking up my position, I was told that there was nothing left for me to do, that everything had been done. But that was clearly not the case! We have found ways to stabilise the markets and support the euro area economy. Thanks to the action we took between March and June, we estimate that growth will be 1.3 percentage points higher overall, and inflation 0.8 percentage points higher. According to the ECB’s assessment, we have saved one million jobs in the euro area. So we have acted, and our action has been effective.

The pandemic emergency purchase programme, or PEPP for short, which was launched in March, has effectively calmed the markets. But does it actually support the real economy?

The PEPP has a dual objective: first, to stabilise the markets, and this objective has been fulfilled; next, to help bring inflation back to its pre-pandemic path, while keeping interest rates low and ensuring that these low rates are passed on to the real economy, which has worked. Our market actions, in tandem with our programme of long-term loans to the real economy – the well-known targeted longer-term refinancing operations (TLTROs) – have enabled lending to continue at very low rates. Lending rates for households and firms are around 1.4% to 1.5%. In the euro area, the volume of lending has increased by 7% for firms and 3% for households.

Central banks have been taking action for the past ten years and still need to do more. Why is their action becoming less and less effective?

After the crisis of 2008, fiscal policy was not forthcoming. Central banks were working very much in isolation. This was particularly true in the euro area. But we are now in a different paradigm. Fiscal support is playing its part and is working hand in hand with monetary support. This is unprecedented and will be effective.

In July, Europe agreed on an unprecedented joint recovery plan of €750 billion. Did you have a say in setting the amount?

As of a meeting of the Eurogroup in April, I had been stressing the need for a plan that is substantial, quick and flexible, but at the same time targeted at the countries and sectors that need it the most. According to our assessment, that corresponded to an envelope of between €1 trillion and €1.5 trillion. If you take into account the €540 billion of the first emergency package agreed by the Eurogroup – which included support for the provision of loans to firms, the short-time work schemes (the SURE plan), and the additional financing via the European Stability Mechanism (ESM) – and the €750 billion of the recovery plan approved by the European Council on 21 July, you could say we've reached that amount.

Given the urgency of the crisis, isn't there a risk that these €750 billion are allocated too late?

The Commission's aim is to be able to distribute these funds at the beginning of 2021, and this timeline must be kept. The ball is in the court of the national governments, who have to present their recovery plans – some of which are already ready – and of the Commission, which will have to examine them carefully but quickly. We also need rapid progress on the political side, in particular the adoption of the measures by national parliaments.

It is vital that this extraordinary plan, which has broken significant taboos in certain countries, is a success. If it is not targeted, if it gets lost in an administrative labyrinth and does not support the real economy in reorienting our countries to be more digital and green, we will have missed a historic opportunity to make a real difference.

The parallel interventions of the ECB and national governments enabled us to avoid a financial crisis. But if these difficulties continue, do we risk seeing a resurgence of fears that the euro area will implode?

I will repeat the words of my predecessor: the euro is irreversible. Additionally, the €750 billion recovery plan – collective borrowing that represents 5% of EU GDP – is a major turning point for Europe. It has changed things completely. We now have an additional tool at our disposal, even if it is something of an exception. National governments have shown that, if the situation demands it, there is clearly a will to work together in solidarity. Having more than 50% of the €750 billion in the form of grants for the countries and sectors that have been hit hardest is truly innovative.

Does the euro area finally have the beginnings of the budget it always lacked, to go alongside monetary policy?

This recovery plan tool is a response to an extraordinary situation. We should discuss the possibility of it remaining in the European toolbox so it could be used again if similar circumstances arise. I hope that there will also be a debate about a common budgetary tool for the euro area, and that it will be enriched by our current experience.

Such a debate will be tricky: some countries, like the Netherlands, already had strong concerns about the recovery plan…

This sort of opposition is not at all surprising: that's how Europe works. During the last crisis too, at the height of concerns, it took time to set up the ESM. For many governments, acknowledging that a collective response is the right response to a common shock takes time.

Governments have taken on huge amounts of debt during this crisis; debt that has been purchased by the ECB. Some economists are calling for this debt to be cancelled. Is that possible?

Article 123 of the Treaty on the Functioning of the EU forbids the ECB from financing the budgets of Member States, pure and simple. Debt cancellation would be exactly that. Breaking European Treaties is not on my road map.

1 November will mark one year since you took up your post. What has surprised you the most?

The severity of the shock. I experienced the 2008 crisis: between the summer of 2007 and the summer of 2008, problems increased gradually. There were signs that the crisis was coming, of stress in the financial system. This time, the speed and the scale of the shock were unprecedented.

At what point did you become aware of the scale of this crisis?

At the Governing Council meeting on 12 March, we decided to increase our asset purchases by €120 billion. As the situation was deteriorating between 16 and 18 March, we worked relentlessly and under lots of pressure to prepare the decision about the PEPP that was eventually taken during the night of 18 March. I spent that day on the phone to my staff from my dining room in Frankfurt, as we were all in lockdown at that point. Then in the evening all 25 members of the Governing Council met by teleconference. We had to act quickly and decisively. It was a collective decision: “We go big, or we go home!” At 23:30 we published a press release announcing our extraordinary €750 billion purchase programme.

With its reputation as an austere country, Germany’s support for the recovery plan financed by shared borrowing came as a surprise. Is this a substantial change?

This transformation came at just the right moment. Faced with such a severe crisis, Europe had to seriously reconsider its approach to issues related to balancing the budget, debt and state intervention. There was also a realisation that we were all in the same boat: if already weakened economies were to become even weaker, stronger economies would suffer too.

The ECB is considering creating a digital euro. Is this to support growth or to address geopolitical issues such as the emergence of a digital yuan?

It’s simply a matter of making our currency fit for the digital age. When we see how quickly digital payments are spreading, especially among young people, it’s important to meet this demand. If the digital euro were to see the light of day, it would not replace banknotes. It would be a complement to them. If we can have a means of payment that is more efficient, costs less, causes less pollution, can be used as easily as cash, protects privacy while ensuring traceability, reduces the cost of transferring money between countries and strengthens the international role of the euro, we would be remiss not to study it! That’s what we are doing at the ECB by starting to experiment and by launching our public consultation on the digital euro.

Should the ECB contribute to the ecological transition?

It’s a fundamental issue, and I am going to try to encourage the Governing Council to at least agree to reflect on what a central bank can legitimately do to contribute to the fight against climate change. I am aware that some commentators have their doubts. Very well, it's something we will debate. But we must take climate issues into account because they have an impact on price stability, our primary mandate.

Everybody must step up to address what is the main risk of the 21st century. If we don't do so now, it will no longer be possible for us to tackle climate change. It will be too late! Every one of us, no matter where we are, would be to blame if we didn't ask ourselves: what do I need to do to play my part? What can I do? My instinct tells me that we can do more than we think.

Christine Lagarde: Remarks at the G30 International Banking Seminar

SPEECH

Contribution by Christine Lagarde, President of the ECB, during the session "Rebuilding and Sustaining Growth"

Frankfurt am Main, 18 October 2020

The first phase of the coronavirus (COVID-19) crisis was an extraordinary challenge for public policy, but policy responses around the world converged fairly quickly. Governments everywhere acted swiftly to offset the loss of private sector income through massive fiscal interventions. Central banks stabilised financial markets and financing conditions, and – within their respective mandates – worked hand-in-hand with fiscal authorities to absorb the shock. The results were remarkable and averted what would have been a catastrophic depression.

But today the challenges facing economic policy are broader. The COVID-19 recession simultaneously calls on us to avoid structural *damage* and to encourage structural *change*. We need supportive policies to remain in place for as long as needed to avoid scarring of the economy and rising inequality. However, we also need to acknowledge the permanent changes that are taking place and – to extract as much benefit as we can from them – start transforming the economy now.

The potential for both structural damage and structural change emanates from the unprecedented impact of the COVID-19 recession on the services sector.

Compare what we have seen in the first half of this year with what we saw in the six months following the Lehman crash. From the third quarter of 2008 to the first quarter of 2009, services contributed -1.7 percentage points to the recession in the euro area and manufacturing contributed -2.8 percentage points. But in the first half of this year, the loss was -9.8 percentage points for services and only -3.2 percentage points for manufacturing. This has implications for the health of the labour market, the strength of the recovery and the distributional effects of the recession.

First, services are the most job-rich part of the economy, accounting for almost 75% of employment in euro area countries, putting a greater share of the workforce at risk[1]. Second, research finds that the recovery from a services-led recession can be slower than from a durables-led recession, as the latter creates more pent-up demand through deferred purchases[2]. Indeed, demand for consumer goods in the euro area softened in the summer months after bouncing back briefly in May and June, confirming the absence of widespread pent-up demand.

Third, a services-led recession – especially one driven by social distancing in high-contact sectors – tends to increase inequality. At the peak of the crisis, 40% of income for the poorest Europeans was coming from sectors that were heavily affected by COVID-19, compared with 16% for the richest. According to one estimate, two months of lockdown followed by six months with the economy operating at 80% capacity could increase the Gini coefficient by almost 14% in Europe[3]. And this feeds back into the recovery, since lower income households have a higher propensity to consume.

In this context, it is clear that both fiscal support and monetary policy support have to remain in place for as long as necessary and “cliff effects” must be avoided. Otherwise, we risk hysteresis in the labour market, an unnecessary loss of viable businesses and greater inequality. And the recovery in the euro area remains uncertain, uneven and incomplete, while the new coronavirus-related restrictions currently being introduced across Europe will add to uncertainty for firms and households.

Fiscal authorities are already taking action. All of the “big four” euro area countries have extended their short-time work schemes into next year. Our analysis finds that, at the peak of the crisis, such schemes halved the share of firms under liquidity stress and reduced “employment at risk” by almost two-thirds[4]. This week governments also announced their planned fiscal measures for 2021, which suggest that Member States plan to provide sizeable fiscal support to their economies next year.

All the conditions are in place for monetary policy and fiscal policy to continue working together. The GDP-weighted sovereign yield curve in the euro area is in negative territory for maturities up to ten years. And our forward guidance on our asset purchase programmes and interest rates provides clarity for governments on the future path of interest rates.

But precisely because the COVID-19 recession has affected services so deeply, it will also herald structural change. There is always some rotation of businesses during downturns, but the pandemic is different: it is accelerating the pre-existing spread of digitalisation in ways that look set to permanently reshape our economies and our societies.

Nearly 50% of Europeans say they have worked from home during the pandemic and of those only 18% are in favour of a full return to the office[5]. E-commerce increased by almost one fifth in terms of volume of sales between February and August 2020 and online payments have surged. Digitalisation has advanced on a massive scale in areas like education and medicine to reduce human interaction and increase resilience. In the United States, only 11% of consumers used telemedicine in 2019, but that number has increased to 46% with the pandemic, and 76% are interested in using it going forward[6].

This presents a possible future of higher productivity growth, less carbon-intensive lifestyles and more democratised access to essential services. But there is also a transitional challenge. In a more digital, post-pandemic economy, people will still visit shops and consume in-person services, stay in hotels and travel for business or pleasure, but possibly on a smaller scale than before. Sectors such as accommodation, food services and transportation could be lastingly affected. In the euro area, these sectors have been responsible for almost one fifth of the jobs created since 2013.

So not only do we need to protect old jobs, we also need to create new ones that reflect the new patterns of demand after the pandemic. And since this takes time and may require some adjustment – as we do not yet know exactly where demand will be focused – we need to create the conditions for experimentation and innovation today.

The key is to empower young firms. In the United States, new firms represent only 10% of all firms in a given year but are responsible for almost 30% of productivity growth[7]. New firms are also the engine of job growth: on average, firms up to five years old account for only one-fifth of employment, but are responsible for almost half of the jobs created[8]. Firm creation has slowed in Europe, however. In Italy, for example, there have been 37,000 fewer failed companies in the first half of this year compared with the same period last year, and 52,000 fewer companies created.

There is no contradiction between continuing to support the economy and encouraging its transformation. For new and innovative firms to grow, they need macroeconomic policies that support demand, because when uncertainty is too high a “wait-and-see” attitude stops the most productive firms from expanding[9]. They also need microeconomic policies that encourage firm entry and exit and the reallocation of resources across the economy. For example, the negative effects of onerous business conditions – like poor contract enforcement and lengthy bankruptcy procedures – are much stronger for new firms than for incumbent ones[10].

This is the direction in which policy ultimately has to move: it needs to be focused not only on protection but also on transformation; not only on preserving the economy as it is but also on creating new jobs and new sources of growth. In this way we can encourage structural change while minimising structural damage, which is the path we must take if our economies are to emerge from this crisis stronger.

Fabio Panetta: Interview with Kathimerini

INTERVIEW

Interview with Fabio Panetta, Member of the Executive Board of the ECB, conducted by Eirini Chrysolora and published on 17 October 2020

17 October 2020

The pandemic emergency purchase programme (PEPP) has so far secured low interest rate borrowing, especially for countries in need such as Italy and Greece. What do you expect to happen regarding the bonds of these countries when the programme ends? Are you worried that they will fall off a cliff?

The pandemic has driven the euro area economy into its deepest economic downturn. The GDP contraction hit double digits in the second quarter, with disinflationary effects. The ECB has therefore taken decisive measures to protect productive capacity and stabilise markets, providing favourable financing conditions for all economic sectors throughout the euro area. This, in turn, has sustained the flow of financing to households and firms, supporting aggregate demand and avoiding a more pronounced fall in inflation.

But we need to continuously monitor the evolution of the pandemic and its economic implications. The resurgence of infections we are seeing in a number of euro area countries is weakening the recovery, especially in the services sector, where the business activity index contracted in September.

This reinforces the need for prolonged economic support from macroeconomic policies. The ECB will conduct net asset purchases under the PEPP until at least the end of June 2021, and in any case until the Governing Council judges that the coronavirus (COVID-19) crisis phase is over. We will reinvest the principal payments from maturing securities purchased under the PEPP until at least the end of 2022. And any subsequent roll-off of the PEPP portfolio will have to be managed to avoid interfering with monetary policy. In any case, we will not allow any tightening of financing conditions that gets in the way of our aim.

Is there a possibility that the PEPP will be extended beyond June 2021? Could its size be increased beyond €1.35 trillion?

The key driver of economic developments is the evolution of the pandemic, which is depressing investment and consumption. According to European Commission survey data, in September euro area households’ savings intentions stood at their highest level on record since the start of the series in 2000. The current pandemic developments are not positive. On top of the direct impact on spending, uncertainty is likely to increase significantly, with adverse effects on both the economic outlook and the balance of risks.

Both actual inflation and expected inflation are already too low. In September the euro area headline inflation rate was negative for the second month in a row (-0.3%), while inflation excluding the volatile energy and food components was 0.2%. ECB staff have projected that inflation will rise to only 1.3% in 2022, but the most recent inflation data show that there is a risk of inflation dynamics being weaker than projected. Market-based inflation expectations are subdued, and consumers’ inflation expectations have also declined continuously since April.

In view of the sheer size of the downside risks, there should not be any doubt about our determination to preserve price stability. We stand ready to adjust all of our instruments, as appropriate, to achieve our objective of bringing inflation back to our medium-term aim in a sustained manner. During the pandemic we have already adjusted some of our instruments, and this has proven to be effective.

Do you feel that the ECB has once again done more than its share during this crisis? Will monetary policy be able to return to normal after such extensive quantitative easing?

The monetary policy and fiscal policy responses have been essential to protect households and businesses during the crisis, thereby facilitating the necessary public health response.

The mistakes that have characterised past episodes have been avoided. Monetary policy and fiscal policy reacted rapidly to the shock and have mutually reinforced each other. Together, monetary policy and fiscal policy have increased confidence.

A shy policy attitude at the present juncture would have the opposite effect. Our bank lending survey suggests that banks would tighten credit standards considerably if public loan guarantee schemes were not maintained. This could make otherwise viable companies and creditworthy households insolvent. Similar consequences could emerge from a tightening of financial conditions.

The only way to normalise monetary policy in the future is to forcefully support the economy now.

Does the Federal Reserve’s change in inflation-targeting pressure the ECB to follow a more accommodative policy?

Our own strategy review is under way and will be an important focus for our work over the next year. Its aim is to make sure our monetary policy strategy is fit for purpose, both today and in the future.

Some global developments that the Federal Reserve has taken into account in its review are also relevant to our current monetary policy. In particular, the marked decline of the “natural” rate of interest – i.e. the rate at which the monetary policy stance is neutral – observed in advanced economies complicates the task of monetary policy, as it reduces the scope for conducting expansionary policy through rate cuts. This has three key implications.

First, it should reduce our tolerance for inflation drifting downwards away from our aim and prompt us to treat our inflation aim as perfectly symmetric. Second, the instruments we have activated in recent years – such as asset purchases and targeted lending to banks – have been key to containing the risk of deflation and should remain in our toolbox; this would have a stabilising effect and reduce the probability that we have to use those instruments again in the future. And third, it indicates that in extreme situations, such as when interest rates are close to the lower bound, it is essential that fiscal and monetary policy reinforce each other.

To what extent does the €750 billion Next Generation EU (NGEU) package facilitate the ECB’s monetary policy?

NGEU can significantly improve the future path of the European economy. The mere announcement of the recovery fund has contributed to a further decline in fragmentation and supporting sentiment.

But now we need to activate NGEU quickly and use it for productive spending – in other words, to finance investment in a context of growth-enhancing reforms. It is crucial that the funds become available in early 2021, to avoid any fiscal cliff effects. And that the resources are allocated to the sectors that can be powerful drivers of growth in the long term. The link between recovery funding and reforms will further empower the multipliers associated with the recovery spending.

How long do you think it will take for the European economy to return to pre-coronavirus levels? What should Europe's priorities be in this process?

In the first half of the year euro area GDP declined by 15%, and according to the latest ECB staff projections it will return to pre-crisis levels only by the end of 2022. However, the return to more stringent containment measures that we are observing in a number of euro area countries may push this horizon even further away.

Moreover, there is a risk that a slow recovery will exacerbate divergences across sectors and countries: the longer it takes to return to pre-crisis levels, the greater the impact on divergence and inequality. The European fiscal policy response mitigates this risk, but it cannot eliminate it. We need to quickly return to growth.

How could Greek bonds become eligible under the public sector purchase programme (PSPP), and not only under the PEPP, given that they are still not investment grade?

The PSPP follows a clear set of rules about the eligibility of marketable debt securities and implementation modalities; based on the minimum rating requirements, Greek government bonds are not currently eligible for the programme. But we intervened to fight the effects of the COVID-19 crisis with a variety of instruments. The inclusion of Greek government bonds in the PEPP has stabilised financing conditions in Greece. The Greek ten-year sovereign bond yield has dropped markedly since the start of the PEPP, and currently stands at 0.8%, i.e. below pre-pandemic levels.

Greece, an already heavily indebted country, will be burdened with additional debt by the pandemic. Will its debt be sustainable?

Greece has a high debt burden, but the maturity of its debt is very long and the cost of debt servicing continues to be low, as also indicated by the successful recent issuances. The preliminary debt sustainability assessments by the European Commission on the eligibility of euro area countries for the European Stability Mechanism's Pandemic Crisis Support concluded that Greece's debt is sustainable.

Measures adopted by the Greek authorities, as well as those agreed with the European Commission, will have to support the recovery of the Greek economy, allowing debt ratios to abate over time. Looking beyond the short term – where fiscal policy has to manage the impact of the crisis – it is crucial that all resources are devoted to increasing the Greek economy's growth potential and that appropriate investments are accompanied by reforms which support potential growth and long-term debt sustainability.

How do you think the problem of higher non-performing loan (NPL) ratios due to the pandemic crisis should be addressed? In particular, will Greece, which already had a large stock of NPLs before the pandemic, be able to deal effectively with the problem with "Hercules" [the Greek asset protection scheme] or will it need to take additional measures? The Governor of the Bank of Greece has already proposed establishing an asset management company as a next step, a proposal which seems to be viewed positively by the OECD.

The Greek banking sector had an average NPL ratio of 36.7% in the second quarter of 2020. Such high levels of NPLs weigh on banks' solvency and profitability. This, in turn, hampers banks' ability to provide new credit to the economy, with negative consequences for economic growth.

The Hercules asset protection scheme will continue to contribute to sustainable NPL disposals and support Greek banks' efforts to achieve more sustainable NPL levels in the medium term. Nevertheless, even with these accelerated NPL disposals, the resulting NPL levels of Greek significant institutions are likely to remain far above the average for banks under European banking supervision. Against this background, all avenues for NPL reduction need to be examined. First of all, financial sector reforms should facilitate the process of NPL reduction. Further potential additions to the NPL resolution toolkit should also be thoroughly analysed.

The ECB is cooperating closely with all relevant stakeholders on these issues, including the Bank of Greece.

The Greek government recently published its proposal for the new bankruptcy framework, the so-called Debt Settlement and Second Chance Code. What are your views on it? Is it satisfactory? Would it help to put an end to the phenomenon of strategic defaults and restore the payment culture in Greece?

We are currently preparing our formal opinion on this topic. The ECB has had very constructive discussions with the Greek authorities about this major reform. Work is still ongoing on both primary and secondary legislation and on the IT infrastructure, as a significant number of the foreseen processes are envisaged to be conducted electronically. It is crucial that the reform increases the effectiveness of judicial and non-judicial procedures, improves the efficiency of bankruptcy proceedings and simplifies their procedural requirements, and strengthens the payment culture.

Media advisory – Agriculture and Fisheries Council, 19 and 20 October 2020

Indicative programme

Monday 19 October 2020

Place:
European Convention Center Luxembourg (ECCL)

Chair:
Julia Klöckner, Federal Minister for Food and Agriculture of Germany

All times are approximate and subject to change

from 08.30
Arrivals (live streaming)

+/- 09.45
Doorstep by minister Klöckner

10.00
Beginning of the Agriculture and Fisheries Council
Adoption of the agenda
Approval of non-legislative A items
Approval of legislative A items (public session)
Fishing opportunities in the Baltic sea for 2021

+/- 11.00
Common agriculture policy (roundtable) (public session)

+/- 16.00
Farm to fork strategy – Council conclusions (public session)
Any other business (public session)

At the end of the meeting – press conference in live streaming

Tuesday 20 October 2020

10.00
Common agriculture policy (public session)
Any other business

At the end of the meeting – press conference in live streaming

Arrangements for the press conference

Please note that there will be **no physical press conference**. **EU accredited journalists will be able to ask questions remotely** provided they have registered in advance.

In order to participate and ask questions, EU accredited journalists should register using this link.

Those who already registered for the previous press events in the field of agriculture and fisheries do not need to do it again.

Deadline for registration: Monday, 19 October 2020, 18:00.

Further instructions will be sent to all registered participants approximately half an hour after the deadline.

Videos and photos from the event

Visit the meeting page

Weekly schedule of President Charles Michel