

Luis de Guindos: Interview with La Razón



INTERVIEW

Interview with Luis de Guindos, Vice-President of the ECB, conducted by Jesús Rivasés on 14 September 2020

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Are we already living in a new economic world?

At the moment we are suffering the effects of a pandemic. The world was not ready for the type of lockdown that occurred in the vast majority of economies, and the fallout has been severe: the GDP contraction has been unprecedented and the way we do many things has changed. The hope is that, as the pandemic subsides, we return to some sort of normality. There are structural factors that may change, such as our global value chains. From now on, more importance on proximity, not just profitability and cost efficiency, may be placed. The pandemic will also result in more debt, both public and private. These are issues which, once a solution to the pandemic has been found, will still exist and will affect day-to-day economic decisions.

Should the European Union continue to offer stimulus and/or prolong the suspension of the Stability and Growth Pact?

When there is such a sharp decline in GDP and private sector income, as there has been during the pandemic, the public sector has to intervene temporarily to halt the slump. This was unavoidable, and both the fiscal and monetary

stimulus should continue for as long as we feel the effects of the pandemic.

Is the ECB prepared to maintain its low interest rate policy and asset purchase programmes for as long as required?

The ECB's response to the pandemic was, first and foremost, to provide banks with liquidity on very favourable terms to enable them to continue lending to businesses and households. We then expanded our asset purchase programme through the pandemic emergency purchase programme (PEPP) to stabilise financial markets. This avoided fragmentation in the sovereign debt markets. Last of all, some banking supervision rules were adapted to ensure that credit could continue to flow.

Nevertheless, the first line of defence is fiscal policy, both national and pan-European, with the latter embodied by the recovery fund approved by the European Council. The response, from both a fiscal and a monetary perspective, has been completely different from the previous crisis. This time around it has been fast and powerful, enabling us to avoid an even bigger contraction in euro area GDP than the one recorded in the first half of the year. It will also help contribute to the economic recovery.

Is there any possibility that the PEPP, which for the time being is temporary, will be made permanent?

It is a temporary emergency programme which is serving its purpose.

But temporary things sometimes have a habit of becoming permanent...

For now, the PEPP will run until the middle of next year. It has a total envelope of €1.35 trillion, a substantial amount of which has still not been used. The programme is very flexible; it is serving its purpose and there is still room for manoeuvre. It averted a sharp increase in spreads and enabled financial markets to remain calm. Thanks to that, we have avoided having to deal with a debt crisis on top of the public health and economic crisis, and this has been crucial. Looking ahead, the ECB stands ready to adjust all of its instruments as appropriate. For the moment, we believe that the programme is performing well, also from the point of view of pursuing our primary objective – our inflation aim.

To what extent could the ECB expand its balance sheet?

I would phrase it differently: the ECB has to act for as long as its price stability objective is not met.

Will the ECB keep inflation as its primary objective?

It is the EU Treaty that says that the ECB's primary objective is price stability. What has changed over time is the definition of price stability. To begin with, it was below 2%, and in 2003 it was clarified that would mean "below, but close to, 2%". Here at the ECB we are now engaged in a strategy review that will evaluate, among other things, whether the current definition of price stability is fit for purpose.

Would you advocate for the ECB to follow the example of the Federal Reserve (Fed) and consider employment as well as inflation?

The ECB's mandate is price stability. The Fed has a dual mandate – price stability and employment. That being said, when the ECB calculates its inflation projections, it also takes into account economic variables such as economic growth and employment. But our primary mandate, which we do not set for ourselves but is set out for us in the Treaty, is defined in terms of price stability.

Are you worried that the Fed's new policy will leave the door open to higher inflation, and that that door will be impossible to close?

Our inflation projections indicate that the risk is inflation being very low, not very high. After the pandemic, in theory there is the possibility of value chains being less efficient and less global, and that this will cause inflation to increase. But we also take this into account when we make our projections, and even then inflation is projected to reach 1.3% in 2022, which is clearly below the ECB's definition of price stability.

Do you see a euro/dollar currency war on the horizon?

There are certainly tensions around trade and low economic growth but, from the point of view of international economic governance, it would be suicidal to enter into any sort of dispute about exchange rates.

Should the ECB intervene to prevent the appreciation of the euro?

Setting the exchange rate is not an ECB objective. Our objective is price stability. However, when I said earlier that we monitor a very broad range of economic variables, that includes the exchange rate, because it affects medium-term inflation expectations. We keep it in mind, but we do not target the exchange rate because that is not our mandate.

But will the ECB monitor developments in the exchange rate, just in case?

We will monitor it, we will analyse it, it will be an input for the models we use to calculate our inflation projections, but our ultimate objective in doing so is not to influence the exchange rate. Rather, we do it because of the impact the exchange rate has on inflation.

In the case of the euro and the dollar, to use Mario Draghi's words, will the ECB do whatever it takes?

Those words were used in reference to a different issue, not the exchange rate. I'll say it again: we do not target the exchange rate. It is an important variable, as the appreciation of the euro has an impact on our inflation projections, and these projections influence our monetary policy. Not because of the exchange rate itself, but because of its ramifications for inflation in the medium term.

Would some euro area countries have gone bankrupt without the ECB's intervention?

In this crisis, the protective umbrella of all the European institutions, not just the ECB, has been crucial, especially for the most vulnerable countries. Our action has averted a debt crisis and the newly created €750 billion recovery fund has some very innovative elements, such as joint debt issuance and non-repayable grants, and is focused on the most vulnerable, most affected countries. In these countries, which include Spain, the actions of the European institutions – the ECB, the European Council and the European Commission – have undoubtedly limited the impact of a severe crisis and are driving the path to recovery, which we have to make the most of in the future.

In other words, the European institutions saved Spain.

The European institutions have acted as an extremely important protective umbrella. Without them, the crisis would have been worse because we would have had a debt crisis on top of the public health and economic crisis, but we managed to avoid that. This time, the European institutions have responded – they have been the main source of support to minimise the impact of the crisis.

Is Spain now doing its homework?

I don't discuss national political issues. There was a very severe drop in GDP in the first half of the year, of up to 23%. This was all down to the lockdown and Spain's production structure – the tourism and services sectors are very important. We expect a significant rebound in activity in Europe in the third quarter, just like what happened in May and June. And in Spain the recovery should be stronger, because the fall was also more severe. Ideally, we would avoid an uneven recovery across euro area countries, and this is why the recovery fund is so important, because it focuses on the countries that are considered to be most vulnerable.

That's the ideal scenario, but is a stronger recovery in Spain to be expected?

With a drop [in GDP] of almost 23% in the first quarter, a very strong rebound is the most likely scenario in the third quarter, simply as a result of easing the lockdown.

How is a Government like Spain's, with ministers from a far-left party like Unidas Podemos, seen by the ECB?

The ECB doesn't make political comments of that kind. Personally, I usually say that the Spanish economy always surprises on the upside. Spain, like other vulnerable countries, has had lots of support from the EU institutions. Unlike what happened during the previous crisis, in terms of both purchases of Spanish public debt and what the recovery fund is going to provide, Europe is giving Spain its full support. And that's extremely important. It's not the only thing though, because the right economic policy must of course then be implemented.

Are you confident that the Spanish Government will implement the right

economic policy?

It's not about whether I'm confident or not. The only thing I want is for the right policies to be implemented. European institutions have provided vital support to tackle a terrible crisis. That has made it possible for the Spanish economy – both the public sector and the private sector – to continue to obtain funding at very favourable terms and it has prevented a debt crisis coming on top of the public health and economic crisis.

How many more bank mergers are needed in Europe?

Bank consolidation is one of the tools that can be used to address the low profitability of European banks, which have also been hit particularly hard by the pandemic and the economic crisis. There was already overcapacity, low profitability and inadequate cost structures before the pandemic and, in that environment, consolidation is a tool that can help. However, the ECB does not get involved in designing or determining any kind of specific [consolidation] operation.

Days before the merger between Caixabank and Bankia was announced, you said that you thought mergers were urgent and that they could happen quickly. Do you now anticipate cross-border mergers in the relatively near future?

The ECB calls in general terms for consolidation to be used as a helpful tool so that banks' low profitability problems can at least be contained. It's not about anticipating or not anticipating. The ECB – also in its role as supervisor – has identified that there is a vulnerability, a drop in profitability, and that consolidation can be an appropriate tool to try to change that situation. Low bank profitability is not a trivial matter and it has implications for how strong banks are. Of course, in a single European banking market, cross-border consolidation is one of the tools we call for [banks to use] to achieve the necessary improvement in profitability.

Does the ECB see that big cross-border merger on the horizon?

It's not about us seeing it or not. We make recommendations for the banking sector overall, but it must be the banks themselves that make the decisions.

Will there be more mergers this year?

That's not up to me. The ECB has repeatedly said that consolidation can play an important role, but it doesn't dictate which banks should merge, neither domestically nor across borders.

Does the ECB plan to launch its own cryptocurrency?

We would be talking about a digital euro, if anything. An internal high-level taskforce at the ECB is analysing it, just like at other central banks. It's an important issue for financial stability and monetary policy. There's an underlying trend here, because the European economy is going to be increasingly digital, especially after the pandemic. At this stage we cannot say with any certainty whether there will be a digital euro or not, but it's another element of an overall unstoppable trend. In any case, it would always

be necessary to put in place the system that is most beneficial to euro area citizens.

Does the ECB have more power than governments?

The ECB's power is a delegated power. Governments signed a treaty and we have to comply with that treaty. We are legally accountable to the European Court of Justice and institutionally accountable to the European Parliament.

So aren't you and Christine Lagarde the two most powerful people in Europe?

I don't think that's the best way of describing it. What's important is that we do our job well – and it's not an easy one – at a very difficult time. And not just President Lagarde and me, but all of the Executive Board and the Governing Council too. We have a mandate and we will be judged based on how we fulfil that mandate, which was set by political authorities.

Sorry, but you are independent and you have the power to create and destroy money, which nobody else has.

We are independent and we decide which instruments are the most appropriate for us to fulfil our mandate, but that mandate is given to us. We are also accountable to the European Parliament in terms of how we use those instruments.

But who else in Europe can create and destroy money like you can?

That's what happens with any central bank. By definition, central banks set monetary policy. That's their role. And they do it independently because that is what has historically served citizens best. But it's not a role that goes unchecked, as there is a mandate that we must respect. And that's why the European Parliament, the European Court of Justice and, on a more operational level, the European Court of Auditors, also exercise their powers of oversight in relation to the ECB.