Yves Mersch: Interview with Le Monde

INTERVIEW

Interview with Yves Mersch, Member of the Executive Board of the ECB, conducted by Marie Charrel and Eric Albert

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How do you feel about the euro today compared with your hopes and expectations at the time of negotiating the Maastricht Treaty?

At the time, it was a leap into the unknown. The international financial markets were sceptical. And we didn’t know whether citizens would embrace the new currency. Today, I am very satisfied with the outcome. First of all, the euro has won the wholehearted approval of more than 75% of Europe’s citizens. And even the most eurosceptic of political parties have changed their opinion on this given that Europe’s citizens do not want to “undo” what has already been accomplished.

What’s more, it’s a currency valued by the corporate sector and sought after by the financial markets. Only a few years ago, there were still concerns that the euro area might fall apart. The political response to the crisis and the steps taken by the European Central Bank quelled those concerns. Today, the differences in interest rates across countries, across firms in those countries, have been reduced. And there is heightened demand on the part of international investors for euro-denominated assets, even though we do not have the same financial market depth as other countries, such as the United States.

There is still scepticism surrounding the euro. Are you at all concerned by the mistrust of Monetary Union voiced in Italy at the start of the pandemic, or in Greece during the 2012-15 crisis?

It is always easier to blame Europe for what's not working and attribute success to national policies, and that can fan the flames of this mistrust. In spite of all that, public support for the euro is strong. In some Member States, it is even close to 90%. We shouldn't forget about the permanent transfers that flow within the EU from its more developed to its less developed members. If the latter were not in the euro area, their debt would undoubtedly not be financed at such low interest rates. Leaving the euro area would increase their debt servicing costs through interest rate levels and devaluations, which would mean less money for investment, research and education. And by the way, we can also ponder whether or not the younger Member States would remain intact if they left the single currency and the EU.

The euro nevertheless went through a major crisis between 2010 and 2015, which led to huge social upheaval…

The initial agreement was that we would have a single currency, but that fiscal, economic and structural policies would be kept at national level. We were aware that it was a source of tension, which still exists today. But we learned lessons from the last financial crisis. The response to the pandemic has led to much closer coordination, as it happens, between monetary policy and national fiscal policies. And the Stability and Growth Pact (which caps the budget deficit at 3% of GDP) has even been temporarily put on hold.

The EU has also reached an agreement on a €750 billion recovery package. Talks to finalise the package are ongoing. Is this a "Hamiltonian moment" for the EU in terms of taking a step closer towards federalism?

It is a very important step. Europe has shown that it is still capable of employing its political capital to respond with solidarity. This has had a considerable impact on non-European investor confidence. But the European recovery package is temporary in nature, for use only in response to the pandemic. To say that it marks the beginning of the "United States of Europe" is going a bit far. The situation is very different from when Alexander Hamilton advocated for US federalism in the 18th century in the wake of the civil war. At that time, there was a very clear financial benefit to consolidating the debt of the southern states funded by their northern counterparts.

From an economic perspective, has Europe fallen behind the United States since the 2008 crisis?

We can make up the ground that we have lost. The gap has come about due to structural factors. There are strong trends such as demographic change (moving at a faster pace in the United States) behind the difference in per capita GDP. There is also the proportion of funding to the economy provided by banks in Europe. When a banking crisis occurs in an already weakened sector, it has a knock-on effect on the entire economy, and the recovery takes even longer. We have learned from this, which is why we set up the banking union and insisted on the need for a capital markets union. Moreover, European fiscal policies have been excessively procyclical. As a result, countries that built up their reserves are currently in a much better financial position to deal with the pandemic crisis, whereas those with the highest levels of debt know that there are limits to the action they can take.

There is also the issue of private debt. At the beginning, it was higher in the United States, but it has been brought down much faster there than in Europe. Last of all, Europe needs to implement structural reform at national level. Recommendations have been made, but they haven't resulted in action being taken. The same goes for the Stability and Growth Pact: the rules are not being complied with. To me, there is a significant lack of governance which needs to be fixed. To be master of its own destiny and compete with the United States, Europe needs to solve its structural weaknesses.

Since the euro area was created, it has remained an unfinished project, edging slowly towards completion, and only during times of crisis. Do you know why?

The differences across the economic, financial and political cycles, which are never aligned in the various Member States, are holding back progress. This poses a challenge to the task of building Europe, which, as Jean Monnet pointed out, only picks up speed in times of crisis. But once you've been working this way for 30 years, it becomes second nature! It is difficult to avoid these delays and complexities when you embark upon a project as colossal as building the European Union in peacetime. Similar projects in other countries have often been the result of civil wars.

In the long run, will the EU Treaties need to be amended?

We can already implement significant reforms without changing any Treaty, such as creating the capital markets union a must for us or completing banking union. Reform in other areas will be more challenging. Transferring some powers that have remained at the national level up until now, such as budgetary authority, or taxation – still subject to the unanimity rule – will thus be very difficult to do without transferring a degree of national democratic representation – sovereignty – to the European level. The issuance of common European debt is a sign of significant progress, but common budgetary capacity or a European budget worthy of the name are still a long way off. Currently, the European Parliament is above all else responsible for expenditure, but very little revenue: the system is therefore flawed. During the discussions held prior to the Maastricht Treaty, we were convinced that the single currency would act as a catalyst for European integration. We were hopeful that the markets would push in that direction. But in this respect, they have at the very least…been slow to respond.

Many people today are calling for a review of the Stability and Growth Pact at the very least – the target of 3% of GDP for the budget deficit and of 60% of GDP for debt – a target with which Member States are no longer able to comply. Should the Maastricht rules be reviewed? If so, in what way?

The less we have complied with these rules, the more complex and confusing they have become for the general public, which is not very democratic. However, it is true that they are a reflection of the situation in the 1990s when inflation and growth hovered around 2%. We can simplify and revise them to take into account the effects of globalisation, demographic change, and the fall in the equilibrium interest rate. But it is also worth noting that there is currently a debate in Germany to bring the budget deficit to below the 3% mark in 2022 or 2023. At the end of the day, compliance with the rules has nothing to do with the economy. It is more a matter of political science and law. Abolishing the Maastricht rules will not improve the functioning of our economies. For that to happen, we need to improve our capacity for growth, and therefore implement structural reforms.

By aiming to comply with these fiscal rules at all costs, isn't there a risk that we may make the same mistake we made in 2010 by reintroducing austerity policies too early?

Making public spending more efficient is not the same as austerity. The temporary budgetary support measures are not sustainable if there is no recovery in activity levels. From the outset, the Stability and Growth Pact required a balanced budget. Is that a bad thing? We need to find a common response to this issue. If it is the norm to have a budget deficit of, let's say, 5% of GDP, this means that national as well as international investors need to be found to finance it. International investors like policies that are predictable, robust and sustainable over the long term. We have the benefit of a stable currency that has the backing of our citizens. This should not be undermined by an unsustainable fiscal policy.

Over the next few years, what changes would you like to see within the EU?

Structurally, we need to continue with our efforts in education and research which are crucial for our future. But we also need to provide a more tangible response to the issues that are of major concern to our fellow citizens. How will Europe deal with matters of internal and external security? How will it deal with healthcare? Are we convinced that the response to the pandemic should be purely domestic, as should the response to terrorism? The problem is that as the Treaties currently stand, we cannot respond at the European level.

You have attended more than 500 Governing Council meetings. Do you have any regrets or are there any particular success stories that come to mind?

Before joining the ECB, I also attended several hundred ECOFIN meetings and around a hundred EU Council meetings. Europe is part of who I am, so please forgive me. The success stories are always collective, never individual. At the ECB, a young institution, we have always favoured a more federal-style and consensus-based decision-making process. It works very well. And it also makes it possible to overcome the all-too-often intergovernmental approach to European decision-making.