

Benoît Cœuré: Interview with the Financial Times



Interview with Benoît Cœuré, Member of the Executive Board of the ECB, conducted by Claire Jones on 12 June, and published on 17 June 2019

At the last ECB Governing Council in Vilnius, there seemed to be some progress in coming up with solutions to face the risks to the outlook.....

The Governing Council discussion in Vilnius was about making sense of diverse signals from the economy and the financial markets. The eurozone economy is not doing so badly; in fact services and construction are doing quite well. The concerns are really around the manufacturing sector, and the source of these concerns is mostly, if not entirely, to be found outside of the eurozone and may be temporary. The signals coming from the financial markets, however, are quite alarming.

Anything in particular that alarms you?

The constellation of prices in the bond market paints a picture of the global economy which is very bleak. Central banks should never ignore market signals. They shouldn't follow them blindly either. I'm not saying this as a reason to be complacent, but we have to make sense of this divergence between market prices and economic data.

Our baseline staff projection for the euro area economy is not so bad. And that message is something that the Governing Council is broadly comfortable with. But the distribution of risks around this projection has broadened. Risk has increased. And that required reassurance from the Council that we're

ready to address these risks, should they materialise. So far we're talking about contingency planning. But at some point during our next few meetings, we might very well be facing a situation where risks have materialised.

And the question is not whether we have instruments; we do have instruments. We can change our guidance. We can cut rates. We can restart QE. The question is which instrument, or combination of instruments, would be best suited to the circumstances. That discussion only started in Vilnius; we need to take it forward and reflect on the nature of the risks we're facing.

Can you cut rates without tinkering with the way negative rates are applied to banks?

All options come with costs and benefits, and we have to ponder them very carefully. None of this would deter us from acting. We have a clear mandate and will act on our mandate. So, if the conclusion were that cutting rates is the best option, then we would have to consider the impact of negative rates on financial intermediation, especially for banks. We would have to consider whether a tiering system is needed. Today the prevailing view in the Governing Council is that it is not, but we also agree that it deserves further reflection.

Markets have got ahead of you. A lot of people are already pricing in a rate cut. A lot of people are already thinking that the guidance that rates are expected to remain on hold for the first half of 2020 is out-of-date, even though you've moved it forward only last week. Does that not blunt two out of three of the policy options you've mentioned?

I would like to challenge the view that our guidance has to be aligned with the market at any given point in time. If that were the case, then it would not be needed in the first place. The guidance is a way to filter the view of the Governing Council on future economic developments and doesn't have to coincide with market expectations.

But in terms of your capacity to surprise, to really get ahead of markets, that's a bit limited...

Whatever the instrument, we'll calibrate it to what's needed for the eurozone economy.

Some people have the idea that the issue limit on the proportion of a member state's bonds you can buy of a third of all the outstanding stock is not as hard as people might have thought in the past. Would you agree with that?

The European Court of Justice has stressed the relevance and usefulness of limits. The limits are there to guard against monetary financing and to protect the price discovery process. On the other hand, the ECJ has also affirmed the principle that we should have broad discretion in designing our instruments. The limits are ours. We already have some degree of freedom across securities. For instance, we already buy up to 50 per cent of supranational bonds, while for individual sovereigns the limit is lower. I'm not saying that's the way to go, but a more detailed discussion is possible

if warranted by our price stability objective.

We've been very serious about these requirements since we started QE and if we were to restart it, we would have the discussion again in a serious and responsible way.

Some believe that if you have more action from the ECB, you might need more fiscal spending as well...

We have a mandate to fulfil, and we will do what is necessary to fulfil it. There is no quid pro quo between the ECB and governments, and we are not going to threaten them. We all have a job to do. But imagine that if the eurozone were hit by a particularly adverse negative shock, then lack of action on fiscal policy in those countries which can use it would require a stronger monetary policy reaction. And a stronger monetary policy reaction would magnify the potential downsides of rates being low for long.

Does the ECB need to follow the Fed's lead and review its monetary policy strategy, in particular its inflation objective?

I tend to think that we have more urgent issues to face right now, but I'm pretty sure that we'll do it at some point nevertheless.

Having very substantially broadened our range of monetary policy instruments, and having learnt a lot from the crisis, I expect that, at some point, we'll have to take stock of that experience and review our monetary policy strategy, whoever is the next president.

But I would advise against doing so in a piecemeal way. The definition of price stability is an important dimension, of course, but it is not the only one. You also need to ask yourself which instruments have worked well and which have worked less well. You need to reflect on the structural changes in our economy – technology, globalisation, servicification – that have kept us away from our targets. Looking forward, maybe climate change will be another important thing to look at, too.

What's your thinking on how the ECB has changed over the past eight years?

It's a long journey that goes back more than eight years. And the ECB has always been its own beast, even when it started back in 1998. It was never designed to be exactly like the Bundesbank, but it's true that, since then, it has borrowed features from the Fed.

And we've certainly abandoned the small, open economy mindset which was the one of most participants back then.

We've also learnt the hard way that Economic and Monetary Union is much more fragile as a construct than initially thought. And that the job of the ECB is not only about setting prices and quantities for monetary aggregates across the eurozone, but also about dealing with some of the flaws and imperfections that hamper monetary policy transmission. We've had to look under the bonnet and find out how all parts of the engine work.

But let me add that the challenges for the next eight years could be substantially different, and could be even more daunting.

What do you think the key challenges are going to be for the next president?

Let me outline four main challenges. First, global cooperation is eroding. The capacity of global policymakers to deal with shocks to the global economy is today less than it was previously. The kind of coordinated action that we saw back in 2008 would be more difficult to achieve today. I'm not saying it would be impossible, but it would be more difficult.

Second, the eurozone's structural weaknesses, its lingering fragilities, are not going to go away soon. I'm not dismissing all the good work being done in Brussels and other places to strengthen the European Stability Mechanism and to complete banking union, which is something that we didn't have eight years ago, and that's clear progress. But we're still only half way. And as long as this journey is not completed, new crises will inevitably come, and we have to stand ready to ride out those crises.

Third, as the ECB, we do have instruments, and we've shown that we're ready to use them and even design new ones while staying within our mandate. But the cost of using any given instrument might be increasing, which makes the trade-offs more acute. Let me give an example. Rates being low for long may eventually create financial stability risks. So far, they've been limited, scattered around the continent, around sectors, around jurisdictions, and they could be addressed using targeted macroprudential instruments.

But most of these macroprudential instruments are about addressing risk in the housing sector; there is little they can do today about risks in the corporate sector, or in shadow banking.

And finally, there are mounting challenges to our independence. The world today is different from the one we faced in 2011 or 2012. There is widespread mistrust of experts, and what are central bankers if not experts? European politics is much more fragmented, both within countries and at the European level, than it was eight years ago, and that has been evidenced by the latest European election.

The temptation to either overburden central banks with a variety of objectives which politicians cannot achieve, or blame them for political failures, will be greater, and that's something we'll have to live with.

Monetary policy is difficult to understand. And because money creation is something that captures attention and fascinates, expectations of the ECB can also be too high. But there are things that we just can't do. And there are things that we could do, but should not do, because they are political in nature.

I'm convinced that our narrow price stability mandate has served us very well and has protected us from politicisation. A broad mandate is something that we would not be well equipped to manage, because we are not a political institution.

The conclusion is that we will have to safeguard and defend our independence more strongly than we have had to over the last eight years, at ECB level and at the level of national central banks.

So what would be the right credentials for the next president to have, with those challenges in mind?

It's a decision for European leaders and European finance ministers to take. But there are common credentials for any central bank governor. For example, part of the job profile is to understand markets. Because, like it or not, we have to understand what markets are telling us. We don't always have to agree. But we have to understand the language they speak.

Also, you need to understand the political environment – because you have to be able to uphold your independence, and because monetary policy is not the only game in town and in many cases needs supporting action.

If you want to see the fiscal response or regulatory response that will help monetary policy, you need the ability to talk to political leaders, respecting our different mandates. And finally, good economics never harm.

How do you make the public more aware of what the central bank can and cannot do?

First, you need to explain what you're doing, and there are certainly many ways we can do it better. This is an area where central banks can learn from each other.

For instance, what the Bank of England has been reflecting on in terms of using plain language, trying to resist using arcane, academic language when talking to citizens, is something we could make good use of.

It's even more important for the ECB to be active reaching out to people. Being a European institution in a tower in Frankfurt, we can seem even further away.

It's a big challenge. Frédéric Bastiat, the French economist from the 1840s, wrote a wonderful book which is titled "Ce qu'on voit et ce qu'on ne voit pas", "What you see and what you don't see".

Monetary policy works by trickling down first to the banks and the financial system and then on to the whole of the economy. So people see the direct impact – unemployed workers will see that we're lifting stock prices, banks will see that we're shrinking their interest margin. They don't see the indirect impact – jobs being created, wages being lifted thanks to higher consumption and investment – and that's what we have to do a better job of explaining.

One of the big problems of the euro is that it hasn't produced as much economic integration as you would have thought. How do you address that?

That's true. We need more integration and we need more convergence. Which is why the budgetary instrument for convergence and competitiveness that has

been agreed by the Eurogroup is a useful step, although it should evolve over time to include counter cyclical features.

What do you think of the involvement of the ECB in the troika that designed and imposed the Greek bailout programmes? Would you defend it as the right decision?

The ECB's involvement in the troika was a symptom of one of the many flaws in the eurozone as it was set up. Being in the troika was not the right place for a central bank.

But back in 2010, the institutional framework was highly deficient, and the only way to gather and aggregate the relevant expertise was to bring together the Commission, the IMF and the ECB. The ECB was asked to do it and did it as a service to European governments. I don't think we could have escaped from playing that role and we played it in an honest and professional way.

Now, the institutional framework has improved, we have a new arrangement emerging between the Commission and the European Stability Mechanism, and ECB involvement is much less vital than it was in 2010.

We've already scaled down our involvement; for some time now in Greece, we've been focusing on financial sector issues, where our expertise is clear, and on broad fiscal topics. We wouldn't take a view on the structure of taxes, or on reforming public administration, or on social benefits, as we have done in the past.

How do you feel about the political will for more integration, after the European elections?

As a citizen, I want to pick out the good signs from the European elections, in particular the renewed focus on the environment and climate change. Now, focusing more narrowly on the single currency and monetary union, that discussion was largely absent from the electoral campaign, in all countries. And that's a lost opportunity.

What remains to be done to complete Economic and Monetary Union is profoundly political. It's not a technical discussion. It's about the appropriate degree of solidarity and of discipline that is needed to make the eurozone more resilient and protect it in times of crisis, and that is highly political. And you would need a broad discussion around it; ideally a pan-European one.

Ultimately the problem is that while European citizens see the benefits of the euro as a currency and all want to keep it, they are not ready to accept the constraints on national economic policies that come with membership of the Monetary Union. And that has to be explained: you cannot be a free rider in a monetary union; you need to have the right policies at home and in Brussels. The European elections could have been the right time to have the discussion. But it didn't happen, and misunderstandings and misgivings will stay with us. This creates a lingering fragility.

How involved should central banks be in combating climate change?

Climate change is a defining issue for the global economy. No one can ignore it, certainly not central bankers. We cannot be blind and deaf to the discussion.

We need to understand how climate change will shape the economy. The time horizon has shortened. Climate change used to be envisaged as a very long-term issue, but it is not anymore; some of the consequences are already visible today.

As a result, it becomes relevant for macroeconomic policy-making.

The discussion about the links between financial stability and climate change has started already. Mark Carney has played a leading role in that discussion, in the Financial Stability Board and in the G20. Considerations such as the carbon footprint of our pension and own funds portfolios can be – and often already are – taken into account. The discussion is now increasingly shifting to monetary policy. There, we have to be much more cautious: we have a clear price stability mandate, and everything we can do to combat climate change has to be assessed against it.