

Luis de Guindos: Interview with La Stampa



INTERVIEW

Interview with Luis de Guindos, Vice-President of the ECB, conducted by Marco Zatterin on 26 June 2020 and published on 1 July 2020

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The International Monetary Fund has just revised down all of its projections. How is the European economy looking from the ECB's perspective?

The level of uncertainty is very high, so various scenarios need to be considered while acknowledging that it is difficult to produce projections. In reality, one thing is certain: we have experienced a deep fall in economic activity. This fall was very rapid, very sharp, and took place within the space of two-and-a-half-months. As governments have started to reopen their economies, we have begun to see a recovery in activity, with indicators pointing towards a rebound in a number of countries.

And yet there is persistent uncertainty.

It's normal that there should be a recovery when economies reopen, just as it's normal not to know what will happen after the summer. Many unknowns and question marks remain. But the most worrying thing is that a two-speed recovery seems to be starting to emerge. The fall has been sharp everywhere, but in some countries it was steeper. There is a group of more resilient economies that reacted better than others. For this group, GDP will therefore

increase at a faster pace. This could lead to two-speed growth in Europe. We must keep a close eye on this.

What lessons have you learned from the pandemic?

That, to a large extent, countries weren't ready to deal with it at the beginning. This task falls to governments and public health authorities, it is not just an economic issue. The ECB acted quickly and effectively. But other EU tools, including fiscal instruments, would ensure that we are never taken by surprise again. We have understood that we need to complete Economic and Monetary Union. If we had completed the banking union, progressed towards a genuine capital markets union, and if we had had a common budgetary instrument for the euro area, the shock would have been more contained. The only way to avoid asymmetries in the fallout from the pandemic would have been to have had a single response in place at the European level.

Essentially, are you saying that with greater unity, Europe would have been stronger?

Exactly. That is what I mean.

The ECB's response has nevertheless been massive. What is your assessment of its impact?

The ECB's response focused on three pillars. We significantly increased our bond purchases, mostly sovereign bonds, we provided banks with huge amounts of liquidity to grant loans to the real economy, and together with the competent national authorities we introduced support measures for bank capital to avoid a credit squeeze on companies. The impact on the financial markets has been very positive. In addition, the measures taken have avoided fragmentation in the dynamics of bond prices, particularly for sovereign bonds, to ensure the smooth functioning of the monetary policy transmission mechanisms. Now the situation has improved, and financial conditions are not as tight as they were only two months ago. That means that the measures we have taken have had a positive effect. We have avoided a credit crunch which, when the economy was plummeting in the midst of a public health crisis, would have had significantly adverse consequences.

Is "Whatever it takes" still the ECB's motto?

It was crucial in 2012. The crisis is different this time, and we have proven our determination by avoiding a squeeze on credit to the private sector and by improving financing conditions in general. Our commitment is unwavering. As is clear from our communication, we stand ready to recalibrate our non-standard measures and pandemic programmes – such as the pandemic emergency purchase programme (PEPP) – so that they can be adapted to suit the circumstances. The last time we did this was at the beginning of June when we increased volumes and extended the horizon.

Are you ready for a second wave of the virus?

I am not a virologist, but as a central banker, I know that we must prepare for the worst while hoping for the best. A second wave is a distinct

possibility.

And if it comes?

Monetary policy is not the only tool we have. National fiscal policy has been the first line of defence this time around. It has worked well, but the reaction has been asymmetric because the same measure cannot be applied everywhere and not all countries have the same amount of fiscal space. That's why I believe that a pan-European fiscal response is important to avoid what I mentioned earlier, i.e. a two-speed recovery. That's why we need to complete monetary union, and have a genuine banking union, a single capital market and a common budgetary instrument.

The measures you have taken have suffered a blow following the ruling of the German Federal Constitutional Court. How do you feel about that?

I don't want to comment on the rulings made by the national courts. It is important to remember that the ECB falls under the jurisdiction of the European Court of Justice. We are a European institution. We are accountable to the European Parliament and, from an operational standpoint, we are subject to scrutiny by the European Court of Auditors. We do not answer to the national courts, but only to EU bodies. That said, through the Bundesbank, documents that explain the suitability of our actions were provided to German institutions. This happened already in the past. We have decided to cooperate while at all times respecting the principle of the ECB's full independence.

A principle for which, when the EU treaties were being drafted, the Germans fought tooth and nail.

That's exactly right. I don't think anyone can disagree.

What would a two-speed recovery mean for Italy?

For Italy, the problem is primarily related to growth, which was already close to zero before the coronavirus. It's a question of productivity, competitiveness and structural reforms that are still to be completed. In this phase of the crisis, national fiscal policies have to be expansionary. In the short term there is no alternative but to spend. But once the emergency is behind us, all countries with high debt levels – not just Italy – must resume their efforts to address the problem of medium-term sustainability and compliance with the parameters set by the EU.

The ECB has been criticised for being too "pro-Italy". It has been said by the "frugal" countries that you helped Rome to not implement reforms.

I have no objections to being described as "pro-Italy" because it would mean being "pro-Europe". I am pro-Italy, or pro-France, or pro-Spain, I am also pro-Germany. We are all in the same boat.

From the perspective of a politician, do you envisage or do you fear that there will be social tensions when the pandemic is over?

When I was a minister I was called a “technocrat” and now I am being asked to speak as a “politician”! That’s life. But, now seriously, this crisis will leave scars and we must minimise the potential damage. This calls for major action in terms of fiscal policy. The new reality will be more complex because GDP will fall significantly and there will be an impact on employment and on standards of living for Europeans. The main antidote will not be monetary policy – which of course we will conduct being mindful that we are not almighty – but reforms and fiscal measures by governments. In our work, we will also aim to reduce the effects on inequalities.

Let’s talk about the banks. You have avoided a credit crunch. But the banks have been criticised for being slow to provide liquidity to firms.

The banks are not to blame in this crisis, and they should be part of the solution. The shock has created uncertainty and the fear of a financial market crash. The need to avoid a credit crunch required the combination of two factors: ensuring that liquidity reaches banks, which we have done, and activating the public guarantee schemes that are necessary to channel funds to firms. At the start there were actually many doubts as well as bureaucratic problems. It was not an easy task. Now, however, the national guarantees have started to operate. Liquidity is flowing. We have avoided the worst.

The return of the virus could cause an explosion in banks’ non-performing loans (NPLs).

According to staff analysis, government loan guarantee schemes, if fully deployed, could transfer about 30% of losses from banks to the public sector, on average across euro area countries. The impact of NPLs would be reduced, even if NPLs are set to rise. Bank profitability is very low and will be further dented by the crisis. A first measure to support the banking sector would be completion of the banking union with the approval of the missing third pillar, namely the common European deposit insurance scheme (EDIS). This would provide reassurance for citizens, savers and markets. I hope it can be achieved soon.

Do you believe that the capital requirements for banks need to be increased?

In this temporary emergency, things are moving in the opposite direction. The ECB has temporarily eased the capital requirements for banks, which were in a better position at the start of this crisis than they were for the previous crisis. We ask this flexibility to be used to grant loans and to avoid a credit crunch. The more solid capital position must be used, in conjunction with the buffers, to support the economy.

Are there too many banks? Should there be some consolidation?

Banks should address the issue of low profitability which, for the European banking system, is extremely contained and will suffer from the effects of the crisis. They should double or triple efforts to cut costs, make structural changes and increase efficiency. This process in many cases would ultimately require consolidation, which will be key at the national level for

small and medium-sized credit institutions, but also at the European level for larger credit institutions.

There is talk of a bad bank for NPLs. What do you think of that?

The priorities need to be clear. The first is to complete the banking union with the third pillar. Reopening and concluding the debate on EDIS would send a very strong signal. Other solutions can then be considered. When I was Minister for the Economy in Spain, a bad bank was shown to be a valid tool. But there are other things to do first. Having this discussion now is premature.

Looking ahead, do you subscribe to the notion of the “new normal” when the pandemic is over?

I don't like talking about a “new normal”. Normal is normal. There's the new and the old. I prefer to think of a new reality. We have learned a lot from the threat of the virus and its consequences for globalisation. I am in favour of globalisation, but it has its pros and cons, particularly because a pandemic can now spread more rapidly. We have learned the importance of the role of the healthcare system, that the world economy was not prepared for lockdown and that the security of the global supply chain needs to be considered. I hope that a vaccine will soon be found. It will be a more digital world, which will bring advantages but will also have an impact on inequalities. Europe will have a competitive advantage in terms of combatting the climate emergency. All in all, we will have a “new reality” rather than a “new normal”, which I hope will be as close as possible to the “old normal”.

What have you missed the most during lockdown?

The most novel experience was not meeting up with friends. I missed football and Atlético de Madrid. But above all I missed my two grandchildren.