1-002

COMMITTEE ON ECONOMIC AND MONETARY AFFAIRS

MONETARY DIALOGUE WITH MR JEAN-CLAUDE TRICHET, PRESIDENT OF THE ECB (pursuant to Article 113(3) of the EC Treaty)

BRUSSELS, MONDAY 8 DECEMBER 2008

1-003

IN THE CHAIR: MRS BERÈS

(The meeting was opened at 4.30 p.m.)

1-004-000

Chairman. – Mr Trichet, I declare open this meeting of the Committee on Economic and Monetary Affairs and this monetary dialogue.

This hearing is taking place promptly because, as you know, the members of the Committee on Economic and Monetary Affairs like to meet you as soon as possible after a European Central Bank decision. Many observers have described the decision taken by the European Central Bank last Thursday as historic. I believe that this will form one of the important points of our dialogue today, in addition to the two issues that we have asked you to speak about, as is common practice.

We understand why the start of this meeting had to be delayed and you are therefore forgiven. The format of our meeting will simply have to be adapted slightly. As we already have plans to meet you in Frankfurt next Monday, when the Committee on Economic and Monetary Affairs will make its annual visit to meet members of the Executive Board, we have decided that the part which should today have been *in camera* will be postponed until our debate in Frankfurt.

Without further ado, and thanking you in advance for adapting to a slightly different format given the circumstances, I give you the floor for an introductory speech which should, on this occasion, really be quite short to allow the maximum number of members to speak according to our rules.

1-005-000

Jean-Claude Trichet, *President of the European Central Bank. – (FR)* Thank you very much, Madam Chairman. Thank you for forgiving my late arrival which was due to fog in Frankfurt. We had to wait two hours for the plane to take off.

Members of the Committee on Economic and Monetary Affairs, I am delighted to be having this fourth meeting with your committee this year. I shall begin with a very quick assessment of the economic and monetary situation, followed by an explanation of the reasons underlying our interest rate decisions. I shall also provide some very brief information on our monetary policy operations.

1-006-000

(DE) In conclusion, I would like to look at the management of the financial crisis in Europe and highlight some of the proposed reforms to the international financial system which I believe are particularly important. After that I will be happy, as always, to answer your questions.

1-007-000

Since my previous hearing before your committee on 10 September, euro-area annual inflation has continued to decline, falling to 2.1% in November. With lower commodity prices and weakening demand, annual inflation is expected to be in line with price stability over the policy-relevant horizon.

Turning to economic developments since September, there has been an intensification and broadening of the financial turmoil, contributing in the third quarter to a contraction of 0.2% in real GDP growth compared to the previous quarter. Global economic weakness and very sluggish domestic demand can be expected to persist in the last quarter of 2008 and in the next few quarters. Subsequently, a recovery should gradually take place, supported by the fall in commodity prices and assuming that the external environment improves and financial tensions weaken.

As a whole, average growth in 2009 could be between -1% and 0%, according to Eurosystem staff. This outlook remains surrounded by exceptionally high uncertainty. Risks to economic growth lie on the downside, relating to concerns for a stronger impact on the real economy of the ongoing financial turmoil, protectionism and possible disorderly developments owing to global imbalances. Estimates of underlying broad money growth point to a sustained, but moderating, rate of expansion. This supports the view that inflationary pressures are diminishing further with some risks remaining on the upside in the medium to longer term.

On 4 December we decided to reduce the key ECB interest rates by 75 basis points, putting the overall reduction of our key interest rates at 175 basis points in less than two months. We will continue to keep inflation expectations firmly anchored in line with price stability, thereby supporting sustainable growth and employment and contributing to financial stability.

I will very rapidly give an overview of recent monetary policy operations and the Eurosystem's collateral framework, which was one of the issues you wanted to address. In view of the intensification of money market tensions, the Eurosystem stepped up its efforts to ensure that solvent banks continued to have access to liquidity.

Most notably, we decided to supply liquidity on an unlimited basis and at a fixed rate. In addition, we intensified our close cooperation with other central banks, in particular with the Federal Reserve. I am, of course, ready to respond to all your questions on this particular issue.

Let me turn to the management of the financial crisis, on which the panel of experts have prepared studies. The market turmoil has heightened the importance of addressing financial challenges in a comprehensive and coordinated manner, both globally and at European level. In the context of the increase in cross-border activities of financial institutions, coordination is particularly important, given that the institutional setting for financial stability remains predominantly based on national competences. As regards the measures to render the financial system more resilient in future, I commend the work which is being pursued at the global level by the Financial Stability Forum and the G20 and at the European level by the Ecofin Council.

I would like to emphasise five strands of work which I consider particularly important. Firstly, financial institutions must improve their risk-management systems in all areas, particularly in those such as securitisation and liquidity risk where the crisis has highlighted grave shortcomings. In this context, we welcome the strengthening of the prudential framework, as envisaged in the current revision of the Capital Requirements Directive.

Secondly, financial institutions should avoid excessive short-termism in their behaviour, which tends to place undue emphasis on returns over risks. To that end, a number of improvements are necessary, including specific guidance by supervisors on internal compensation schemes.
Thirdly, transparency should be enhanced in all respects, including all financial institutions, opaque financial instruments and markets such as OTC derivatives markets. With regard to the latter, I welcome the initiative to establish a central counterparty clearing for the CDS markets.

Fourthly, all the potential procyclical effects of the present functioning of the financial system, including the current regulatory framework and, in particular, the implication of the present prudential rules and accounting standards, need to be mitigated.

Finally, the supervision of cross-border financial institutions needs to be enhanced. To that end, the recent measures in the EU, including the compulsory establishment of colleges of supervisors for all cross-border banks, are particularly important.

As regards the future, I am sure that substantial improvements could be envisaged, in particular by the high-level group set up by the Commission which is gathering eminent personalities. Whatever proposals are made to enhance banking surveillance at a pan-European level, I would stress the importance of a very close relationship between central banks and banking surveillance authorities. This has always been the sentiment of the Governing Council of the ECB, and the most recent events have confirmed the pertinence of this view.

1-008-000
Chairman. – Thank you very much. Thank you also for having managed to limit your introductory speech. I do feel that, in this monetary dialogue, it is very important for you to hear the members and that was the only way to do it. I now give the floor to Mr Mitchell for one and a half minutes. You will appreciate that, on this occasion, you must not take any longer.

1-009-000
Gay Mitchell (PPE-DE). – I thank Mr Trichet, and I do realise that this is a time for cool heads, but nonetheless I think it is also a time for some accountability. The recent 0.75% reduction is very welcome, bringing the rate down to 2.5%, but compared with the Bank of England rates of 2% and the US Federal Reserve rate of 1% it still begs the question of whether at a time when inflation appears not to be threat, the Central Bank is being too cautious. Surely growth is now the issue, not inflation. Is it not time to look at what is happening in other banks and perhaps go one step further?

My second question is this: not all the rate cuts which the Central Bank is giving are being passed on to the consumer. Some banks are passing them on, some building societies are passing them on, but others are not passing them on. Some building societies and banks, seeing others not pass them on, are suggesting that they may not in future pass them on. They are claiming that the reason for this is the interbank rate. I do not know whether that is true or not true – it is a good shield to hide behind – but I would like to ask you the following question, Mr Trichet. You mentioned the relationship between central banks and surveillance authorities in Member States. Can you use your influence to try to bring down the interbank rates so that this cannot be used as an excuse, so that bankers themselves can return a certain amount of confidence to the market?

1-010-000
Jean-Claude Trichet, *President of the European Central Bank***. –** Each central bank in the world is doing what it deems appropriate, taking all things into account: the economy concerned, the features and characteristics of this economy, its flexibility, the shocks that it has to cope with. If I understood you correctly, you compared our present interest rates with the interest rates of, for instance, the Bank of England. Had you compared our interest rates with the interest rates of the Bank of England since the inception of the euro until very recently, you would have observed the contrary: we had lower rates than the Bank of England. I have never heard you say that we should increase our rates. I just want your confirmation that comparison is not a good reason. As we speak, we have some central banks with interest rates which differ from ours – some are higher, others are lower. I trust that they are all doing what is

appropriate, taking into account the full body of their responsibilities and their economies.

As regards the interbank rates, I have mentioned that we are providing liquidity in a way that is extraordinarily forthcoming. We have enlarged our collateral framework and have been extremely forthcoming again in providing liquidity at fixed rates and on an unlimited basis, in particular to permit the most appropriate functioning of the interbank market and especially to gradually decrease the spreads over the normal market rates without any counterparty risk that currently make up the Euribor rate. Again a large part of what we are doing in refinancing the commercial banks is designed to permit the progressive diminishing of those rates that you mentioned.

I would agree with you that, as we speak, the rates on both sides of the Atlantic are too high, as indeed are the rates on both sides of the Channel. We are all doing what we can to get back to normal as regards the functioning of this particular market and the interbank market, and to reduce this so-called Euribor in the case of the euro, or Libor in the case of the US dollar.

1-011-000
José Manuel García-Margallo y Marfil (PPE-DE). – *(ES)* Madam Chairman, I am going to refrain from commenting on the interest rate issue as this has already been covered by Mr Mitchell. Instead, I am going to concentrate on the issue of injecting liquidity. There are two elements to this: collateral and maturities.

As regards collateral, new rules were announced on 4 September which will come into force on 1 February next year. These have been interpreted as tightening up bank funding conditions. I should like to know whether you agree with this assessment.

Secondly, although maturities have been extended, the financial institutions feel that they are still too short. Banks lend in the long term and therefore need funding in the long term. In other words, they need certainty about maturities. Strong complaints are being heard in the sector and I am conveying them here as best I can.

I should like to make a comment covering both these issues: tightening of collateral and possibility or not of extending maturities, bearing in mind that the latter also depend on collateral. Collateral had been specified for short-term loans but, if this can be changed, can we also see a change to allow long-term maturities?

1-012-000
Jean-Claude Trichet, *President of the European Central Bank***.** – These are, of course, very important questions. We have two duties in this domain. We have to allow the commercial banks to refinance themselves in an appropriate fashion and in a forthcoming fashion, taking into account the tensions that we are still observing on the markets in general and the money markets in particular. On the other hand, we also have to protect the integrity of the ECB as an institution and be cautious in terms of risk management ourselves.

That is the reason why we took a number of decisions on 4 September which were aimed at improving the overall risk management of the Eurosystem. Having said that, we had an intensification of the crisis on 15 September, as you know, and, without jeopardising what we had done in terms of optimising our risk management, we have been even more forthcoming since the intensification of the crisis than we were before, particularly by accepting a triple-A paper, which we did not do before.

You can be sure that we will continue to be as keen as possible to be forthcoming as regards the collateral framework for as long as we have these exceptional tensions that are observed on the market, and to attend to our own risk management, which is a duty that we have vis-à-vis all the owners of the Eurosystem institution, namely the taxpayers themselves.

1-013-000
José Manuel García-Margallo y Marfil (PPE-DE). – The second part of my question was not answered.

1-014-000
(ES) I also asked you about the possibility of extending loan maturities, from six months to a longer term. I did not just ask you about collateral.
The European Central Bank began by lending in one-day operations. It then extended loan maturities. What I am now asking you is whether even longer maturities are possible to meet the funding needs of financial institutions.

1-015-000
Jean-Claude Trichet, *President of the European Central Bank***.** – If you are asking me whether it is our intention to continue to refinance the commercial banks, not only on a weekly basis but also on a one-month, three-month and six-month basis as done at present, then we have no intention of interrupting that at this moment. As you know, it is for all those maturities that we have a supply of liquidity which is unlimited and at a fixed rate.

1-016-000
John Purvis (PPE-DE). – Mr Trichet, following on from that, you say that you must concern yourself essentially with the value of the collateral you are taking in. How do you keep an eye on the valuations of this triple-A mortgage paper that you are holding for three months maybe? How do you keep track of that? Is there a balance sheet at the bank that we could possibly have a look at to see just how much risk you are taking?

1-017-000
Jean-Claude Trichet, *President of the European Central Bank***.** – As you know, we have enlarged our collateral framework, as have all the central banks in the world. As a matter of fact, we were the first to be able to accept private papers. Since the inception of the euro our own rule has been that we could accept private papers, which was not the case on the other side of the Atlantic. Now practically all central banks – and in particular all European central banks and the US Fed – have progressively enlarged their collateral. We did the same

ourselves because not only have we accepted a private paper but, as I said a moment ago, we have gone down to a triple-B paper. So we have considerably enlarged our collateral framework. We have a systematic methodology to assess what is appropriate as regards the value of the guarantees that we have, with a view to taking the appropriate value. Inside the Eurosystem, there are therefore systematic methodologies to assess the value of the various papers concerned and to have the appropriate 'haircut' where and when needed. This is extremely important, and of course all the more important when you are dealing with very illiquid markets, which is unfortunately the case for a large grouping of securities, as everybody knows, because part of the difficulties we face is that some of these markets are illiquid.

1-018-000
John Purvis (PPE-DE). – Well yes, and we are still not seeing the improvement that we would like to see coming through. If the situation got even more difficult, if the money was not passing through the banks into the real economy, if we were faced with a major economic crisis – as we essentially already are – could you envisage any circumstance where the Central Bank would accept guarantees from the Member States, for example, or from sovereign governments, or would that infringe your independence?

1-019-000
Jean-Claude Trichet, *President of the European Central Bank.* – I would say that we have several different issues there. One issue is, what do you do when the refinancing is not normal but is a case of emergency liquidity assistance, namely for an institution which is solvent but has exceptional liquidity problems and these liquidity problems make it impossible to apply the normal rules? In other words, if they do not have sufficient collateral eligible for our refinancing operations to present to the Eurosystem, then we can envisage providing emergency liquidity assistance in exceptional circumstances on top of the other eligible collateral that would be presented. I would not rule out, in such cases, that the national central bank concerned could have government guarantees in order to permit this emergency liquidity assistance, provided this really is a liquidity problem and not a solvency problem. If it is a solvency problem, then we are in a different environment.

As regards other papers that would possibly be eligible for our refinancing, if a particular bank presents to us a particular paper which has been issued by a bank and is guaranteed by the government – all governments now have schemes which permit them to guarantee papers from three months to five years in the overall system that has been put in place in Europe as a defence against the systemic solvency problems that we have at present – then that paper would normally be eligible.

1-020-000
Donata Gottardi (PSE). – *(IT)* Mr President, I would like to begin with one of the points you made, and one on which I think we are in total agreement, namely, the fact that greater coordination is needed but that there is the problem of national jurisdictions, meaning precisely that coordinated and one-way anti-cyclical policies need to be put forward that are not just a combination of national plans.

I believe we must then reflect on the change in the role of the Central Bank in terms of what has been its chief concern up to now: that is, price stability and controlling inflation, and hence also through the treaties. It was in this way that socio-economic policies were supported and purchasing power protected. It is now clear that, in this changed scenario, we must ask ourselves what the job of the European Central Bank should be.

I also believe that we can agree on the fact that this may be an opportunity to reconsider the development model, too, to avoid cuts solely in the commitments of expenditure on general services, and to really try to assess the impact, on an estimated and on an actual cost basis, on public finances, which should be of a high quality where macroeconomic objectives are concerned.

Therefore, if this is the context, what can we do to ensure that the crisis in the financial system does not give rise to negative impacts in terms of employment and that the resources exhausted during this period do not drive small and medium-sized enterprises out of the market?

One of the points has already been dealt with, so I will only briefly mention interest rates and the decisions of the central banks, but you have already given a response on this matter…

(The President cut off the speaker)

How can we aspire to coordinate public investment policies, do we employ an instrument, for example, like the Eurobond? What are the expectations of the Central Bank with regard to this idea of coordinated financing of investments?

1-021-000
Jean-Claude Trichet, *President of the European Central Bank.* – We have engaged in these extraordinary measures – the supply of liquidity on an unlimited basis for refinancing on a one-week, one-month, three-month, six-month basis – and engaged in a collateral framework which is much more forthcoming with the idea that this is what the real economy – small businesses, medium-sized businesses, the whole productive sector, the banking sector – needs in order to be as active as possible. We have done all that precisely with a view to making the banking sector capable of providing the services that the real economy expects.

When the governments themselves decided on these exceptional guarantees and embarked on this exceptional recapitalisation, they had exactly the same ideas. It is very important that we not only protect the banking sector from very serious difficulties – which was clearly the case after 15 September – but that we enable the

system to function on a more normal basis as soon as possible. You can interpret all that we have been doing in this respect from that angle.

1-022-000
Elisa Ferreira (PSE). – *(PT)* My first question is: what is your view on the situation of countries that are apparently interested in belonging to the Eurogroup without belonging to the European Union, as is the case with Iceland? Is that possible? What is your opinion on this?

My second question is: I welcome all the recent actions of the European Central Bank but, in concrete terms, how can we get this liquidity into the real economy? This is a fundamental issue. Is it in the hands of the governments, commercial banks, the European Central Bank or the Commission? How can we resolve this issue?

My third question is: the relationship between the real economy and monetary policy has not worked well in the medium term. Events have happened that we were not expecting to happen. How can we improve this relationship in the future so that there is convergence and a better link between inflation control and economic growth? Will this crisis make us think about a new way of interpreting the monetary policy mandate?

1-023-000
Jean-Claude Trichet, *President of the European Central Bank***. –** I will respond to your questions in the order they were asked. With regard to countries and economies that are not in the euro zone or in the European Union, as far as we are concerned we would apply the legal framework, so I have nothing to say about that. However, when Europeans decide that a country becomes a Member of the European Union, it is subject to the Maastricht Treaty and we will treat the process as we are asked to by the European democracies. I have, however, no particular view on any country which is not a member of the European Union.

On the second question, as I have already said – and I would agree on the importance of this question – everything we ourselves have done and continue to do every day, and that the governments have done, is aimed at allowing the banking sector to function as correctly as possible. This is not only to prevent the banking sector facing a crisis situation – as would otherwise have been the case after 15 September – but also to allow it to finance the real economy as normally as possible. Let us not forget that in a market economy it is, of course the duty of the banks to determine good risk and bad risk, and we cannot ask them not to assess their risks at all whilst reproaching them for having taken too many risks in the past. This is a rule we have to respect in a market economy. The risks are assessed by commercial banks. Having said that, it is absolutely clear that everything we are doing at the ECB is precisely with the aim of allowing banks to have a normal attitude vis-à-vis the real economy.

As regards our duty and the mandate that we have received from the European democracies, we really trust – as I think has been demonstrated in the most recent past – that by being a solid anchor of stability and confidence and by solidly anchoring expectations, and particularly price stability in line with our definition of less than two but close to two, as I always say, then we are paving the way in various circumstances. We are experiencing very difficult circumstances at a global level, but we are paving the way for functioning as smoothly as possible with the real economy behaving as well as possible under the circumstances. I must say, however, that even without the financial crisis, we would have had a slowing-down in the economy after long years of very active growth at a global level and after having had to cope with the oil shocks that had a very powerful depressive effect on every economy in the world. In addition, of course, we have had to cope with exceptional tensions in the financial sphere.

1-024-000
Wolf Klinz (ALDE). – *(DE)* Madam President, Mr President, in recent weeks, amounts in the billions have come out of circulation in the new Member States in Central and Eastern Europe. I would be interested to know whether you think that there is a high risk of these markets drying up and to find out about the crisis and liquidity management measures being taken in cooperation between the European Central Bank and the central banks of these countries.

One further question: The Member States have reacted differently to the crisis in many areas. Are you satisfied with the approaches which the Member States have taken or do you believe that they may lead to distortions of competition and that there is a risk that the Member States, including those in the euro zone, will tend to drift apart rather than converging?

1-025-000
Jean-Claude Trichet, *President of the European Central Bank***. –** You are absolutely right that one of the consequences of the financial turbulence we are experiencing is that capital has a tendency to go back to its headquarters, its location. This is true at global level, it is true for capital that runs in dollars in particular the world over, it is true for all kinds of capital and it is true for the emerging world in general.

Since the mid-September events in particular, we have seen to what extent the emerging world, which had been privileged because of its great resilience up until then, has started to become less resilient. This is true for the new countries. They have to be very keen on coping with the difficult situation and we have to be aware of that.

The second question you asked related to inside the euro area. As regards guarantees and recapitalisation, which are two major decisions that have been taken by all governments, the rules that have been – or are being – accepted by the Commission, and on which we ourselves have worked, are to ensure that we have a level playing field seen from our own standpoint of the good

functioning of the single market with a single currency. This all seems to me from the present information – even if the Commission has not taken a final decision on recapitalisation – to be a good way of allowing the system for which we are responsible to function as correctly as possible.

I think it was really exceptional that Europeans were able to work out these appropriate concepts on a pan-European basis. It has been done for the guarantees. It will be done very soon I am sure for recapitalisation. We ourselves have worked very actively in this domain.

As regards fiscal policies, our view has always been that you first have to respect the Stability and Growth Pact which is the rule of the game in the euro area and which is the quid pro quo for the fact that we do not have a federal government and a federal budget. That is extremely important for confidence in the euro area as a whole. Having said that, some countries have room for manoeuvre, others do not have much room for manoeuvre and others none at all, so each country has to do what is appropriate in its own circumstances. We know that if we do not respect that, not only will we fail to respect the Stability and Growth Pact, but we would take risks as regards two important effects.

One concerns the spreads we are observing. You can refinance, but if you refinance additional spending with a high additional cost, then you are not better off: on the contrary. That is something that we must bear in mind.

There is also what I would call the 'Ricardian effect'. If you are with economic agents who are already afraid because your own fiscal position is not very good, and your fiscal position deteriorates, then you might have an effect on confidence which would be very bad, and obviously you can lose more than you gain with the additional spending. There are very sound financial and economic reasons that would back the common sense I was expressing, so each particular country has room for manoeuvre and must act, taking into account its own level of room for manoeuvre. That is not bad: it is good.

1-026-000

Alain Lipietz (Verts/ALE). – *(FR)* Mr Trichet, I should like to thank you for coming here today and for your explanations.

I am not entirely convinced by what you said about Iceland. Iceland straightaway asked France and Germany for help, before turning to the International Monetary Fund. France and Germany refused saying that it was a European matter. Iceland then turned to Russia and immediately obtained the money. In my opinion, it is not very wise to have placed Iceland in Russia's grasp or to have brought Iceland closer to Russia. I feel that we should now be regarding Europe as an economic power and not simply respond, somewhat formally, as you have done.

The second problem, which forms the crux of my question, concerns this history of liquidity. I have been struggling to understand the difference between liquidity and solvency when the fair value is the market value. Obviously I am aware that you have models for determining the value of securities, but as these are unknown, we are not really clear on what part the market value plays in these. I interpret the development of your policy since September as follows: firstly, 'accounting risk' securities were expanded in order to inject liquidity. Now, the talk is about 'BB-' ratings. Do you not think that, in the long term, different selection criteria need to be used? For example, should we not decide that securities from the European Investment Bank, based on the EU's priority investments, such as the application of Kyoto and post-Kyoto, are much more eligible than others, instead of using the decreasing order of solvency indicated by rating agencies?

1-027-000

Jean-Claude Trichet, *President of the European Central Bank.* – *(FR)* As regards your first question, I must once again give the European Central Bank's answer. We must abide by the relevant Treaty. Clearly, no one expects us not to do that and we cannot, given the Treaty, not differentiate between countries that are in the European Union and those that are not. The countries that are in the European Union, but not in the euro, are members of the Governing Council of the European Central Bank. We have a relationship with them, and some of them, only two in fact, have an opt-out clause. All the others have made a legal undertaking to one day join the euro area and we must prepare for that as professionally as possible. We are therefore faced with very different situations. Obviously I cannot give an opinion on your comment as to what Member States of the European Union should do in certain cases of countries that are not members. There is Iceland, but of course there are also many others.

As regards your interpretation of what we have done, I must say that you seem to have interpreted what all the world's central banks have done, faced with circumstances that are absolutely exceptional and now seem to be persisting, in that they have been forced to expand their guarantee systems. We have done this ourselves, even though we had a guarantee system that was much more open than that of the United States, for example, with whom we often tend to compare ourselves. However, the United States have made good progress, if I may say so, in terms of the eligibility of their guarantees.

It is also true that, since 15 September, all the central banks of the industrialised countries have been forced to take additional decisions given the fact that tension on the markets, particularly the money markets, has been running exceptionally high.

As regards your final point, I would say that our duty is to accurately assess the quality level of the various papers put before us and to do so as objectively as possible. As a result, when we are faced with papers that seem to us to be of very good quality, we can accept them much more willingly at their face value, with very

limited discounts. If we are faced with papers that seem to us to be less solid, obviously we are forced to make what we call 'haircuts' in economic jargon, and that is what we are doing. I cannot say more than that because that is the rule and we do not differentiate according to our judgement of the quality of signatures. We differentiate according to what we consider to be in the interests of the European Central Bank and the Eurosystem as a whole, given that this concerns all the national central banks in the Eurosystem.

1-028-000

Guntars Krasts (UEN). – The measures taken to tackle the current crisis, such as interest rate cuts and the easing of collateral lending requirements which are Central Bank activities, could well bring us to the next crisis, or plant the seeds of the next crisis. One area where fear really persists is asset inflation which shows its dangerous economic character at very regular intervals. In line with all the other central bankers, you have refused to couple responsibility for monitoring an asset crisis with responsibility to take action in the event of an asset bubble. What is your position now?

I have another short question. Why has the dollar been strengthening against the euro despite the spread in interest rates? Is it, perhaps, the market's reaction and expectations concerning the inability of European policy-makers to make the right decisions, or is it positive thinking about American policy-makers?

1-029-000

Jean-Claude Trichet, *President of the European Central Bank***. –** Regarding the first question, it is true that all the central banks I know in the world are saying it is their primary mandate and duty – whether they are targeting inflation or whether they have a definition of price stability as we have – to deliver price stability as measured by the Consumer Price Index (CPI). No central bank in the world would say that it was targeting asset prices. For a very large number of reasons, we do not think that it would be reasonable to take this path, but we have a concept of monetary policy which is based on two pillars: an economic analysis on the one hand and a monetary analysis on the other.

The economic analysis looks very much like what you would do if you were targeting inflation. Monetary analysis is the strong tradition of the central banks that created the ECB, the fathers and mothers of the ECB. This examination of the evolution of monetary aggregates, their components and counterparts compels you to take into account the evolution of credit. The fact that credit would gallop is something we would interpret as being dangerous for price stability in the medium-to-long term – even very long term – and which also has an impact on asset inflation. So, in a way, our own monetary policy concept is one which presents aspects that permit us to lean against the wind in some respects. Even if we say – and I am very attached to this idea – that we are looking at the risk to price stability on a medium-term, long-term, and even very long-term basis, your question is extremely pertinent, particularly after what we have observed.

All my colleagues and I have to be as accommodating as possible. This has been my experience. With the benefit of hindsight, from time to time, those who were always calling for the central banks to be accommodating might say that they are perhaps happier to have central banks which are able to consider the medium and long term because, when a bubble bursts, this is of course not good at all.

Having said that, I think your question is very important. I will not comment on the exchange market. As you know, we are in a floating exchange system, and I do not think that the two reasons you mentioned would be appropriate in the present circumstances for obvious reasons. It is not an overall judgement of the various economies which is at stake, but I will not comment any more on that.

1-030-000

Cornelis Visser (PPE-DE). – My question concerns the Growth and Stability Pact. We have already addressed it. There is pressure on governments to increase their budgets and budget deficits. The Dutch Minister for Finance has said that there should be a limit of 3.5% for the budget deficit. Could you indicate what would be the preference of the European Central Bank in this respect? What would be best? You have already mentioned the long-term perspective and that it might be bad to increase your budget at this stage because in the longer run it will be a disadvantage for the economy, but what would be your recommendation?

1-031-000

Jean-Claude Trichet, *President of the European Central Bank***. –** This is a very important question. As I mentioned, you have the recommendations of the Stability and Growth Pact, the rules of the Stability and Growth Pact, and then there are the indications you get from the financial markets on the one hand and from your own people on the other. That is a judgement that very much depends on the situations of the various countries concerned.

I would be very cautious in mentioning the fact that there is a general rule. Having said that, the Commission itself has very important responsibilities, and one of those responsibilities is to see and judge when to start an excessive-deficit procedure. That is my understanding, but again this is the responsibility of the Commission.

As you know, we in the ECB are calling on governments to be as wise as possible, as sound as possible, in this domain, for obvious reasons. If I remember correctly, the Commission said it would start an excessive-deficit procedure, taking into account the various criteria that exist in the present framework of the Stability and Growth Pact, and that an excessive-deficit procedure would certainly be started over 3.5%. It is perhaps for that reason that your government has decided that it should not go over and above the threshold.

1-032-000

Antolín Sánchez Presedo (PSE). – *(ES)* I particularly want to mention the institutional aspects of the current crisis.

The current institutional system is actually very complex and it is clear that it has not enjoyed much success in preventing the crisis.

As regards the management of the crisis, I have read comments made by some experts who say that the European Central Bank should have been much more active in terms of liquidity and that, if it had been, we might have avoided certain actions being taken by Member States which have proved to be quite disjointed.

It is probably a question of being flexible, but not too much: on occasions reducing the collateral requirements which can create a moral risk, and on others being flexible as regards volume and maturities.

The third institutional aspect is supervision. The European Parliament has adopted a report and, in line with those aspects of the Lamfalussy approach, has set up a working group on supervision. Some experts consider that countries in which the banks are supervised by the central banks have functioned better than those in which this is not the case.

I should like to know what you think the role of the European Central Bank should be in the future supervision system, whether it should guarantee financial stability and how it can work with other authorities which, in my opinion, should be integrated European authorities and not simply based on cooperation agreements.

1-033-000

Jean-Claude Trichet, *President of the European Central Bank***. –** Concerning the first question as regards the ECB, I have never seen any analysis telling us that we did not take sufficient action with regard to the provision of liquidity. As I have already said, this committee knows that better than anybody because we have been in touch since the very beginning of the financial crisis. I came here, at your request, on 11 September 2007. At that time, I explained what we had done on 9 August and since then. We have been very active. We were the first central bank in the world to judge that we were in exceptional circumstances and that what we had in front of us was very important and should not be neglected. With our collateral framework, we were also quite well-equipped from the very beginning to cope with this exceptional situation. As I said, as time went by we had to improve our collateral framework to take new decisions after 15 September of this year. To sum up, we have been active since the very beginning and have assumed our responsibilities in circumstances that really were absolutely exceptional.

Regarding supervision, the position of the Governing Council of the ECB has always been that we believed a very close link was needed between national law, the central bank constituency in general, the ECB and the Eurosystem as a whole, and banking supervision. We were not in favour of a strict separation between the two and on that particular point were very much in agreement with the United States. All that has been observed since the beginning of the tensions seems to confirm that it is good that there is a very close relationship between central banks and banking supervision. So we are taking that line and continue to follow that line very firmly.

There has been some work done by the European Parliament and I remember having to respond to a question on that particular point in a previous meeting with you. A new high-level group has been set up by the Commission to look into what kind of improvements could be brought about. We stand ready, and I myself will have an opportunity to be in contact with this high-level group in order to see what we can do. I would say that there is certainly room for improvement, particularly to make sure that we have good coordination in Europe as a whole, and particularly in the euro area itself. For those institutions that are cross-border, we stand ready to participate in improvements.

1-034-000

Chairman. – Thank you, Mr Trichet. I believe that we will have occasion to return to that issue because you have ended on exactly the same point that we reached during the previous hearing. I feel that Mr Sánchez Presedo's question was aimed at finding out what you meant when you said: 'We stand ready.' 'Ready for what?' was, I believe, the question which members would have liked you to answer, but we will have other opportunities to return to that issue.

In that regard, I imagine that our meeting in Frankfurt will provide an opportunity to return to some of the issues raised by members. As a result, intuitively going beyond Mr Sánchez Presedo's question, there are at least three issues that I would imagine members would be keen to hear answers on, particularly the issue of the valuation of collateral. You said that 'we have a systematic methodology'. What is that methodology? What is its degree of transparency? This is an issue now being debated publicly and on which we are being questioned very directly. We will need to return to this in Frankfurt.

As regards the issue of sending signals on monetary policy to the banking system itself, this is an issue that was raised in discussions between us before the crisis. I feel that all the questions that were asked at the time have been somewhat exacerbated by the crisis, particularly when you compare how signals on monetary policy are sent to the banking networks here and in the United States. On that point, I feel that we really must go further into the detail of the issue.

The question from Mr Lipietz as to whether, beyond the European Central Bank logic, the qualification of eligible collateral could contribute to a clearer European strategy, is one to which I imagine that members will also want to return.

We will have this opportunity next Monday, in Frankfurt, when we hope that no one will be delayed by a plane, the snow or a pilot who injures his head. In any event, we will return here on 21 January for our next monetary dialogue.

(The meeting was closed at 5.35 p.m.)