COMMITTEE ON ECONOMIC AND MONETARY AFFAIRS
MONETARY DIALOGUE WITH JEAN-CLAUDE TRICHET,
PRESIDENT OF THE ECB
(pursuant to Article 113(3) of the EC Treaty)
BRUSSELS, WEDNESDAY, 21 JUNE 2006

3-003

IN THE CHAIR: MRS BÉRÈS
President

(The meeting was opened at 9 35a.m.)

3-004
Chairman. – Ladies and gentlemen, I should like to start on the work of this monetary dialogue meeting.

Mr Trichet, President of the European Central Bank, welcome to this Chamber and to a meeting of the Committee on Economic and Monetary Affairs.

At the time of our previous meeting on 20 February 2006, you will recall that we had a meeting with the national parliaments at which we talked about the conditions for growth in the euro zone. This time we are asking you first to answer two questions. The first is about the procedure for nomination to the European Central Bank, because, as you know, this Committee had opinions to express about the most recent appointment to the Executive Board, Mr Jurgen Starck, whose portfolio was awarded under conditions which perhaps you will explain to us; the second subject which we have chosen for discussion today concerns the number of the Central Bank's objectives and how it decides which to prioritise.

That will no doubt give you the opportunity to tell us a little about your frame of mind and the way you reacted to the initiatives of the other Jean-Claude, Jean-Claude Juncker. Mr Juncker and the Commissioner, Mr Almunia, have in fact written to you, and Mr Juncker told us the essence of this correspondence at the time of our last meeting with him on 20 May 2006, and we have read of your reactions to it in the press.

I believe that I understood in your presentation this morning that you wanted to be a little more explicit about the macroeconomic issues involved in monetary policy. I trust, accordingly, that you will explain how you intend to respond to this letter, and I am sure that will be one of the points about which my colleagues will want to question you later.

Without further delay, Mr Trichet, I give you the floor.

3-005
Jean-Claude Trichet, *ECB***. –** *(FR)* Thank you very much, Madam Chairman.

Ladies and gentlemen, I am delighted to appear before the members of the Committee on Economic and Monetary Affairs today, and to continue our regular dialogue.

These quarterly meetings are very important for the European Central Bank and, if you will allow me, I shall begin with an assessment of the economic and monetary situation.

(DE) I would then like to make a few comments on the contribution made by monetary policy to economic welfare and stability. To this end, I would again like to explain the basic principles of the ECB's monetary policy.

At the time of my last appearance before the European Parliament in February, I described how the available data at that time were in line with an assessment of a re-acceleration in economic growth in the euro area in the first months of 2006, and with a broadening of the expansion of economic activity. In addition, the cross-checking of our economic and monetary analyses underlined the prevalence of upside risks to price stability over the medium to longer term. I will now present to you our current assessment of how the economy and the outlook for price stability have evolved since February.

Starting with the economic analysis, the main indicators that have become available since the start of 2006 are positive, providing further evidence that the economy is evolving broadly in line with the scenario for economic developments that emerged at the end of 2005. According to Eurostat's first estimate, real GDP in the euro area grew in the first quarter of 2006 by 0.6% on a quarter-on-quarter basis. This compares, you will remember, with 0.3% in the last quarter of 2005, with domestic demand, including private consumption, making a significant contribution to higher real GDP growth. Our previous expectation of a re-acceleration of GDP growth in the first few months of 2006 has thus materialised, confirming

our assessment that economic growth is broadening and gradually becoming more sustained. This assessment is further confirmed by available information on economic activity in the second quarter, notably by the main confidence surveys and indicator-based estimates, which continue to provide encouraging signals on the evolution of the economic outlook.

Looking further ahead, the conditions and economic fundamentals are in place for growth in the euro area to remain close to its trend potential rate on a sustained basis. Economic growth in the euro area's main trading partners remains strong, providing support for euro area exports. Investment is expected to grow robustly, benefiting from favourable financing conditions, corporate balance sheet restructuring, and gains in earnings and business efficiency. Furthermore, we expect consumption growth to further strengthen gradually over time, in line with developments in real disposable income, as the labour market situation, and in particular employment growth, gradually improves.

This outlook for economic developments is also reflected in the June 2006 Eurosystem staff macroeconomic projections, which foresee average annual real GDP growth of between 1.8% and 2.4% in 2006, and between 1.3% and 2.3% in 2007. These projections for growth in 2006 are broadly unchanged from the ECB's previous staff projections of March 2006 and for 2007 the latest projections are slightly lower, mainly reflecting the recent rise in oil prices. The most recent forecasts by international organisations and private sector institutions also confirm a broadly similar picture.

In the view of the ECB's Governing Council, risks to the outlook for economic growth provided by these projections are broadly balanced over the shorter term, while, over the longer term, downside risks relate mainly to potential further oil price rises, a disorderly unwinding of global imbalances and protectionism.

Turning to price developments, according to Eurostat's flash estimate, annual HICP inflation increased further in May, to reach 2.5% from 2.4% in April, largely as a consequence of higher energy price developments. In the remainder of 2006 and in 2007, inflation rates are likely to remain elevated, with the precise levels depending mainly on future energy price developments. Meanwhile, the moderate evolution of labour costs in the euro area is expected to continue, notably reflecting ongoing global competitive pressures, particularly in the manufacturing sector. However, the indirect effects of past oil price increases are expected to have an upward effect on inflation in 2007, as already signalled by recently observed strong increases in industrial producer prices, which grew at an annual rate of 5.4% in April. The announced changes in indirect taxes will also have a bearing on inflation next year.

This outlook for inflation is also reflected in our own staff projections in June 2006, which foresee annual HICP inflation in a range between 2.1% and 2.5% in 2006, and between 1.6% and 2.8% in 2007. Compared with the March 2006 ECB staff projections, these ranges embody a slightly higher baseline profile for HICP inflation in 2006, largely reflecting the assumption of higher oil prices.

This outlook for price developments remains subject to upside risks including further increases in oil prices, a stronger pass-through of past oil price rises to consumer prices than currently anticipated, additional increases in administered prices and indirect taxes, and – more fundamentally – stronger than expected wage developments due to second-round effects of past oil price increases.

Turning to developments in monetary aggregates and credit, liquidity in the euro area remains ample by all reasonable measures. The annual growth rate of M3 increased to 8.8% in April 2006, from 8.5% in March 2006, supported by the robust expansion of its most liquid components. Credit growth has also remained very strong, with the annual rate of growth of loans to the private sector standing at double-digit levels.

The rapid rate of monetary growth continues to be driven mainly by the expansion of its most liquid components. Thus, the latest developments confirm that the stimulative impact of the low level of interest rates remains the dominant factor behind the current high trend rate of monetary expansion, which signals inflationary risks over the medium to longer term. The further acceleration of monetary and credit growth in this environment of already ample liquidity points to increased upside risks to price stability at longer horizons. Monetary developments therefore require careful monitoring, in particular in the context of continued strong dynamics in housing markets.

To sum up, annual HICP inflation rates are projected to remain elevated in 2006 and 2007, mainly as a consequence of upward pressures from high oil prices and indirect taxes. Risks to this outlook for inflation remain on the upside. Against the backdrop of strong monetary and credit growth and the ample liquidity situation, the cross-checking of the economic analysis with the monetary analysis confirms that upside risks to price stability over the medium to longer term prevail.

On 8 June 2006 the ECB's Governing Council increased the key ECB interest rates by 25 basis points, thus further adjusting its monetary policy stance after the interest rate increases in December 2005 and March 2006. By means of its timely further action, the Governing Council is helping to keep medium- and long-term inflation expectations at levels which are in line with price stability, thereby making an ongoing contribution to sustainable economic growth and job creation in the euro area. Notwithstanding the increase in key ECB interest rates on 8 June, our monetary policy in the euro area remains accommodative. It is essential to ensure that inflation expectations in the euro area remain firmly anchored at

levels in line with our definition of price stability. The firm anchoring of inflation expectations has permitted, inter alia, to maintain since the creation of the euro a low level of risk premia across the whole maturity spectrum, and to prevent costly wage-price spirals in the context of considerably higher oil prices. It is essential that this important asset of the euro area economy be preserved.

Let me now turn to the contribution of monetary policy to economic welfare and stability. Having explained the more specific and current reasons for the ECB's recent monetary policy moves, let me now put them in a broader perspective. As you know, the Treaty states that, without prejudice to the primary objective of price stability, the Eurosystem shall support the general economic policies in the Community, aiming at a high level of employment and sustainable and non-inflationary growth.

It is sometimes argued that the ECB's overriding focus on price stability implies that we do not pay sufficient attention to this latter part of our mandate; in other words, that in our policy we do not attach sufficient importance to growth, employment and the welfare of European citizens. I should like to elaborate a little on these particular issues and tell you why these assumptions, in our view, are misguided: price stability, and economic growth and employment, rather than being substitutes, are complements in a relationship which makes price stability a necessary condition for sustainable growth and job creation.

Price stability contributes to economic welfare and sustainable growth in many ways. An immediate way in which price stability contributes to welfare is by protecting the purchasing power of money, both for consumers and for savers. By protecting purchasing power, monetary policy also makes an important contribution to social cohesion, as the weakest groups of society are generally the least able to protect themselves against inflation. Moreover, inflation has the effect of transferring wealth from savers to debtors, as savers face a loss in the value of their assets, whereas the real value of debts diminishes as a result of inflation. Maintaining price stability prevents such arbitrary and unjust redistributions of wealth and income brought about by inflation.

Price stability also contributes to a better economic performance. Inflation undermines the proper functioning of markets, as the information deriving from price developments becomes blurred. Stable prices, on the other hand, enable markets to better allocate resources to their most efficient use, which enhances growth and employment. Very importantly, an environment of stable prices also *reduces* risk premia – I have already mentioned that – in medium- and long-term interest rates, as investors will not demand a high inflation risk premium to compensate them for their potential loss in purchasing power. This reduces real medium- and long-term market interest rates and increases the incentives to invest.

All these arguments show that price stability provides a substantial contribution to economic growth and social welfare. Yet, against the backdrop of relatively low growth rates in Europe, it is sometimes asked whether we could not achieve higher growth rates by accepting a somewhat higher rate of inflation. History has clearly shown, however, that growth and employment cannot be increased by inflating the economy by means of a loose monetary policy. This means that in the long run an increase in the quantity of money will only lead to an increase in prices. This implies that, in the long run, monetary policy can only, in that respect, influence the level of prices. The levels of real income and employment are ultimately determined by real factors. These include technological progress, productivity growth, the growth of the labour force and all structural aspects of the economy, such as the good functioning and flexibility of goods and labour markets, tax policies and the quality of education, which are all outside the realm of monetary policy. By maintaining price stability, monetary policy is providing the conditions for such real factors to work better.

The strong consensus among academics and policy-makers on the basic principles that I have just outlined has not always existed – some of us remember the time it did not exist. Forty years ago, there was a widespread view that monetary policy could durably raise the growth rate of the economy and that it could achieve permanently lower rates of unemployment by accepting higher inflation. This view was proven wrong by reality. The inflationary policies adopted in the 1970s to counter the effects of the oil price shocks did not succeed at all in reducing unemployment. On the contrary, these policies in fact only led to persistently higher inflation as well as unemployment. In addition, these policies also caused very large fluctuations in real activity.

By contrast, the recent oil price increases have had a limited effect on inflation and on output and unemployment. This has been the case because of the high credibility in Europe of the ECB in safeguarding price stability. Because of this high credibility, inflation expectations are now well anchored. Since the public has remained convinced that inflation will remain low in the long run, the energy price increases have not generated significant second-round effects on wages and prices. As a result, monetary policy has been able to maintain a more accommodative stance. This stance has been decisive in counteracting the negative effects of the oil price increases on the real economy.

Today, the insight that price stability is the primary goal for monetary policy has also been translated into the mandates of central banks of advanced economies and also of a very large number of emerging economies. It is the general case all over the world to give the central bank the primary goal of preserving price stability. It is the general case. It is certainly the case in all central banks and countries that have an inflation target in concept.

This also holds true for the US Fed. The mandate of the Fed is sometimes contrasted with that of the ECB, because it comprises not only a goal of price stability, but also the goals of maximum employment and moderate long-term interest rates. Although the Fed's mandate does not establish a hierarchy among these goals, the Fed has made clear on a number of occasions that it considers price stability as a necessary condition for and the best contribution of monetary policy to achieving the highest level of welfare and sustainable economic growth. The track record of the Fed in controlling inflation over the past decades speaks for itself. The successive Chairmen of the Fed have made clear that the Fed considers price stability not only as a goal but also as a means for the Fed policy to achieve its other statutory goals. This is very much in line with our own framework and with the thinking I have just explained to you.

To sum up, it is an error to think that a choice needs to be made between price stability on the one hand, and sustainable economic growth and welfare on the other. Price stability is both a precondition for and a means to enhance durable economic growth and welfare.

That being said, we should all be aware that, if price stability is a necessary condition, it is not a sufficient condition per se for sustainable economic growth and job creation. As I have pointed out before, the growth potential of the euro area economy is ultimately determined by its structural features. That is the reason why the ECB calls so often upon policy-makers to embark resolutely on the structural reforms of the Lisbon Strategy – I know that we are in line with the European Parliament on that particular point – and on the full completion of the internal market. Both would elevate the 'speed limit' of the euro area economy.

I am now ready to answer your questions.

3-008

Chairman. – Thank you, Mr Trichet. Our monetary dialogues continue and are similar but sometimes they change too.

They are similar when you emphasise price stability; they are similar when you consider that we have a shared objective in the implementation of the objectives of the Lisbon Strategy; but they also break new ground because this is the first time, I think, that Article 105 of our Treaty, which defines the objectives of monetary policy, has been referred to by the President of the European Central Bank, on his own initiative, and not by a colleague, in order to argue the merits of a sound balance for monetary policy

That is the way that the conditions of public debate evolve, I suppose.

I think that some of my colleagues will want to return to these different issues. I should like to begin the first round of questions. I wish first to greet a large group of visitors and now I shall give the floor to our coordinator, Mr Alexander Radwan, for a minute and a half.

3-009

Alexander Radwan (PPE-DE). – *(DE)* Madam President, I would like to welcome Mr Trichet to the European Parliament. You are certainly aware that the conservative Members here in Parliament support your policy geared towards lower inflation and currency stability. The fact that we have regularly talked for a long time about reforms in the Member States – your predecessor, Mr Duisenberg, did the same – is certainly nothing new.

Several weeks ago, Commissioner Almunia criticised Member States for the fact that they are not applying the reformed Stability Pact in the form in which it was agreed. As we said at that time, one of our main points of criticism centred on the fact that if Stability Pact reform is undertaken in a form which gives some degree of flexibility to the repressive sphere, but then sets priorities in the preventative sphere, the Commission also then requires options in terms of being able to apply sanctions. Unfortunately, it has never advocated this.

We are now in a situation where, in more affluent times, we do not notice that the preventive arm takes effect, in other words, when states have money again, they should be prepared to save. Instead, when they come into money again, they want to spend it accordingly.

Do you share Commissioner Almunia's opinion on this issue and how should Member States be urged to abide by the rules which they themselves have set? A small contradiction exists here in terms of what regularly happens.

I would appreciate your opinion on the letters sent to you by Messrs Almunia and Juncker regarding a future, more extensive trialogue and also regarding a transition to a coordinated economic policy. I always find it wonderful if attempts are made to push forward in this area. As far as I am concerned, the ECB's objective is currency stability. I would be grateful if Member States at least adhered to the rules which they set themselves before considering new coordination mechanisms.

3-010

Jean-Claude Trichet, *ECB*. **–** Thank you very much for your questions and for your support for our policy. You are absolutely right to mention the fact that we have a policy which has not changed since the very first day under the presidency of my predecessor. We kept intact the highest level of credibility which was available in the euro area and we still have this highest level of credibility. This is a major asset for the European economy, the euro area itself. We will inflexibly be faithful to our mandate – our primary goal is price stability, in line with your own support.

On the Stability and Growth Pact, you are well aware of the ECB's position: we were against any change in the corrective arm of the Pact. We said that very clearly because the stability and growth pact is a decisive component in the EMU. I would say it is the 'E' in 'EMU'. We have no decision-making powers in this domain, we only give our analysis, our diagnosis and our recommendation. We observed as you did that there was unanimity to amend the pact and we immediately said, 'you have been unanimous to amend the pact, let us apply this rule as rigorously as possible'. That is our position and the reason why I am in full agreement with Commissioner Almunia in his own assessment of the situation. We call, with the Commission, for the rigorous implementation of the pact.

From that standpoint and I have two main remarks. One is that in a period of growth which is relatively close to our potential, we should not embark again on the mistakes of the past. That is very important: put aside what will be necessary in more difficult episodes in the business cycle. We have also noted for those countries which are in the excessive deficit procedure that there is a tendency not to rigorously implement the call for reducing at a level of at least 0.5% the structural deficit on an ongoing yearly basis. So these are the two main observations which we share with Commissioner Almunia and with the Commission.

I would say to sum up that we would certainly support all the remarks that were made by the Commission.

3-011

Cristóbal Montoro Romero (PPE-DE). – *(ES)* Mr President of the European Central Bank: thank you for your explanations. I believe that we have made progress today, as Mr Radwan has said, also in relation to those explanations. Today you have given us – if you will pardon the expression – a theoretical, doctrinal, explanation of the nature of monetary policy and of what it is for. There is no question that that is useful as well, in terms of the European Union's academic education.

I would also like to say very clearly, however, Mr Trichet, that the European Central Bank's raising of interest rates and the speed of that rise jeopardise growth in the European Union – in the euro zone – where growth is already weak. It is not me who is saying that, but rather the OECD, the International Monetary Fund and the forecasts of the European Commission, which warn that Europe's economic growth in 2007 may be less than that of 2006. Those risks are jeopardising the evolution of the financial markets and stock exchanges.

The second risk relates to the appreciation of the euro and, in this regard, there are certain warnings that I would like to pass on this morning. I would also like to emphasise the importance of heterogeneity in the behaviour of the countries of the euro zone, because you will be aware that there are countries in the euro zone – and I do not know whether you know any of them – whose inflation is currently twice the European Central Bank's objective, whose external deficit is 10% of their Gross Domestic Product and whose public spending programme for next year is 7%.

Although I appreciate the difficulties, Mr Trichet, I would ask you to be cautious about that rise in interest rates given the risk of jeopardising economic growth.

3-012

Jean-Claude Trichet, *ECB*. **–** Let me comment on the three points you made. First of all, it is true that we have diverse positions as regards in particular inflation in the euro area. I am telling the various governments and ministers concerned that we are responsible for the average of the euro area. We have 313 million fellow citizens in the euro area, which is in the order of magnitude of the US. Just as the US is looking at the average inflation in the US, we are looking at the average inflation in the euro area. The various governments or social partners concerned all over Europe are responsible for their own differential vis-à-vis the average. That is absolutely clear. You mentioned some figures, I do not want to comment on any particular figure, but this must be absolutely clear.

Another remark, of course, is that as I have explained, what we do we do to preserve price stability, to be credible in preserving price stability and therefore to continue anchoring inflationary expectations. It is remarkable that we have maintained the anchoring of inflationary expectations in a number of years in which we have had permanent and major shocks to the economy and to inflation – as a result of oil price increases in particular, but not exclusively. We will continue to do that because it is the best service we can render to the European economy as regards sustainable growth and job creation.

This is a hypothesis, and it will not happen because will not permit it to happen, but imagine for one second that we lose credibility. The inflationary expectations are increasing. The are increasing by x basis points. You will immediately have these x basis points in the medium and long-term market rates. They will all increase to capture the fact that the inflationary expectations would be 'disanchored', and you do not want that. What you are asking me is precisely to avoid that, and that is why we will continue to do what we judge appropriate to maintain this anchoring.

3-013
Kurt Joachim Lauk (PPE-DE). – *(DE)* Madam President, I would first like to thank you, Mr Trichet, for your unambiguous remarks, and especially also for your statement that a low rate of inflation protects the poorer section of the population. I consider this an important addition which is often overlooked.

I have three brief questions. Firstly: as regards budgetary policy, is the increasing lack of discipline on the part of the big states – Germany, France and Italy – a cause for concern as far as the euro is concerned? Secondly: Mr Juncker has offered to give you additional advice. He has therefore implied that you need additional advice to carry out your job. He has offered to help you. Where do you stand in relation to this offer of help? Is it helpful or is it simply interference in an area for which he is not responsible? Thirdly: the Stability and Growth Pact. You have already said that you were always an opponent of Stability Pact reform. Commissioner Almunia was an advocate of reform. He watered down the pact contrary to your opinion. How do you view Mr Almunia's shift in position, given that, initially, he was a co-inventor of this watering down approach but now maintains that this approach does not work. In your view, is this more of a cabaret type interlude or has Mr Almunia genuinely shifted position?

3-014
Jean-Claude Trichet, *ECB***. –** Three questions, three very short responses. Yes, I think the discipline of the major economies, but also of all economies, is extremely important and it is true that we have permanent concern in this respect. The Commission, the ECB and the other countries have permanent concern. So we again only have one motto in this respect which is: rigorously implement the pact as it was approved unanimously by the governments concerned in the Council and ECOFIN – the pact itself is under the ECOFIN's responsibility.

I have two remarks on the second point. First, we – and I personally – will always fiercely defend and preserve the independence of our institution. Everything relies upon the credibility of our institution. If we were credible from day one it is because the institution itself was deemed credible. We had no track record, no facts or figures that we could invoke to back our credibility, as the euro was created out of nothing on 1 January 1999, and our institution had no track record. This is absolutely indisputable: it is recognised by academics all over the world; it is recognised by the people of Europe.

Second, as regards the relationships we have with the Eurogroup, I would say from our standpoint that they are intimate. We fully implement the treaty and our rules. We have a lot of meetings: three every month. That is the highest level of organised meetings by governments vis-à-vis a Central Bank or the reverse. We are scrupulously respecting the Treaty, of course, and this permits not only direct contact between the various people responsible and the various presidents, but it also allows for the Chairman of the Eurogroup to understand from the insider the reasoning of the Governing Council of the ECB, which is a collegiate body. It also allows me and the Vice-President to understand how the Eurogroup itself is reasoning. That is very important.

I would add, and this is my third remark, that personally I have a lot of esteem for Jean-Claude Juncker, with whom I negotiated on the Maastricht Treaty. He has a very important and difficult task in chairing the Eurogroup of ministers of finance. Those are my three comments.

As regards the position we might have today on the Stability and Growth Pact, we made it very clear in 2004 that we thought that we should not open up Pandora's box. The past is the past. Everybody knows that it was a period in which we had given a recommendation. That recommendation has not been followed. I would say that today the Commission is doing its job in ensuring that the current Pact is rigorously implemented. I said already that I was fully backing what Commission Almunia told you, and I think he is doing his job in the current circumstances and taking into account the laws and regulations as they are today. Again, the past is the past.

3-015
Ieke van den Burg (PSE). – I thank Mr Trichet for elaborating on his policies on price stability. I wish to begin by saying that nobody disputes the important goal of price stability. The discussion is about whether it should be the only target and the only goal. If you then say in connection to, for instance, the Fed, that in fact it is the same issue, I think that is the important issue: whether there is room for other explicit targets for monetary policy, and particularly in a situation where these inflation threats are not extremely high our position is that there is room for these other targets and for a more conscious policy.

What strikes me is that you are only speaking about how your counterparts in the Eurogroup and in the Commission are dealing with a sort of collection of individual Member States' – fiscal policies, particularly, as well as structural reforms and that type of thing. What is your view about a European policy coordination and an intelligent policy mix to be taken,

particularly at the European macroeconomic level? This seems to me to be more than just the sum of individual policies of Member States and just the respect for Treaty provisions. Perhaps you could give us some more imagination about macroeconomic policies at the European level.

3-016

Jean-Claude Trichet, *ECB***. –** Again, if in my introductory remarks I insisted on this relationship between price stability as a necessary condition and the best means to achieving sustainable growth and job creation, it is because the question comes up very often – including, of course, in the European Parliament – and because there is a paradox. Very often it is presented as if we were isolated in the world with our own concept. However, it is the exact opposite: our concept is fully in line with almost all other countries' economies and central banks in the world. Even, as I said, in the United States of America, this relationship of necessary conditions, the best means to achieve sustainable growth, is mentioned as openly as in the public debate.

Let me also underline one point. When you look at the anchoring of inflationary expectations, I would perhaps accept that if we were at the level of 1%, you would tell me your definition of price stability is less than or close to 2%. You are at 1%. Perhaps, in a way, you are taking out an insurance policy against going above 2%, which is very high, obviously. But we are not at 1%, we are at 1.9%. Who can think of a better arithmetical achievement, when your definition is less than or close to 2%, than 1.9%? Where do you see there the illustration of the fact that we would overdo our own responsibility? We do what we have to do, no less and no more. That is something which the people of Europe understand pretty well. You have your own constituency. I can tell you from my travels throughout Europe that the message its 313 million people are sending us is very clear: maintain price stability. There is no other message, and it comes from absolutely everywhere in Europe. That responsibility is given to us by the Treaty. We are called upon to be vigilant by the people of Europe.

On coordination, the Eurogroup itself is an entity which is there precisely to exert peer surveillance. I would echo what you said: it is extremely important, as regards the Stability and Growth Pact, that the ultimate decisions are taken by the Council. The Council is a college, so peer surveillance is absolutely decisive. I should also say that, in a domain which is so important – that of the structural reforms and implementation of the Lisbon Agenda – I am very much in agreement with the messages that came from the European Parliament on perhaps replacing the national programmes with an overall European context and identifying the best performers. Perhaps also you were bold enough to say also the worst performers – the naming and shaming, which you know has not been accepted by the Council. I would be very much in line with the European Parliament in this respect. Benchmarking has been one of the keys of the Maastricht Treaty, and perhaps explains why I can tell you that we maintain credibility because we had benchmarked at the best level of credibility. In terms of structural reforms, in our opinion, we should also benchmark more resolutely and more visibly, and there, once again, I am very much in agreement with your own recommendation.

3-017

Dariusz Rosati (PSE). – Thank you, Mr Trichet, for giving us a very interesting and, as usual, very clear statement on the monetary policy of the Central Bank.

I should like to ask you two questions. The first one is a follow-up to the question raised just now. You were telling us once again that the best contribution that monetary policy can make to growth and jobs is to provide price stability, and that price stability is both the goal of monetary policy and the means to achieve other goals. Yet we have a situation where the Treaty speaks clearly about two goals, because it says that, of course, the primary goal is to achieve price stability, but, without prejudice to the primary goal, the Central Bank is supposed to support growth and employment objectives if it does not compromise the first goal. Could you tell us about the circumstances in which you would say that this is exactly the situation as described by the Treaty in the second part of this first sentence, i.e. we have price stability; there is no threat to price stability and now I can support growth and jobs? Could you tell us somewhat more about this? How you would support growth and jobs? Because looking at the past policy of the European Central Bank, it would be very difficult to find such instances in which you would explicitly apply the second part of the Treaty.

My second question refers back to the debates we had here on the definition of price stability within the context of discussing the convergence reports. As you said, the ECB applies the price stability definition, which speaks about the inflation rate at below but close to 2%. At the same time you applied in the convergence report the price stability criterion which was calculated as the average of the three lowest inflation rates in the EU area. My question is: why are you applying two different definitions of price stability in one institution, while the Treaty speaks clearly about only one price stability?

3-018

Jean-Claude Trichet, *ECB***. –** Concerning your first question, I have answered it in advance. It is our opinion, which is shared by almost all countries' economies and central banks in the world, that by ensuring price stability you will also attain all the other goals that were mentioned. By the way, you know that in the Treaty we are called upon to support not just one or two but *all* the goals of the European Union. But, again, it is because there is this relationship of necessary conditions that by attaining price stability we will also attain the other goals. You cannot separate them and we cannot make an *arbitrage* between these various goals. That is really very important. I cannot even imagine any country in the

world allowing an institution to make an *arbitrage* between price stability, on the one hand, and growth and job creation on the other. It would be something which would probably be the most important political *arbitrage* in the economy in question. That would not be given to an independent central bank. It is because there is this complementarity and this very close relationship between price stability and sustainable growth that we have this goal of price stability given the world over to independent institutions.

On the convergence report, I would only mention the fact that the Commission and the ECB have applied the rules as they are stated in the current Treaty and we have examined this situation very carefully. Our own lawyers, the Commission's lawyers and, to my knowledge, the Council's lawyers, have all said that this is the correct implementation of the Treaty as it is. We know how difficult it is to change the Treaty, and if we do not respect the Treaty in any particular domain, we would not only be unfaithful to our mandate – and I am speaking not only for the ECB but also for the Commission – but we would also open up any kind of interpretation of any other criteria, which would be a total catastrophe. So I know that there have been some disputes on the way in which we are applying the Treaty, but there is no doubt that it is the correct implementation of the Treaty.

3-019
Margarita Starkevičiūtė (ALDE). – *(LT)* I come from Lithuania. I would like to express some disappointment about the whole story surrounding Lithuania's accession to the euro zone and the political consequences which are now being felt in Lithuania. I feel that many questions should have been solved earlier. This is one of the problems which other new Member States will also face. We all have to introduce the euro by a certain deadline. It is likely that at that time our growth rate, due to the convergence process and inflation, will be somewhat greater than in other old members of the euro zone. There will be such conflict the whole time though: old countries will not want us very much because our accession would mean the rate of interest would have to be increased. Although you once commented that the influence of the new countries on the economy is not significant – well yes, today it is slight, but it is growing. In future, the European Central Bank will face a similar problem to the one experienced in Ireland in that there will be a group of countries which want the euro or have the euro while having higher inflation and higher growth rates, and more mature countries which will have lower growth rates and lower inflation. Finding a rate of interest suitable for both sides will be complicated. We understand that problem perfectly well as every day in Parliament we have to coordinate different development phases. How do you propose to solve this and do you take these matters into account?

3-020
Jean-Claude Trichet, *ECB***. –** First of all, I am not going back to the computation of the criteria of price stability, which has been done by the Commission, as well as by us, again in full implementation of the Treaty as it is.

You mentioned the vastness of the enlarged euro area, after the entry of some of the countries that joined the EU in May 2004. Next year we shall have the first entry. Then you said that there will be additional difficulties as regards running the monetary policy, because of the different situations in the various countries. I would say that in a vast continental economy of 313 million people and rising, it is normal to have a certain level of diversity. In the US there is also quite a high level of diversity. You might be surprised to know that when we make a picture of the standard deviation – the diversity – both in growth and in inflation on a state-to-state and country-to-country basis, we obtain the same order of magnitude. So, in any vast continental economy, you have diverse entities inside, but what you have to do, of course, is to take the appropriate decision to ensure the smooth functioning of this vast economy as a whole. It is what we will certainly continue to do.

The catching-up exercise of those who are still at a level of GDP per capita that is much lower than the average, is something which will call for a growth differential over time until they catch up. It should not be confused with the differential between the rate of growth of a mature economy – which also might be different and might be associated with the degree of structural reforms, the degree of flexibility in the economy that has been engineered. In my opinion, Ireland is not to be compared to Lithuania or Slovenia, because Ireland's economy has a GDP per capita that is much higher than the average and is continuing to grow very fast, because Ireland has a *very* flexible and restructured economy that explains this differential. We would call for everyone to make every effort possible – some to catch-up to the average level, and they are in a 'catching-up' mode, and others to speed up their growth by increasing their speed limits. That would be very true for all the mature economies.

3-021
Gunnar Hökmark (PPE-DE). – Thank you for your statement, Mr Trichet. I would like to ask about the timing of interest rate increases, because as you said in your presentation, you forecast that economic growth will be lower in 2007 than it is in 2006. How do you look upon the fact that the interest rate increases you are doing now will have the full effect on 2007? Is it so that you see other problems than the growth we are discussing – for example the deficits of some countries, which you did not mention in your presentation? That is the first question.

My second question is about the rules for entering the euro zone. I totally agree that you should not change the rules. You should apply the rules where they are there. But how relevant or how smart are the rules? Theoretically you could have three EU Member States that are not members of the euro zone with such low inflation that an applicant country with a

lower inflation rate than the average in the euro zone – or even the lowest inflation rate among the members – could not enter the euro zone because of this. How do you look upon this as a theoretical example? It has some relevance in the current situation we have been discussing. Do you not foresee that there should be a change of the rules that we should then apply?

3-022
Jean-Claude Trichet, *ECB***. –** In reply to the first question, which is a very important one, I said that we did not decide *ex ante* on a particular mode of interest rate increases or on a series of interest rate increases. Our understanding of our responsibility is that we have to do at any time what is necessary to counter the inflationary risks as we see them. We have to preserve the anchoring of inflationary expectations. That is way we look at our duty and it is very well understood, I have to say, by observers and market participants. We never commit ourselves unconditionally in advance over whether to maintain rates at a certain level for a considerable period of time, or to engage in a particular mode which would be to define *ex ante* and unconditionally.

So I can only tell you that we will continue to do all that is necessary to counter inflationary risk and anchor inflationary expectations. It seems to me that is very well understood by observers. I said that *very* clearly at the press conference in Madrid immediately after our last decision.

On the rules, well, the rules are the rules! We know from experience that changing the Treaty is certainly not easy.

I realise that there are lot of criticisms based on a constellation of situations in the euro area and in the European Union. In the particular case that we are discussing, as you have seen, one country met the criteria and was accepted. The other country, in the eyes of the Commission and in our own eyes, did not meet the criteria, but we have proved that it was not an impossibility. The proof of the matter is that Slovenia has been accepted. I am not going to say any more about that. Again, we shall apply the Treaty as it is. It is the common view of the institutions concerned.

3-023
Othmar Karas (PPE-DE). – *(DE)* Madam President, Mr Trichet, I do not wish to repeat what everybody here has said already. I have just one request. I am grateful to you for the rigour with which you have stated the political-economic correlations. You deem it necessary for us to explain time and again the value of price stability in terms of growth and employment. I consider it necessary, however, and I am inquiring whether it is possible for you, as the ECB, to conduct an added value campaign for the European Union regarding the euro, along the lines of the information campaign pertaining to the introduction of the euro, to describe the added value achieved as a result of introducing the euro compared with former currencies in all Member States and to emphasise here, too, the value of price stability as regards growth and employment.

You have touched on my second point. However, I would very much appreciate clarification regarding the current deficits as to that part accounted for by structural deficit and that part accounted for by innovation deficit. I would like us to support mutually the benchmarking of Member State activities aimed at reducing the structural deficit. Tell me what we can do to support your request.

3-024
Jean-Claude Trichet, *ECB***. –** I very much share the view you have expressed that we have ensure appropriate communication with the people of Europe in terms of what the euro represents. As I said, the message that they are sending us is 'preserve price stability – we are not necessarily satisfied with what we observe as regards inflation in our own economy'.

It is also true that the people of Europe are not fully aware of the advantages associated with the euro, or of the fact that we were able to maintain the credibility of the currency in very difficult circumstances – with major oil shocks, for example. There is also the issue of the level of anchoring of our inflationary expectations. We are reflecting on that, and are looking with the full team – the national central banks are themselves a member of the team – for a way to optimise our overall communication as a team which is responsible for the euro for our fellow citizens. In my opinion, we can certainly make progress in explaining exactly in the direction that you suggest.

As regards the structural deficit, as I said one observation that we are making for those countries which are in the excessive deficit procedure is that there is a tendency not to fully respect the Pact as regards the yearly reduction of structural deficit of at least 0.5% a year. The Commission is doing its job. We in the ECB are in full agreement with the Commission on the messages and the monitoring of what is going on, but of course, anything that comes from Parliament would also be very important and influential to convince the countries concerned of the importance of this steady reduction of their structural deficit.

When I compare the industrialised countries as a whole, it is absolutely clear that in terms of public spending as a proportion of GDP, we are higher or much higher than our other friends, whether these friends are the US, Japan, Canada, Australia and so forth. We are as an average – in the euro area as well in the European Union – much higher, and there is

no doubt that we are paying a certain price for that. Even if there might be an explanation for some of the differences that would not necessarily go over and above statistical differentials, it remains that there is a structural difference, which is a handicap for the European Union.

3-025
Antonis Samaras (PPE-DE). – Core inflation – excluding energy and food – was only 1.5% in May, down from 1.6% in April. Since real inflationary pressures as represented by the core measure are decreasing or even subdued, do you not think that we should keep the rates at least constant? We could even relax them, but not increase them. We have rising capital costs due to oil, we have export problems due to an increasing euro and we are trying to implement Union-wide reforms which can obviously be better accomplished when there is growth, not in a stagnating environment. I understand that it is the ECB's job to impose stability, but, Mr Trichet, you have to admit that there is a difference between stability and rigidity. By trapping an economy in a loophole of long-term stagnation, we might get rid of inflation, but that is bad economics, and bad politics, for that matter. I would especially like to ask you whether you believe that the criterion of core inflation is one that shows that matters linked to inflation are doing better than we say?

3-026
Jean-Claude Trichet, *ECB***. –** I should like to make some comments on your question, which is of course a very important one. First, as you know, we are called upon by the Treaty, as well as by the people of Europe, to deliver price stability on headline inflation, not on core inflation. This is something which any of us can experience on a day-to-day basis in discussions with our fellow citizens.

Secondly, it is not documented by research that core inflation is a good predictor of future inflation. There are a great number of cases in which core inflation joins up with headline inflation; headline inflation does not go down to meet to core inflation. Even from an academic standpoint, one has to be extraordinarily cautious in considering that core would be a good predictor.

Thirdly, in core inflation there are a number of prices that are pushed down – notably manufactured goods – by the presence at a global level of production coming from China and emerging economies in Asia, such as India and so forth. This constitutes permanent downwards pressure. There is permanent upwards pressure in the current episodes on commodities, oil and other input into those economies. If you put out what is going up and you leave what is going down, of course you are not necessarily capturing what is currently the global economy, which is producing a largely demand-driven oil shock, and not necessarily a supply-driven oil shock. I mention that with some caution, because there are episodes in recent history where you could see that things are much more demand-driven, and other episodes where it is a little bit supply-driven. Taking everything into account, I draw you attention to the fact that in a period of very rapid relative price changes at a global level, one has to be very careful in subtracting some elements and not other elements which are associated by the presence of the new, very big Asian economies in the picture.

We are being closely observed by all European savers, investors, economic agents and members of the public. The rest of the world is also watching us. What we are capturing as far as information on inflationary expectations is concerned – I underlined the notion of anchoring – is an objective measure of the judgement which is made both by economic agents on the one hand through our surveys and panels, and by financial markets. I confirm to you that what we are doing is exactly what is called for under the current situation, and allows us to continue to benefit from a financial environment in which medium- and long-term market interest rates are minimising the component in terms of expected inflation and risk premiums against future inflation.

3-027
Pervenche Berès (PSE). – *(FR)* Thank you, Mr Trichet. I should like, for my part, to ask you three brief questions.

First question: I should like to say that I agree with your statement about the future of stock exchange harmonisation in which you stated your preference for a European solution. It remains, however, for you to define the conditions of a European solution and the conditions that need to be in place for such a solution to be acceptable, that is, one in which everyone feels they are winning.

My second question relates to the composition of the Executive Board and to the methods of appointing its members. What improvements could be made whereby the arguments that surrounded the last nomination do not arise again in 2010 and, in particular, so that the question of the transparency of the portfolios of the various members of the Executive Board forms part of the initial stage of the decision making procedure?

Lastly, you referred to Article 105 in order to argue in favour of price stability, price stability and price stability in the interests of growth and employment. When Jean-Claude Juncker and Joaquin Almunia write to you to suggest greater coordination, you will answer that you are doing your job and that it is up to others to do theirs.

The others, however, are specifically asking you for greater coordination. In which case, why not tell them that perhaps the time has come to go a bit beyond the current situation, and not, as you kept repeating this morning, that is enough?

3-028
Jean-Claude Trichet, *ECB***. –** *(FR)* On your last point, I did not say 'that is enough'!

I said – and I am very pleased about this – that these two authorities, namely the executive authority and the monetary authority, are very much accountable to one another, meet on a very regular basis and have a clearly defined legal relationship.

Regarding the question that you asked me about stock exchanges, I said that, all things being equal, I had a preference for a European solution or solutions. I was expressing a personal point of view, because, as you know, it is not for us to decide on this matter.

This position seems to me quite natural and straightforward. I also said 'all things being equal' and that it was not for us to decide on the matter.

As regards the composition of the Executive Board, according to the Treaty it is the responsibility of the executives and it is we who are calling for the Treaty to be implemented strictly, in terms of the quality of the women and the men who join us. I should like to say in this regard that the initial Executive Board has now been completely renewed. By credibility, I mean the credibility of the institution. We are credible at thirty, right now and there will naturally be many renewals of the Executive Board and also of the Governing Council during this period. What matters is the credibility of the institution.

When I see the men and women who have been appointed, all with your approval, let us not forget, Lucas, Gertrude, José Manuel, Lorenzo and Jürgen, the last to be appointed, I can say that we have men and women of what I consider very high calibre. It is with them that we form this team called the 'Executive Board', that is, the management of the Bank.

The allocation of tasks internally is our own affair, and forms part of the institution's independence. There is no question of involvement in the distribution of tasks because it is done through a collective, group decision by the Executive Board itself. It is not even the Governing Council of the European Central Bank which takes this decision. It is the Executive Board itself, the Executive Board each of whose members has been nominated after consulting you and after consulting the European Central Bank, and, as you know, on the decision of the Heads of State or Government. That is the law and we believe that it has been strictly adhered to and must be strictly adhered to.

As for the last point, I have already spoken about this.

3-029
Pervenche Berès (PSE). – (*FR)* May I return to the issue of the portfolios? You spoke about a collective decision. To be more specific, I believe that right up until Mr Jürgen Starck came into office, nobody knew what his responsibilities were going to be. I imagine, therefore, that you were able to work out the collective decision very quickly.

I give the floor to Mr Sanchez Presedo.

3-030
Antolín Sánchez Presedo (PSE). – *(ES)* Discussing monetary policy decisions is a truly complex matter. There are countries in which there is growth, in which there is a budget surplus and where an excessively relaxed policy can create tensions, including inflation, or affect real-estate values. I assume, however, that the European Central Bank takes account of the overall situation of the euro zone and, naturally, some of the imbalances that may exist go beyond monetary policy.

Nevertheless, I would like to focus my question on two issues. Firstly, when analysing the components of inflation, you said that manufactured goods create downwards pressure. The International Monetary Fund's April perspectives document of 2006 states that over recent years, in terms of imported and oil-based products, globalisation has led to a fall of a quarter of a point in the advanced economies and of half a point in the United States, but that this effect will probably not exist in future years. I would like to know whether you agree with that diagnosis.

Secondly, the United States, which has apparently benefited more from this process than the European Union, nevertheless has significant commercial imbalances. There is currently a situation in which the short-term yield curve in the United States is higher than that long-term yield curve, which means that there is a possibility of problems relating to economic slow-down. In order to contain inflation, interest rates should be raised, while in the long term those rates are lower. That naturally raises the possibility of a degree of economic slow-down.

Have the European Central Bank's decisions also taken account of all of this?

3-031
Jean-Claude Trichet, *ECB***. –** On your first question, I would not confirm to the decimal place the IMF analysis on the impact of these changes of a decisive parameter, but it seems to me to be an order of magnitude which could be accepted. But again, I do not subscribe to it because it is their responsibility.

On the yield curve, first of all I will tell you that our responsibilities relate to Europe, inflation in the euro area and the yield curve of the euro area. Let me mention only one figure. The last time I looked at the long-term rates on the euro and on the dollar, I could see on a 10-year basis that the differential was around 110 to 115 basis points. We pay 110 or 115 basis points less for a loan on a 10-year basis, and it would be longer if it were 20 years or 30 years.

Let me mention in passing that, when I speak of a lower level of inflationary expectations and a lower level of risk premiums for future inflation, I am speaking of something which is real and which could be measured in the financial markets.

Concerning your last remark, as regards our monetary policy, we have two pillars: we look at the economic analysis and the monetary analysis, we cross-check and make a synthesis. We take into account absolutely all the available information. We do not have a mechanistic approach. We do not have one parameter that could be immediately transformed into a mechanistic policy decision. We take all parameters, we make a synthesis and then we make a judgement on the inflationary risk. We adjust and if necessary modify our monetary policy stance in order to counter the inflationary pressures that we are assessing. We have no rule other than that, no mechanistic approach. We are as comprehensive as possible and we make a judgement.

3-032
Zsolt László Becsey (PPE-DE). – *(HU)* Mr President, I would like to ask for your advice concerning a communication issue. What should I do, when the most famous Hungarian economist states, in respect of the enlargement of the euro zone …

3-033
I would like to ask you for advice. What can I do if the most famous and prestigious Hungarian economist says, in relation to the enlargement of the euro zone, that the decision and the whole procedure was shameful. Concerning the criteria relating to inflation, two countries out of three are out of the euro zone. You also mentioned the nominal average of the three lowest inflation rates, not the three best performing countries in terms of price stability. As regards the case of catching-up countries which cannot be asked to use 'deflation', this very famous Hungarian economist wrote in a Hungarian newspaper that he does not understand why they are asking for deflation from the catching-up countries. The economist I am talking about is Alexandre Lamfalussy, your predecessor, known as the father of the euro zone. Nor does he understand the inflation criterion of sustainability in relation to a catching-up country like Lithuania in the light of the decision based on another Maastricht criterion with Italy on debt issuing and the debt level. So what can I say in this situation?

My next question is a related one. Can you imagine an EU national from a non-eurozone country being a member of the Governing Board – for example Mr Balcerowicz or Mr Járai? Strictly speaking, on the basis of the Treaty, representatives of EU Member States should be able to attend, not just those of euro zone Member State.

3-034
Jean-Claude Trichet, *ECB***. –** I am not sure that I completely understood your last question. I shall take the questions and you can tell me if I have answered them properly.

In reply to the first question, I have already said that we apply the Treaty. Your country has signed up to the Treaty as it is, and I have checked that, at the time of the Convention, there was not a single proposal to change that computation of those criteria. I mention that in passing. Now I know that there are criticisms; you have echoed those criticisms. We have proved recently that this approach and implementation of the Treaty did not prevent Slovenia from entering.

You mentioned deflation. I am not sure that I understand what you mean, because we certainly have no call for deflation.

On sustainability, it is the Treaty again. I am surprised that you say that Mr Lamfalussy could say the Treaty is not easy to understand, because it is absolutely clear that in terms of the Maastricht criteria – and, as you know, there is not just one criterion, but five Maastricht criteria – it is important that we measure not only the situation at the time we take the picture, but also whether this is sustainable. It seems to me that the economic underpinning on having a judgement on sustainability is *very* important. I have always insisted on that, in my previous position as well as now. It is something which, again, is extremely important. Of course there is a judgement. Sustainability is not a mechanistic calculation: it is an appreciation; it is a judgement. But we need that judgement.

I am not sure I understood the last point. We should not blur responsibility, of course. Countries that are not in the euro area are not present in the Executive Board or the Governing Council. That is the rule as far we have it. However, they are present and welcome – and there are many of them – in the staff of the ECB. The ECB, together with the other national central banks in the Eurosystem, is *the* central bank of the euro area. There is, of course, the Central Bank of Poland and the Bank of England, etc. We are *very* open to having many Polish citizens as members of staff in the ECB itself. I am very happy with that and, again, as I said, they are all welcome – the Hungarians, etc. We are very open in this respect.

3-035

Elisa Ferreira (PSE). – *(PT)* First question: the European Central Bank prevents inflation during a non-inflationary period. Price stability is a necessary condition, and, as has already been mentioned, is insufficient for growth and jobs.

My question is as follows: how, in that case, do you interpret the specific reference to the ECB's contribution to growth and employment in the Treaty? Would it not be enough to have a reference to the necessary conditions? What is the ECB's contribution towards the sufficient conditions?

Second question: did I understand you correctly when you said the exact level of inflation in the euro zone is determined by legal opinions and not by contributions from economists?

Third question: what is your understanding of the role of the ECB as the currency of the largest trading bloc in the world, particularly as regards the exchange rate of the euro against other currencies such as the dollar, and the role of exports in boosting growth in Europe and in preventing the risk of world disorder to which US deficits and the price of oil could be the precursor?

Last question: you have made a number of references to the need for structural reforms in various countries. These reforms cost money, especially when they relate to the labour market and the Lisbon Strategy. To what extent is the ECB prepared to accommodate the costs of these structural reforms, within its criteria, as part of its macroeconomic reading of the situation?

3-036

Jean-Claude Trichet, *ECB***. –** I have already responded to your first question. Price stability is both a necessary condition and a means to deliver sustainable growth and sustainable job creation. It is important to fully understand this relationship. It explains why our primary goal is price stability.

On the second point, we have to apply the Treaty. The Treaty is the Treaty and nobody has the authority not to apply the Treaty. It is as simple as that. It seems to me that it is a waste of time to persist on that point. Those who are convinced that it should be changed, must proceed to try to change it. However, at the present time, nobody can expect us – the Commission, the ECB and the Council – to do anything other than respect the Treaty. Again, we have proved that it is perfectly possible to enter into the euro area. I am so happy that Slovenia is entering and that our team of 13 – as it is today with the ECB and 12 national central banks – will be a team of 14 as soon as next year.

As regards the imbalances and the global imbalances, I participated in the recent meetings of the 'Gs' – including the G7 – in Washington. We have a judgement on what has to be done to help the orderly, progressive unwinding of global imbalances. Homework has to be done in the US on the level of public finance deficit, on the level of savings in the US economy. Homework has to be done in Japan; homework has to be done in Europe.

Structural reforms – which were the subject of your last question – are a key element in Europe. They are key homework we have to do to increase the speed limit of European economic growth. That is good for us, of course: it is not a sacrifice that we would make on the altar of the unwinding of global imbalances. It is in our own selfish interest to have more growth and more job creation, and it would also contribute to the unwinding of global imbalances. It is necessary for all of us do our homework in our own domain, according to the current level of the global consensus. Again, I insist on the fact that, it is true for Europe as a whole and it is true for each individual country. Those who have embarked on those reforms have a much more flattering level of growth and a much lower level of unemployment than the average. That is clear. Ireland was just mentioned. Look at Ireland! It has structural reforms and it has prosperity, growth and job creation.

3-037

Giovanni Pittella (PSE). – *(IT)* Madam President, ladies and gentlemen, among other areas covered in the June bulletin, the European Central Bank highlights the excessive rise in house prices, particularly in some Member States of the Union, such as Italy, Belgium, France and Spain.

Mr Trichet, my question is as follows: given the anticipated impact of a rise in house prices on price stability, what countermeasures can, in your opinion, be suggested to the national governments in order to mitigate this negative impact?

3-038

Jean-Claude Trichet, *ECB***. –** You are absolutely right. When we observe the dynamism of the monetary aggregate, particularly of M3, we see that this dynamism is reflected in components as well as counterparts of M3, and amongst the counterparts the dynamism of the outstanding credit for financing housing is extremely impressive. This is something which has to be watched very carefully. I have said frequently that we have to monitor what is happening there.

Of course, there are many different situations. You have quoted, according to our analysis, a number of countries where things are clearly moving upwards extraordinary rapidly. Of course, there are other economies, such as Germany, where the situation is substantially different.

However, we have to look at the euro area as a whole. As a whole, a phenomenon is visible in the euro area that has to be monitored carefully. We have done that recently and it was one of the elements we took into consideration when we took our three last decisions to increase rates.

3-039
Eoin Ryan (UEN). – I should like to thank you for your presentation, Mr Trichet.

Let me come back to the last question, because it is the one I wanted to ask. You said in your opening remarks, and you have just repeated it, that monetary developments in the housing market need careful monitoring. Could you elaborate a little more on that? I know that it changes in the euro zone quite substantially. You make a lot of very complimentary remarks about my own country, Ireland. However, in the last seven to ten years we have had huge inflation in the housing market. We have had endless reports from experts. Every year we get three or four very detailed reports on how this is going to end in tears, but, with a few exceptions, they have all been wrong. I should like you to give us your views on that or elaborate a little more. You say that Ireland is doing all the right things. Our economy is growing, and we are very happy with that, but we still have a problem with housing inflation and I would be interested to hear your views on that.

3-040
Jean-Claude Trichet, *ECB***. –** Yes, it is true that I have been quite flattering about Ireland, because it seems to me the Irish economy deserves it in a number of areas, particularly because early engagement in structural reforms has proved very productive. The fact that the GDP per capita in Ireland is now well above the average – it is well above the UK GDP per capita as one example, but also well above the French, Italian and German figures – is something which has to be understood as a demonstration of the need to embark on structural reforms.

That being said, it is absolutely clear that there is a phenomenon of increases in your case, as well as in a number of other countries. This has been mentioned in our bulletin. These increases have to be monitored very carefully. At the level of the whole euro area, we have to understand what is happening at national level as well as possible. There are of course messages, there are warnings, there are prudentials, implementations of prudentials by the various national authorities which, combined with what we decide at a European level, would perhaps pave the way for the best future possible. Of course with the cycles it is very difficult to take control of these developments, but I trust that the Irish authorities are aware of their own capacity of influence in this respect. We all count on them as well as the Spanish, French or other authorities, where you have more or less the same phenomenon.

3-041
Karsten Friedrich Hoppenstedt (PPE-DE). – *(DE)* Madam President, firstly, I must apologise for not being present from the outset, but I was attending a large Commission hearing on Solvency II. I have also inquired whether the question I am putting has already been raised. I would very much like to know, because this has also been mentioned recently by Mr Stark, where you stand in relation to the fact that in China, at least according to the information generally available, so-called bad loans to washed-up companies are on a huge scale – 300, 500 billion – which the Central Bank has to make good time and again. This is only an observation, however. My question is this: how do you assess the future of derivatives, particularly Chinese derivatives? When we read the press and scrutinise other information, this appears to be a not inconsiderable problem.

3-042
Jean-Claude Trichet, *ECB***. –** As everybody knows, the Chinese economy is a major new partner at a global level. It has a major influence on a great number of areas and it will continue to exert more and more influence. The Chinese economy undoubtedly has a lot of structural reforms to engage in to take into account of its very rapid development, and that is particularly clear to me and to all other observers, including the Chinese authorities in the field of commercial banking. It is also clear in the relationship between commercial banks and enterprises in general and public enterprises in particular in China. All I can say is that what you mention is certainly an important issue in the eyes of the Chinese authorities and all global observers. As you know, they have taken steps towards an economy that is as market-based as possible. A lot of measures have still to be taken, it is an ongoing process. We encourage the Chinese to modernise the whole of their economy in line with the development of this economy, which is quite striking, as everyone knows.

3-043
Mia De Vits (PSE). – *(NL)* Madam President, I have not been able to follow the whole discussion either, but I do know that it was about the candidate countries. I have a question in that connection. Obviously, when candidate countries join the euro zone, they must meet the requirements of the Stability Pact in terms of inflation figures. I would like to ask Mr Trichet, though, how he assesses the sustainability of this condition.

3-044
Jean-Claude Trichet, *ECB***. –** As you know, we have on the one hand the Stability and Growth Pact, which deals with the fiscal position and fiscal soundness of the various countries concerned. We have the two Maastricht criteria, which deal with the fiscal position, the yearly deficit and the debt outstanding, and we have the Maastricht criteria for entry into the euro area. You probably mentioned inflation as one of these criteria. I am very clear on that, the Commission and I are applying the Treaty as it is, and if and when it is changed we will apply the Treaty, we always apply the Treaty.

We have to make a judgement on the sustainability of meeting the criteria. It is certainly true for inflation as well as for the other criteria – those criteria of low long-term interest rates and for inflation. It is a judgement, we are looking at it as thoroughly as possible and we make a judgement on whether it is sustainable or not. There is no mechanistic approach, but there is a judgement to be made by the Commission and by us. We have met our responsibilities in the past and we will continue to do so in the future. We will use our best judgement to give our feelings on sustainability.

3-045
Alexander Radwan (PPE-DE). – *(DE)* Madam President, Mr Trichet, in your introduction, you touched on the current discussions regarding the development of European stock exchanges. I have just one brief passing remark: I hope that we in Europe are becoming more European and are ourselves adhering to the yardsticks we set now and again in our political remarks. However, this is rather aimed at the Member States.

We are faced with two options: one European and one transatlantic. How would you assess the development were you to compare the transatlantic and European options? On the one hand, as regards a European regulatory scenario, to what extent may European regulations be overlapped by other regulations and another jurisdiction and how do you view both options in comparison with one another in terms of the development of a strong, uniform European financial market?

3-046
Jean-Claude Trichet, *ECB***. –** As I already said, my personal preference is for the European solution, and it goes without saying that whatever solution is chosen by those who have to take a decision, the European regulation must remain the European regulation. It is an absolute must. I cannot imagine that it would not be the case.

3-047
Pervenche Berès (PSE). – *(FR)* May I just ask you two final questions?

The first goes back to the one that Mrs Ferreira asked you about exchange rates. Your answer talked about global imbalance, but in fact more and more people in Europe are saying that the current exchange rate between the euro and the dollar to a large extent explains the slow rate of growth and lack of capacity for harmonious development within the European Union.

Since you consider that you have a responsibility as regards exchange rates, even if on that point the Treaty is rather more ambiguous, how do you assess this situation and what is the impact of the exchange rate on European growth?

Secondly, I wish to say that there is another point on which I am in agreement with you. Regarding your comments about the risks involved in the multiplication and development of arbitrage funds, I should like to know your assessment of the kind of initiative that should be taken and the direction it should take at European level, if not within the context of the transatlantic dialogue.

3-048
Jean-Claude Trichet, *ECB*. **–** *(FR)* On the first point, I will say this: when I have something to say, I say it. Perhaps you will remember that from the end of 2003 or the beginning of 2004.

I have just signed the G7 communiqué, which includes a paragraph about exchange rates. Right now I stand by my signature and by what we signed up to, along with the other G7 signatories. If and when I have another message to give you, I shall give it to you.

Concerning hedge funds, Madam Chairman, in our report on financial stability we have for the first time explicitly mentioned hedge funds as being one of the domains in which we must achieve a much better understanding of the underlying phenomena. There has been a major upsurge of activity with these funds. We have to understand what is happening, and understand it as thoroughly as possible. That is what the best possible management entails at European level and in the context of the global economy, because clearly this phenomenon is a global phenomenon.

At the moment, as regards financial stability and the risks for financial stability posed by hedge funds, we are depending on the vigilance of the counterparts, that is the commercial banks, the banks in general, which are under the control of the prudential authorities and which are the counterpart of these hedge funds. We depend to a large extent on these institutions, which we control and which we expect to be extremely vigilant with their partners.

Does this system work well? Is it sufficiently transparent? Transparency is very important to me personally, as I consider that it has enabled the global economy to make considerable progress on stability, particularly after the Asian crisis. We have considerably raised the level of transparency in international finance and in the behaviour of the public sector and of private institutions.

Is it possible, in the domain of hedge funds, to make real progress in transparency that would enable us to feel more certain about the stability of the entire global financial system? That remains to be seen.

Of course, since the phenomenon is a global one, the solution must be global. We must therefore be in close contact with our partners, with our American partners and our American friends, and that is the case. We also have very close contact, in Europe, with all of those concerned, including, of course, the British authorities.

3-049
Chairman. – There is nothing to stop us imagining, however, that in that domain, Europe could take the lead.

Mr Trichet, thank you for your participation in this monetary dialogue.

(The sitting was closed at 11 30a.m)