Klaus Regling in interview with CNBC

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Transcript of interview with ESM Managing Director Klaus Regling
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Interviewers: Geoff Cutmore, Steve Sedgwick and Karen Tso

This [ESM Pandemic Crisis Support] is an incredible fund, no troika surveillance and no reforms demanded as a result of taking these loans. Yet countries like Spain would rather turn to the markets and pay interest at 0.84% today than turn to your fund. Do you have an image problem with the corona loans that you're dishing out to European members?

Yes, to some extent that's true, but it’s early on. We had the approval of our Board [of Governors] on Friday and all euro area member states, including Spain, voted in favour. So everybody's in favour. All our member states want to make this available. It's an offer, no country has to take it. It will be available until the end of 2022. So that's a lot of time. Also, it's in principle a precautionary credit line. We know that from the IMF. So it can be arranged, and the expectation is that the money will not be drawn. So we will just wait and see what happens. I think it's good that our Board of Governors, which is basically the Eurogroup, the 19 finance ministers from the euro area countries, agreed to make this available. And it's a very different facility, a very different offer from what we did 10 years ago when we were created during the euro crisis. And I think that's good because it shows we can adapt to different circumstances.

Clearly there's a difference between member states approving these loans

versus actually tapping them. So what are we hearing from Italy? Because there seems to be the same resistance to tap the ESM from the Italians. Do you think that they will turn to you for support?

Well, I don't know. It's up to the Italians, like the other 19 member states. Of course, Italy, like all the other countries, all of them and all countries around the world, will have much larger fiscal deficits this year, going up in some cases to double-digit numbers. And this is not a European issue, obviously, it's a global issue. And we don't know how bad it gets because, you know, now it is a virus, it will be under control. So I think therefore that it's very good that we could make all the preparations. We know this Pandemic Crisis Support facility is available; if countries want to use it, they know it's available. So it can help them. And I think that's positive, even if they don't draw on it. It's good to have assurance it's available, but also one has to look at the broader context - the ESM is only one element in the crisis response of Europe.

There's a lot of action at the national level, obviously, like in other countries around the world. But then what's unique in Europe is that on top of what the member states do themselves, there is an offer from different European institutions. The ESM is one of them. It's an important part, but the European Investment Bank will do something, the European Commission has agreed already on one offer - the programme called SURE to support unemployed in member states, and the Commission is working on the recovery plan.

So we have this very special situation that measures at the national level, which are needed, will be complemented at the European level. And that, I think, will be very helpful because we can compensate with the measures from the European level. It's a fact that the national response is uneven. And we want to protect the single market. We don't want fragmentation, we want to maintain a level playing field. We don't want excessive divergences in the euro area and all the European measures are designed to help countries more that are most affected by crisis, and don't have the same fiscal space as some others. That is the value added of the European institutions.

I feel like I've wasted my time over the last decade. Waiting for debt to GDP to fall, worrying about such metrics as those. Am I going to waste my time over the next decade? When I was worried about Italy's 130% debt to

GDP, will I be worrying about Italy on 160% debt to GDP? It's pretty much a similar story across the eurozone as well. Do these traditional measures such as debt and repayment of debt and lowering debt matter any more?

Well, a number of points. First, I think you didn't wait in vain - the debt ratios were coming down in all European countries until last year. Also because we had an overall fiscal deficit of just 0.5% of GDP in Europe last year, while the US for instance is at 6%. Now the US is moving towards 20% and we may have a deficit of 9% or 10%. So this is my second point. This is not a European issue. It's a global issue. So first, there was progress. And I think we are happy we had the progress in the last decade, after the end of the euro crisis. Now we have a global problem. We have to deal with that. And thirdly, indeed, because the baseline scenario clearly calls for lower interest rates for longer, the amount of debt that can be serviced without running into debt servicing problems is higher. Again, this is global, this is not only in Europe, but it's also true outside Europe.

There are a number of issues floating around that suggest that the much discussed need for solidarity, something you've been on the record on, is just waning at this point. We have this German court decision over the actions taken by the European Central Bank. I wonder if you just care to weigh in on that. How damaging do you think that has been to the perception of cohesiveness for the bloc?

When you say solidarity is waning, I fully disagree. I think the decision on Friday to activate the ESM's Pandemic Crisis Support is one more indication that there is solidarity. There's also solidarity in the actions coming from the other European institutions that I just described - from the European Investment Bank, from the European Commission, because all of these three European institutions are designing their measures deliberately, so that countries that suffer most from the corona crisis and all countries that don't have as much fiscal space as some others, that they benefit more. This is the design principle. So don't say that solidarity is waning, and there will be more because the recovery fund that will be presented at the end of the month will work in the same direction.

But one can even go one step beyond that. There were many ministers in the Eurogroup meeting on Friday evening who said “we can call it solidarity, but it's really also self-interest because it's in the interest of each of the euro area member states, that the area as a whole functions well." And that there is not excessive divergence and that we maintain a well-functioning single market. So this is happening. We have had solidarity for 60 years in Europe; it's often not fully recognised that the EU budget has transfers every year. Some people believe there are no transfers in Europe, which is just wrong. There are transfers; they are being increased now, as a result of the crisis, so all this is happening.

The Court decision in Germany that you mentioned was not directed at what the ECB is doing now. It relates to a previous programme and I'm sure there will be a solution found between the different German institutions and the German Constitutional Court. It is an important ruling, but they made it very clear that they don't consider what the ECB is doing as monetary financing. And that may sound a bit obscure, but in the euro area this a key definition because monetary financing is not allowed. That is prohibited. And the court made it very clear that the ECB measures are not monetary financing of sovereigns. And the current PEPP (Pandemic Emergency Purchase Programme) programme was not subject; it may become subject in a few years, of another court ruling. But at the moment, I don't expect at all is that the ECB will change its current approach.

The programme that we're talking about at the moment, the Pandemic Crisis Support programme, does require, as has been pointed out, nation states to step forward and request the funds. And there will be enhanced monitoring of how that money is going to be spent. How do you avoid that perception of stigma associated with making that request? Because clearly, as you look at that key BTP to Bund spread, there is evidence that the market is already beginning to draw its own conclusions about the fiscal position that Italy finds itself in.

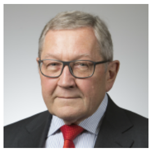
I think if people take the time to look at what the conditions are for the Pandemic Crisis Support, they will realize that the monitoring, including the enhanced surveillance that is done by the European Commission, is extremely limited; completely different from what we had 10 years ago and 8 years ago. It is limited. And that was a deliberate decision to monitor how the money that could be provided by the ESM is used. It should be used for medical expenditures related to the coronavirus, to the crisis; direct and indirect costs up to two percent of GDP. And the Commission has made it clear in writing that it would only monitor that approach. They will check on behalf of the ESM that the money is indeed used for that purpose.

And there is a very common, broad understanding that all of the member states would qualify; they would all have no problem using two percent of their GDP for these extra costs. Because it's also part of the health care infrastructure, nurses, doctors that are being used to deal with the current crisis.

So all that will be completely different from 10 years ago, when we had tough conditionality for a good reason - because there were massive macroeconomic imbalances that had to be corrected in the countries that borrowed from the ESM at the time. There were huge fiscal deficits, huge current account and trade deficits because they had lost competitiveness and that had to be corrected. That's why they lost market access at the time.

At the moment, all of our member states have pretty good market access. Spreads are a bit wider than a month or ago or two, but they are much, much smaller than what we saw a few years ago. So that's why the situation is really completely different. And I think that message is slowly sinking in.

Author



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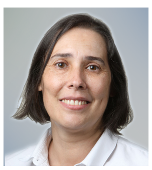

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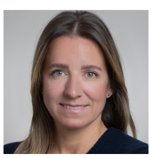

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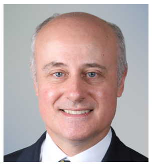

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