Rolf Strauch in interview with Finanz und Wirtschaft (Switzerland)

View PDF
10/01/2018
Interviews

Interview with Rolf Strauch, ESM Chief Economist
Published in *Finanz und Wirtschaft* (Switzerland)
10 January 2018
Interviewer: Ernst Herb

***Finanz und Wirtschaft:* Mr Strauch, is the euro area crisis now completely behind us?**

Rolf Strauch: You need to take a broad view to answer that question. The economic recovery has now been continuing for several years, and is broad-based. Domestic consumption is no longer the only driver of growth. Investments in goods and exports, which are gaining speed, are also contributing. The severe internal and external imbalances that led to the crisis have been dealt with, especially the current account deficits.

Wouldn’t now be the right moment to close down the institutions that were established as a response to the crisis, such as the ESM?

The ESM, which has just celebrated its fifth anniversary, is a permanent institution. One of the lessons we can draw from the euro crisis is that without the ESM, there would no longer be a European Monetary Union. Monetary policy alone was not sufficient to maintain euro area stability. It has been complemented by improved cross-border policy coordination, by the Banking Union, and, as you say, the ESM. The crisis could not have been overcome without structural reforms and our assistance programmes.

But isn’t the ESM signalling to markets that - apparently - there are risk-

free investments?

No, that’s not a correct interpretation of what the ESM does. The ESM combines the principles of the International Monetary Fund on the one hand, and the specific needs of the euro area on the other. Through the IMF approach, we can support member states that have landed in trouble with emergency loans. At the same time, we are flexible enough to respond to specific needs, something we have shown for instance in the Spanish banking sector. And we grant loans with long maturities at favourable conditions, which gives countries fiscal room for manoeuvre. Needless to say, this needs to be accompanied by structural reforms [in programme countries].

Doesn’t that mean that the ESM has quietly become something like a European finance ministry?

Absolutely not. The ESM is primarily a rescue mechanism, and that’s very different from a finance ministry, which also does its normal work during quiet times. At the moment, there is a debate whether to create the function of a joint finance minister, as we aim to deepen the euro area. But that’s a longer-term project and the member states must first agree to that idea before we can start talking about the possible role the ESM may play in this context.

Wouldn’t it be easier to solve the problem of high indebtedness through setting up a European [sovereign] insolvency mechanism? Particularly because it would mean that banks would be more cautious when granting credit in the future?

What the euro area needs is a better balance between diverging economic developments of individual countries. The private sector can make an important contribution to that. That is why we should complete the Banking Union, and work towards a single European capital market. A stability fund can complement it, by functioning as a buffer against asymmetric shocks in a country. Naturally, this presupposes that countries stick to the budget rules. That is why we need to simplify the budget rules, and make them more effective. Another thing is that the ESM Treaty already requires that the debt of a country needs to be restructured if it is still unsustainable despite an ESM programme. But there should never be an automatic debt restructuring, in our view.

Cynics would have it that the ESM was created not to rescue Greece, but primarily by German and French banks.

What good is it to be a cynic? The only thing I will say is that the stability of the euro area is our clear mandate. All member states have agreed to that, and that clearly shows that the goal of the ESM is in the general interest of the euro area.

Two decades ago, the Chiang Mai initiative was established in the Far East, as a response to the Asian financial crisis. The 10 ASEAN countries have pooled part of their financial reserves to fight crises in this endeavour, as have Japan, China and South Korea by now. Do you see a parallel with the ESM here?

You can’t really compare those two crises and the responses that they triggered. Regional Financing Arrangements exist not just in Europe and Asia, but also in other regions of the world. They are all tailored to the needs and crisis experience of that particular region, and are part of the global financial safety net.

Japan’s efforts to set up an Asian Monetary Fund two decades ago failed because of U.S. resistance. Don’t you think that all these Regional Financing Arrangements that we now have are weakening the IMF, which is dominated by the U.S.?

No. The global financial safety net is multi-layered, and the layers are complementary. The IMF stands in the centre of the global financial safety net, but it cannot solve all problems on its own. You can see this for instance from the fact that the ESM disbursed more than 2.5 times the amount of credit during the euro crisis than the IMF globally over the same period. At the same time, the regional financing arrangements and the IMF cooperate closely.

How so?

The IMF in a recent paper has come up with the idea to institutionalise this cooperation, and at the ESM we are clearly in favour of that. The current discussion about setting up a European Monetary Fund doesn’t mean that the IMF is no longer welcome in Europe. It’s just a reality that the IMF has reduced its engagement in Europe. And so we simply cannot rely on it to the same degree as we did in the past if there is a future crisis.

Greece is still highly indebted. Isn’t that a guarantee there will be future problems?

I disagree, and I say that because of an international comparison. Programme countries including Greece have implemented the most meaningful reforms of all industrial countries, according to the OECD. That’s why these economies are showing the highest growth rates in the euro area. Greece for instance, has managed to reduce its budget deficit from 15% of GDP to a small surplus. When looking at debt, you shouldn’t gauge the level so much, but more the ability of the country to service its obligations. And the financing needs are absolutely manageable, particularly also because of the favourable conditions of the ESM loans.

Is that really true for Greece though?

The fact that Greece was able to get access to the capital market without help from others is evidence of the economic recovery in the country. At the very least, this shows that investors have found trust in the economic situation in Greece again.

Your scenario foresees that interest rates will stay low. But what would happen if capital costs would rise back up to let’s say 5 percent, which historically is a normal level?

Our debt sustainability scenarios are obviously based on the assumption that monetary policy will normalise.

But in the past half century, we’ve seen interest rate levels of 10 percent and more. What would that do to the euro area?

Any answer to that question would be purely speculative. We may have seen the interest rate level you mention in the past because of markedly higher inflation. I don’t expect to see such extremely high interest rates again in the euro area.

Author

Rolf Strauch
Chief Economist and Management Board Member

Contacts

Cédric Crelo
Head of Communications and Chief Spokesperson
+352 260 962 205
c.crelo@esm.europa.eu

Anabela Reis
Deputy Head of Communications and Deputy Chief Spokesperson
+352 260 962 551
a.reis@esm.europa.eu

Juliana Dahl
Principal Speechwriter and Principal Spokesperson
+352 260 962 654
j.dahl@esm.europa.eu

George Matlock
Senior Financial Spokesperson
+352 260 962 232
g.matlock@esm.europa.eu