Hearing at the European Parliament's Committee on Economic and Monetary Affairs

Introductory statement
delivered by Christian Noyer
Vice-President of the European Central Bank

Brussels, 27 September 1999

It is a pleasure for me to attend today's hearing with your Committee. This is the first time that I am able to represent the ECB in the regular exchange of views between our institutions. As I was told, this is also the first time that most of you are participating in these particular hearings following the election of the new European Parliament and the setting-up of the new Committee on Economic and Monetary Affairs. I suppose that I am right in understanding that the establishment of this new Committee underlines the importance that the European Parliament rightly attaches to economic and monetary developments. Moreover, I should like to express my conviction that the new format of your Committee will contribute to improving further the quality of our discussions. I should also like to assure you once again of the great importance that the ECB attaches to these regular hearings.

For me, representing the ECB at today's hearing is all the more satisfying now that economic developments point to a much brighter outlook for the euro area economy than was the case earlier in the year. I should like, first, to present the ECB's views on these developments. Following this I shall reflect on how we can seize this opportunity to ensure that the current recovery becomes a prolonged phase of non-inflationary economic growth and employment creation, to the benefit of all European citizens. As usual I should also like to report briefly on the current activities of the Eurosystem.

Recent economic developments and prospects

The euro area economy is in the process of recovering from the slowdown in output growth which had been observed around the turn of the year 1998-99. This process is expected to gain momentum with a sustained strengthening of real GDP growth in the second half of this year and next year. The provisional result of a slightly lower real GDP growth rate in the second quarter of 1999 compared with the first quarter, which is likely to reflect some distortion in the quarterly pattern, does not contradict this projection. Overall, data for the first semester of 1999 point to a moderate growth of real GDP in the euro area, laying the basis for an acceleration in the second part of 1999 and the year 2000.

The recent cyclical movements of production have been driven by export opportunities, which are now beginning to benefit from a recovery in world trade, enhanced by a favourable competitive position. The expectation of further export growth in the period ahead finds support in the recently improved assessment of export order books by manufacturing firms. Moreover, the risks to the outlook for the world economy have become more balanced. While the possibility of a pronounced slowdown of the US economy with negative repercussions on world trade cannot be excluded, such a scenario appears, at present, unlikely. At the same time, there is the possibility of a stronger economic recovery in Asia. Overall, the brightening external environment should be expected to support the euro area economy.

As regards the domestic side, prospects are for continued strength in domestic demand. While industrial confidence has recovered to its long-term average level, consumer confidence has remained fairly close to the all-time highs reached at the turn of the year. This indicates that a broadly based recovery is under way, extending to both the services sector and industry.

With regard to employment in the euro area, we have seen continued job creation in the first quarter of 1999, but a slight slowdown in the second quarter. However, it is expected that the slowdown of economic growth around the turn of the year will have only limited negative effects on employment growth. And I should stress that this has to be ascribed to the moderate wage developments of the past few years. It is clear that a continuation of wage moderation will be a prerequisite for translating the expected growth recovery into a significant growth of employment. However, as we have emphasised on many occasions, a substantial and sustained reduction of unemployment in Europe is contingent on accompanying comprehensive structural reform measures aimed at increasing flexibility in the labour and product markets, a point to which I shall return in a moment.

To some extent, the improved outlook for the euro area economy is mirrored by the upward trend in long-term government bonds in recent months. At present, the average level of 10-year bond yields in the euro area stands at around 5.2%, or about 125 basis points higher than the level seen at the end of April 1999. Euro area stock markets also indicate growing optimism about the prospects for economic activity in the euro area. The increase in share prices in recent months, which occurred against a background of rising long-term bond yields, tends to suggest that financial market participants have raised their expectations about the prospects for corporate profitability in the euro area, in conjunction with their expectations of accelerating output growth.

While the prospects for economic activity are thus relatively favourable at present, chances for continued price stability are also good. However, consumer price increases have seen some upward pressure in recent months, rising from 0.9% in June to 1.2% in August. This was mainly accounted for by a stronger increase in energy prices, reflecting the continued rise in oil prices. As regards the outlook for price developments, while some downward pressure may be expected to emanate from ongoing deregulation and increased competition, we expect consumer price increases to rise somewhat further in the near future, mainly as a consequence of higher oil prices and the lagged effects of exchange rate developments. Looking over a horizon of 12 months or so, we expect consumer price developments to remain below the ceiling we have defined as being compatible with price stability over the medium term. However, upward risks to the maintenance of price stability cannot be ruled out, in particular in view of the rapid growth in monetary aggregates and in credit to the private sector and given the possibility of a more pronounced acceleration of economic activity than expected.

Indeed, monetary growth in terms of the broad aggregate M3 has been on a rising trend since the start of this year, moving gradually away from the reference value of 4½% set by the Governing Council of the ECB. This upward movement mainly reflected a continued strong demand for the most liquid components of M3. This may be explained to a large extent by the very low opportunity costs of holding these monetary assets, but perhaps also by the gradually improving economic conditions in the euro area.

At the same time, the growth rate of credit to the private sector remained high, fluctuating steadily around 10%. Our impression is that the high demand for bank loans is broadly based, originating from both households and corporations. The main factor behind the sustained growth of credit to the private sector appears to be the overall low level of bank lending interest rates. Moreover, the sustained growth of credit should have been supported by the ongoing economic recovery in the euro area. Furthermore, in some countries, the interplay of credit growth and rising house and land prices plays an important role, as well as the need to finance more intense merger and acquisition activity. Finally, I should mention that easier access to financing owing to the increased degree of competition in the banking industry since the start of Monetary Union may also have encouraged borrowing. All in all, monetary and credit developments signal that at present the liquidity situation in the euro area is rather generous, signalling a possible risk to price stability in the medium term, which the Eurosystem needs to take seriously.

Overall, taking into account both pillars of our monetary policy strategy, the following can be concluded:

While the prospects for continued price stability are good, it is necessary to remain vigilant with regard to upside risks. Against this background, the Governing Council of the ECB decided last week to keep the interest rates on the monetary policy operations of the Eurosystem unchanged, as it did at all of its meetings after 8 April 1999.

Conditions for prolonged non-inflationary growth

Now that the outlook for the European economy has improved, I should like to reflect on the most essential requirements for the current recovery to become a period of prolonged, non-inflationary and employment generating output growth. In our view, a period of sustained higher output growth and lower unemployment would call, first of all, for more decisive measures to tackle the still existing imperfections, in particular inflexible market structures. Secondly, the consolidation of public finances, which has made considerable progress in the past few years, would have to be continued and in several cases intensified. In many areas, the implementation of these policy requirements will certainly require a break with often deeply rooted habits and allegedly acquired rights. However, the current economic upturn would provide a golden opportunity to make serious headway in these two areas.

This message may appear anything but original, since it belongs to our standard vocabulary. However, this by no means makes the message less relevant. Rather, the need to reiterate this message casts light on the persistence of the underlying problems and the difficulty of actually implementing structural adjustment policies even when they are widely recognised as being appropriate.

Politicians are constantly confronted with such difficulties, in particular, when policy adjustments interfere with so-called acquired rights. Therefore, it is hardly surprising that efforts to correct unsustainable deficits and welfare benefits do not meet with universal support.

Even though budgetary deficits and, to a lesser degree, also public debt-to-GDP ratios have been reduced over the past few years, we have to keep in mind that this, to a large extent, was due to the low level of interest rates. At present, the budgetary situation of most Member States still needs further improvements. Beyond a further reduction of debt-to-GDP ratios, there are a number of other issues that have to be tackled by governments. These include especially the reduction of structural deficits, the reform of the welfare state and improvements to the composition of government expenditures and receipts.

Ultimately the pursuit of sound budgetary policies will by no means unduly restrict governments, but rather create the basis for an efficient conduct of fiscal policies. This, in turn, would certainly have a positive impact on economic growth and on the ability to maintain a stable and balanced social environment.

Under the Stability and Growth Pact, governments should maintain a budgetary position close to balance or in surplus over the medium term. The current economic recovery should help countries to achieve such a budgetary position more quickly than planned. In this regard, it seems imperative that higher tax receipts are used to intensify the consolidation process via the setting of more ambitious deficit targets. Indeed, the so-called automatic stabilisers should also operate during cyclical upturns and not only be regarded as relevant in periods of sluggish growth.

As regards the role of governments, I should also like to stress their particular responsibility in the setting of the overall conditions for a smoothly functioning economy. This applies not only to tax and expenditure reforms that are conducive to growth and employment creation, but also to the need to reduce rigidities in labour, product and service markets. These impediments, which have severely constrained output and employment growth in recent years, definitely need to be overcome.

The emphasis with which I am calling for such reforms stems not least from our overriding commitment to maintain price stability across the euro area over the medium term. In this regard, it seems worth recalling that rigidities in the functioning of markets are among the main triggers of an early resurgence of inflationary pressures in the event of adverse supply and demand shocks. Moreover, as a result of spillover effects, this often applies even in cases where such imperfections are restricted to only a few areas of the economy.

The attention that I have drawn to the public sector, which, in terms of spending, accounts for about half of GDP in the euro area, is also due to the fact that monetary policy is most effective when it is supported by responsible policies on the part of other economic actors. This also applies to the social partners, as they are largely responsible for the setting of wages. With regard to the latter, the key message is that wage increases which are not matched by productivity gains are undoubtedly an important source of inflationary pressures and higher structural unemployment.

It is the primary responsibility of the Eurosystem to set the monetary policy that best serves the maintenance of price stability in the euro area. In this regard I should like to stress that the Governing Council of the ECB is in a permanent process of reviewing the risks to price stability on the basis of a broad set of economic variables, whereby monetary growth plays a prominent role. These ongoing assessments include all aspects of the domestic and external economic and financial environment. Consequently, they take into account the overall performance of and outlook for the euro area economy.

Setting the monetary conditions so as to maintain price stability in the euro area is certainly the best contribution that the Eurosystem and the single monetary policy can make to creating an economic environment conducive to growth and employment. In this respect, however, we shall need the support of other policy areas. Whether the euro area will see a prolonged phase of non-inflationary and employment generating output growth depends on whether we shall be able to avoid repeating past mistakes and to decisively address still unresolved problems. If other policy-makers were to contribute to the efficient functioning of the economy by addressing the largely structural problems now, the objectives of the Community, including, inter alia, sustainable and non-inflationary growth and a high level of both employment and social protection, would be best served.

In order to enhance the understanding of what is actually required and to promote the pursuit of appropriate policies, it is certainly of use to have an open exchange of views among all macroeconomic policy actors. This should be carried out in such a way as is envisaged in the newly established macroeconomic dialogue, in full respect of the independence and prerogatives of the actors involved and without blurring the division of responsibilities in the individual fields of competence. I am convinced that the dialogue between our institutions will also contribute to a better understanding of the macroeconomic policy requirements.

Current activities of the Eurosystem

Before I finish, I should now like to draw your attention to some other important activities of the Eurosystem. To save time, I shall mention these only very briefly. However, should you be interested, I would be glad to provide you with more details on these and other Eurosystem activities at a later stage.

First of all, I am pleased to say that a little over two months ago we began the production of euro banknotes and coins. The banknotes are being produced in accordance with specifications of the very highest standard and will include a wide range of security features. Moreover, as you are already aware from your meeting last week, we have also launched a Europe-wide information campaign, in co-operation with the European Commission, to raise public awareness prior to the introduction of euro banknotes and coins on 1 January 2002.

As regards the Eurosystem's preparations for the transition to the year 2000, we are now approaching the final phase of our testing activities. I am happy to report that our testing of the applications necessary for the conduct of monetary policy has so far proved these systems to be year 2000 compliant. As far as our monetary policy framework is concerned, we are convinced that it is flexible enough and has the built-in mechanisms designed to deal with any level of liquidity demand that might arise, even under the most exceptional circumstances. Just last week, the Governing Council decided that the main refinancing operations of 21 and 30 December 1999 will be lengthened to three weeks so that no such operation will be initiated or mature during the first week of the year 2000. Moreover, in the interests of smoothing the transition, not only for EU central banks, but also for other financial institutions, we have decided to close the TARGET system on 31 December 1999. This will allow a full day for end-of-year operations and making full back-ups of all the relevant systems.

As far as TARGET is concerned, I should like to express satisfaction that the system is now widely used, as intended, for both domestic and cross-border large-value payments. The system now processes approximately 3.5 million domestic and cross-border payments per month to a value of around EUR 20 trillion. The system has clearly increased the use of real-time gross settlement in the EU since the introduction of the euro. Moreover, cross-border payments now represent around 20% of the total and 40% of the value of all TARGET payments.

While on the subject of cross-border payments, I should also like to draw your attention to the publication of the ECB's report on "improving cross-border retail payment services in the euro area". This report, which forms part of the Eurosystem's ongoing efforts in this field, outlines a number of objectives for improving the efficiency and quality of cross-border payment services.

Other recent publications by the ECB include a report on the effects of technology on EU banking systems and the so-called "Blue Book" on payment systems in countries that have applied for membership of the EU. I should also like to recall that the beginning of June saw the launch of the ECB's Working Paper series. Seven working papers have already been published, including most recently, to mention but one, "a cross-country comparison of market structures in European banking". To end, let me add that, in the interests of transparency, we intend to put together a compendium of ECB legal acts, which should also be published in the near future.

I am now at your disposal to answer any questions that you might have.

EMAC - Committee on Economic and Monetary Affairs

Monetary dialogue with Mr Christian NOYER, Vice-President of the European Central Bank

Brussels, 27 September 1999

Mrs Randzio-Plath, Chairwoman

Mr Noyer's introductory speech…..

Mrs Randzio-Plath:

Thank you Mr Noyer, Vice-President of the ECB, for that statement and I think that we really must emphasize our wish to get more information in particular on the publication of further reports, the repayments system report and your working papers. There has been progress made on these fronts over the last quarter so colleagues I will open the floor and remind you that we agreed amongst the coordinators that first of all we would have a round on monetary policy concepts and strategy and a second round then on how the ECB contributes to growth and employment and a third round on the international dimensions of the euro and the exchange rates and a fourth one on transparency and other issues.

So colleagues, as I've got a list, if you wish to be added to the list let the secretariat know. Mrs Villiers and then Mr Pérez Royo on the first round.

Do you have a point of order to raise?

Mr Abitbol:

Point of order, if I may, Madam Chairman. Several times since I joined the Parliament, since I joined this Committee, I have drawn your attention to the need to respect what I see is the first level of transparency of information; the use of the various official languages of the European Union. I am particularly amazed to see a French representative of the Bank — there is only one anglophone member country of that Bank, that is Ireland — I am amazed that he spoke English and the text is only available in English too whereas the monthly reports are also in English. Mr Noyer, my first question: The ECB, is it really without enough linguistic currency and credit currency to be able to produce it in French? Talk about dialogue with various opinions, what about French public opinion, or the north-south dialogue? I feel that the north is OK but the south is beyond the pale, so what should we do? France is not the only one, there are three countries where French is spoken so France is not the only - and there is only one English one. OK that was a statement (chair interrupts)..

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Mrs Randzio-Plath:

OK, it was a statement but look at the Rule 117. All documents have to be tabled in one of Parliament's official languages and statements can be in any language and obviously then it would have to be translated. The Committee has always respected those language rules and there is no infringement at all. I'm sorry but we have kept to the letter of the rules and it is our rules, the Parliament's rules which count here. We are in the Parliament after all and each institution sets up its own internal rules as it sees fit. We take note of your point of view and respect it for what its worth but it is up to each institution to decide on their own internal rules and we have kept to the internal parliamentary rules, so thank you. So we come to the first round, Mrs Villiers.

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Mrs Villiers:

Thank you Madam President. My questions are prompted by the latest quarter's statistics which show the renewed diversion in inflation rates across the euro-zone particularly for faster growing economies like Spain and Ireland. It also shows continuing high growth in Ireland and taken together with the significant and unexpected divergences that we have seen between some of the poor economies, particularly France and Germany over the last few months, this must of course give some cause for concern to the ECB in setting a one-size fits all interest rate. That has prompted three questions on my part. Do you expect this divergence to last? In what ways do you expect further convergence to occur and isn't the euro-zone's current interest rate level calculated to increase inflation in the faster growing economies, in fact leading to further divergence?

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Mr Noyer:

Thank you very much indeed. I shall speak in English because this question was raised in English, but before I do so, could I say in French "Talking about the first thing… I will do my best. I don't know all community languages but there is one factual mistake made. Since January, since we have been conducting the monetary policy of the euro area and started publishing the monthly bulletins, we have set up an infrastructure for these bulletins to be published simultaneously in all languages of the Community. Please believe me: it is extremely difficult, because in the monthly bulletin you find many detailed explanations in our major effort to be transparent. The economic and monetary analysis behind the decisions of the Governing Council of the ECB is available only a few days before the publication of the bulletin. We just have those few days to draft all the economic reasoning and make it accessible to all Europeans and to translate it into all Community language. Obviously these translations are also done systematically for all the legal texts which we publish. But we really wanted it to be the main vehicle of transparency, this publication of ours, this monthly bulletin. It should be published simultaneously in all Community languages to that end. Should there have been a problem or a hitch or a half day's lag in one or other of the languages, it is just a hitch in the functioning, but the principle "same day, all languages" applies. Sorry to digress"

Now, with regard to the three questions that were raised about inflation rates differential and the outlook for these differences to remain or to increase, there are several elements. The basis of course is that we have only one single monetary policy. The single monetary policy addresses euro area-wide data and euro area-wide economic developments and monetary developments. There is no way that we can make any differentiation, so if there are special tensions on one side or the other in some region, or in Member States belonging to the euro area, they have to be addressed through other policies. Now, is there something that is of special importance and of special concern for the euro area? Well if you take in comparison the United States, we have actually made an interesting study about that which will be published very soon in one of the editions of our monthly bulletin. Before it is even published, I can give you the main results of this study. It is a study trying to compare what happens in the euro area and what happens in the United States and what happens in other individual countries. Clearly there is no evidence that differences in the euro area are more important than in the United States or even in smaller economies. The differences in growth rates or inflation rates that you may observe in the euro area are not more important than what you may observe between various regions of the United States, various states of the United States, or what you could observe in the Member States of the euro area before monetary union (between some 'länder' in Germany or some regions in France) or what you may observe today in countries where there is a single monetary policy for a single country (such as the United Kingdom, or other countries where you may have differences between various regions). There is no evidence that the challenge facing the ECB is more important than the challenge facing the Federal Reserve System or the Bank of England today, or than that facing the Bundesbank or the Banque de France or Banca d'Italia and others yesterday. We think that if it is possible or has been possible to cope with that difficulty elsewhere, then it should also be possible for the monetary authorities or the other policy makers to deal with that in the present situation. Now I should like to add one or two additional remarks that may be of interest for the Parliament. There has been a number of important studies made over the years about what happens in the monetary union. That is to say that in the monetary union there is a tendency for the absolute level of prices to converge to the same level; it is not as simple as I am putting it, but the general idea is that if you start the monetary union with various regions having absolute levels of prices that are different, there is a natural tendency for them to converge very closely so that it is just inevitable that in the parts of the monetary union where the absolute level is lower, the rate of increase is higher than in the parts where the absolute level at the beginning was higher. That is the general tendency, but it is very likely that the sort of differences that you have observed for a certain time will continue to exist until the absolute levels are sufficiently close, or else will remain because there are other structural factors that enable them to remain.

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Mr Pérez Royo:

Thank you very much indeed. Mr Noyer, can I just focus in my time on two questions on monetary policy. The Central Bank, the ECB has right from the very beginning described its strategy for monetary policy as being a strategy based on two pillars. The first being growth in monetary mass which is a sort of reference value and the growth of prices on the other side stay in a band of reference values of less than 2%. The growth of monetary mass has month after month gone beyond its reference value by a percentage point without it actually leading - quite rightly - to the ECB to review its monetary policy. I think it's right that you haven't reviewed your monetary policy but I would remind you that that is inconsistent with your remit as it pertains to the growth of the monetary volume, the monetary mass. So don't you think it would be better to recognise that the first pillar, growth of the monetary volume, can really at the moment play a very limited role, especially in such situations as now, and the ECB has got to look at strategy based on one pillar, that is the trend for inflation based on price indices. In other words don't you think it would be apt and more transparent firmly to recognise that the main element of the monetary policy of the ECB is the objective of inflation? That you can have only one basic pillar and that is the inflation indices? And the second very brief one linked to that, if it is true that the Central Bank has a central objective for monetary policy and that is inflation, when does the ECB think it will publish its inflation goal, quantify it?

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Mr Noyer:

Well, on that first question, we do not feel at all that our first pillar does not provide us with the necessary information to be able to analyse the developments and the risks for price stability. We feel that, on the contrary, the two pillars give us equally important information. Obviously in the first pillar there is a risk here that it may be interpreted in the wrong way, and we have to be very cautious and that is why we said that we couldn't be content with just one. First of all the reconstitution of time series are done on the basis of estimates and we have frequent revisions of those series still today. And another important factor is the fact that there is some uncertainty as to the transmission system within the monetary union between money and price developments. That said, despite all of this and the fact that we had to carry out a number of revisions, the relationship we have been able to reconstitute over the long series which we have done, as well as over the short series which we have published since the beginning of the year, we feel that these give us a fairly good relationship. So we have no reason to feel that the data we are getting on monetary developments are particularly distorted compared to other sources which we have. If you look at the second pillar, there are two things which I might just mention here. The second pillar is very often misunderstood. It is very often presented as being an inflation forecast and the reaction to such a forecast. Well, it is not really that. It is not an inflation forecast carried out by countries which have the inflation targeting system, as it's called. It is an assessment that is carried out on the basis of all of the real economy and financial economy indicators which are generally used by Central Banks, which have a strategy of inflation targeting. They use those to produce an inflation forecast. But we have a much more complex analysis than simply producing an inflation forecast and the consequences of that, the deviation from a fixed target. The methodological difficulties which we have are even more difficult when it comes to producing an inflation forecast, the development of various indicators and the relationship between them and inflation leading to a forecast. We monitor this indicator-by-indicator and we try to establish whether the information which we have got from the majority of the indicators is contradictory or whether it goes in the same direction as the monetary indicators. It is true that for a large part of the year we obtained this information quicker than that on the reference value of monetary growth, but we saw that the jump in monetary growth took place at the beginning of this year. That could be interpreted as the result of the initial shock of introducing the euro, then it slowly grew and now we have a spread which is beginning to become significant compared to the reference value. Many of the indicators in the second pillar also give an indication of significant developments such as long-term rates etc., those kind of indicators, and then more detailed financial indicators and the real economy indicators. So I think there is quite a coherent evolution there between the two pillars, and we think that the uncertainty is similar across all of the indicators and it is only by cross-referencing the information which we get from the two pillars and all of the indications in those pillars that we can carry out a global assessment which has the best chance of being right.

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Mr Pérez Royo:

Thank you very much indeed for what you said. That hasn't really added much to what we already knew from previous dialogues that we've had with Mr Duisenberg. We already know that the second pillar, objectively, methodologically is not in kilter with the inflation objective. What we wanted was some sort of instrument of monetary policy which is more transparent, but in any case Mr Duisenberg, himself - that is why I put the question to you - allowed in this Committee that the Central Bank naturally, obviously has to have an inflation target, even if it doesn't publicise it, doesn't make it public. That was my question which I would really like to press. Secondly, it is a reiteration of the question that I made to start off with, that's true, but if it is true that the ECB works with a two-pillar strategy could Mr Noyer explain or make more tangible to us what role is accorded to the first one, the growth of M3 money supply? Could you give us more detail, fewer ifs and buts, on the role accorded by the Bank to M3 monetary growth?

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Mr Noyer:

Regarding democratic responsibility, I think that we have undertaken to do what the Treaty requires us to do, which is to ensure price stability. So if we have an inflation rate of less than 2% in the medium term, we realise that that is the basis on which we will be judged. Either we succeed in delivering that or we don't, and people can criticise us for not maintaining price stability. So we have a quantifiable objective and we have made that clear to the Parliament and to all the citizens of the Union. Now, regarding publication of an inflation forecast - not a target because we do not have a price stability target - but the inflation forecast is in fact linked to the more general question of publishing internal forecasts on economic developments, be they price developments or other variables. So far we have not been able to publish our own forecasts. We have simply made comments on forecasts published by other bodies such as the European Commission. Now why is that? There are various reasons but to give you just the main reasons: First, of all our estimates and models are very young. We haven't yet tested them sufficiently and so we do not want to run the risk of publishing forecasts which turn out to be of insufficient quality. We do not feel that this will do anything for transparency if we were to publish forecasts which have not been tried and tested under our own system. So it will take some time. I cannot tell you exactly how long. But there is the problem of being able to prove the solidity of our analytical instruments. Secondly, publishing an inflation forecast may possibly lead to our strategy being misinterpreted. If we say that we have a certain strategy, and the public interprets the forecast which we published as meaning that our strategy is a different one, then there would be confusion as to what we are doing. So we need to think very clearly, very carefully before we publish, if we decide to publish about how we are going to do it. So there are issues which have hampered publication, and we are still reflecting on this. We are not sure whether it would be positive or negative, but at the moment it is out of the question due to methodological problems and a certain amount of uncertainty which still exists in our models.

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Mr Papayannakis:

Mr Noyer, when you were speaking about price stability just now it appeared that you are favouring a certain type of monetary policy over others and you made it very, very clear that there are certain structural measures which you are going to be adopting. You talked about trying to fight against market inflexibility and trying to create a situation of wage stability. Now we knew all of that already. However we have seen in lots of countries of the European Union that lots of inflation pressure comes from other sorts of income, not wage income, either business profits or another significant source which is the uncontrollable and unpredictable income of the middle classes from investments and other sorts of business activities. You didn't talk about those sorts of income. I would like to know whether in addition to wage income you have some sorts of policy predictions in those areas as well.

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Mr Noyer:

No, I must say that it really is the responsibility of governments to decide how they manage the growth of workers and the number of workers employed in their economy. The question of entries at the border is a general economic problem. Now, one point I thought I had made in my introduction (but perhaps I didn't make it clear enough because it is linked to the question which you asked regarding economic analysis): At the moment and over recent years, wage developments have been moderate for various regions. You cited some of them and I could mention others as well and the way we interpret this is that these moderate developments have made it possible to limit the negative effects of the economic slow-down at the end of last year and beginning of this year, the negative effects on employment. So there have been beneficial effects and in the same way wage moderation has also made it easier for the Central Bank to establish price stability. We have no criticism of the social partners. We would rather congratulate them on this, but now that growth is coming back again, if we want to maximize the number of jobs created and if we want to make achieving price stability as easy as possible and for the Central Bank to have to intervene as little as possible to achieve price stability and to facilitate growth, then we think that it would be desirable for this development to continue. I mean wages should be able to increase within the limits of productivity gains. I mean that is one of the basic economic rules if we want to ensure proper inflation control.

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Mr Papayannakis:

I'm sorry perhaps I wasn't clear enough in Greek before. Perhaps I could continue in French and ask two additional questions. You talked about wage stability. I'm not talking about that but I think that most of the pressures for inflation come from the middle classes, from investments and other bad business activities. I asked before: What sort of policy are you planning in those areas?

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Mr Noyer:

Excuse me. It is clear that that is a general rule. Any growth in income in a specific sector which is not linked to an increase in productivity is going to create an inflationary pressure and so we don't want to encourage that. But we are not trying to take the place of the social partners and you said quite rightly that inflationary pressures may develop in the services sector and may not be linked to wages as such.

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Mrs Randzio-Plath:

I'd just like to point out that we are now taking questions on monetary policy and we are going to come on later to monetary growth and employment policy.

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Mr Lipietz:

Vice-President, I would like to thank you very much for this very frank presentation. I have two questions on monetary policy and more in general on price policy, growth I will come back to later. First of all management of monetary policy. One of my questions relates to that and then once again I want to put a question on your objectives. But first of all on management: I very much appreciated the fact that you made such an open and frank presentation and I think quite rightly you have left behind the caution which is usually exercised which means that bodies do not comment the policy being pursued by other organizations. You haven't hesitated to criticise and make recommendations to the Governments, to the Parliament and to the Social Partners. And you have done this in quite an outspoken way. And that was the first thing that I was quite surprised about. I was surprised that the text which the Central Bank has written to the Parliament only uses two of the languages of the Parliament and it is really quite outspoken. You talk about acquired rights, alleged acquired rights. In fact you're very often talking about conventional, acquired rights which have been set down in conventions and you seem to be contesting the legitimacy of those. Now I wonder what exactly do you mean by that in French? If you think that each authority has the right to make suggestions to other authorities which I think is quite right when it comes to economic policy and the price stability objective, what weights would you give to agreements, conventions compared to the decision in which you take in the Central Bank? If you think that there should be a dialogue and that each party can make recommendations to the other. Well there I would like to ask you a question on targeting. You have made a very specific recommendation for one of the partners in fixing price stability which are the social partners. You recommend that wage increases should be matched by productivity gains. Now you haven't said the same things for profits, that increases in profits should not exceed increases in productivity. Now why haven't you done that? Now I would just like to ask how do you define increases in productivity? What aggregate do you use there? Because you were quite right in saying that as a Central Bank we would not be able to fix an objective except for Europe as a whole, but have you fixed an objective for all of these sectors? For example when you are establishing a price target within growth over not more than 2% in the medium term? Do you think that for consumers that is acceptable given the fact that there has been more than 2% change in inflation in the various sectors?

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Mr Noyer:

In principle, first of all I think it is quite clear that what has been decided or what is to be decided by other actors, whether they are acting with the authority granted by democratic representation or whether they are acting in their own right, in either case I think that it is quite clear that they are completely free. We cannot dictate any terms to them. Now, you might think that the recommendations and analysis were a bit strong, a bit harsh, but I do feel that it is very, very important for each actor to act in or take decisions in complete independence without being pressured by anyone. I think that has to be respected. It is true for the Parliament, for the social partners etc. All we can do is draw up analyses and publicise those analyses and our beliefs, our convictions to say what we think the causes are for the trends that are being observed and then they can decide on their own. The actors can decide on their own, it's not for us to decide. Now you asked how what I said before would be actually translated into practice. I didn't want to give specific quantified figures: that would cry in the face of respecting the principle of independent action for the other actors which I have just subscribed to, and another question or another principle which is very important to me is that there is not just one rate of productivity that you have to look at in one industry, in one part of the economy. We have a very diverse European economy throughout the euro area. There are many, many different patterns of economic activity and development from one sector to another, from one industry to another and even from one company to another. So we in the European Central Bank feel very, very strongly that the economy should be decentralised as much as possible today and what might be desirable in the case of one company or in certain cases of one region or even a larger area or an industry shouldn't necessarily be extended to the entire euro area. There might be productivity increases which are lower for one company at one time than they are for another company at another time. Further, those relations might change a bit down the line and you need to allow for those sorts of fluctuations. Now I know that everything I'm saying is a bit genera,l but that's the overall concept. I think it's a fairly straightforward concept. Certainly if a company wants to avoid increases in costs, then its tendency is going to be not to participate in a price increase which would not be in keeping with our target. I think that everyone agrees to that. Thank you.

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Mr Schmidt:

Thank you very much Mr Noyer. Well my question is a general one relating to both parts of this question and answer section so I hope that the chairman will allow me to deal with both points. I would like to hear what you think the effects of the euro will be in general, particularly in view of the fact that four countries are not participating in the euro zone. I would like to hear your analysis of that? Do you think it has negative effects or positive effects in respect of developments in general?

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Mr Noyer:

Well, the effects of the euro should really be analysed in view of the effects on the eleven countries. Of course all the countries would be welcomed by the European Central Bank, I mean all the central banks if they were to decide to come in, but that is a political decision and we have no view to express on that. The only commitment we feel we need to make is to be prepared at any time to have them on board. Now, what we are doing presently, because we think that it is purely a requirement of the Treaty and we have to do it, is to monitor on an ongoing basis the economic developments so as to be prepared to make a convergence report at any time, and we follow the developments. We have regular discussions with those responsible in the central banks to discuss developments, exchange views about the progress being made in some fields, the challenges that are ahead for these countries and what would happen if they wanted to join. We know that in some cases there is a clear political wish to join and of course we take this into account and we prepare ourselves to write the convergence report probably as soon as by the middle of next year, but we don't feel that we have to judge or to decide in any way on monetary policy while taking into account the interest of outside countries. I mean this is not what is required of us by the Treaty and we have to take decisions in the sole interest of the euro area. This is our understanding of the Treaty.

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Mr Goebbels:

Yes thank you very much chairman. I was very interested to hear Mr Noyer's presentation when he spoke before. He said that the Bank's objective was still price stability as it was before. I did take note of that. I also noted that the Central Bank does not seem to be too concerned about recent price or inflation pressures as a result of increase in oil prices. On page 4 you say "continued price stability is also good" and then, "looking at a horizon of 12 months or so we expect consumer price developments to remain below the ceiling we have defined as being compatible with price stability over the medium term". Now what does that mean exactly? Does that mean the European Central Bank and its monetary policy is going to provide an opportunity for an economic upturn in the coming months?

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Mr Noyer:

Well, certainly the European Central Bank does want to give an economic upturn a chance in the coming period. Let me just point out that we do feel that we have fully taken on board the need to provide the best possible economic environment, and we did that in a very straightforward way. This is a general remark which I would like to make and I would like to thank you for allowing me the opportunity to do so. In most cases, there is no conflict or contradiction between economic policy providing the best possible economic environment for growth, and a policy which would allow for price stability at the same time, and I think that the case that you just mentioned is an illustration of that general rule. At the time of the reduction in interest rates, there were not very many risks for a significant increase in inflation. There were much greater risks for a decrease in inflation and at the same time for a downturn. Our medium-term goal of price stability had to be given priority. We thought that it was a good idea to slightly decrease our interest rate in that direction and in that way we think that we also helped to foster an environment of trust. I think that basically we managed to get a good balance of policy in terms of its results. We have been focusing on medium-term price stability and we do feel that that also, at the same time, creates the best possible environment for the maximum rate of economic growth and to create jobs at the same time. And now to take that thought just a bit further. Certainly I don't want to try and anticipate decisions that might be taken, but I do think it's clear that today in the euro area we have a monetary policy which allows for a great amount of monetary flexibility. We have a large money supply and a low short-term interest rate as a consequence of what we decided in early spring for the reasons that I mentioned. There is a lot of flexibility for financing which at some point might not be compatible with combining increased growth and maintaining our primary, medium-term objective of price stability. For a number of months now we have been saying just that. We have been saying that our monetary policy is not going to keep changing in the direction of further easing for the next months. That is a very, very cautious guess but we didn't want to do anything overly hastily or too rashly. We are, however, aware that the upside risks now are becoming a bit greater than the downside risks. That's a change. It is possible that we will have to do something at some point in order not to compromise our medium-term goal of maintaining price stability, to take some sort of action. It would always be better to act in time proactively rather than doing so too late after the event and in a rash and hasty way. It is possible that we would have to take that sort of action in the future. I don't think that it would have any sort of negative or adverse impact on economic growth, but we may have to do something in the future in order to maintain our price stability goal.

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Mrs Randzio-Plath:

Can I come back to that question and just put a supplementary question. When you say that you have this room for manoeuvre with the definition in the medium-term. Does that mean that in the short-term that you would be prepared to allow an excess of the 2% rate and that you are considering one day amending your very rigid definition which today is below 2%?

Mr Noyer:

Thank you. Well that is a crucial question. I would like to express my gratitude for that question and also to Mr Goebbel's question. Now, we certainly can't try to completely control short-term price changes. To take a specific example, let's take oil prices which we have seen can drop quickly or can rise very quickly, so it's entirely possible that you would slightly exceed the lower limit or the upper limit of 2%, let's say for one month or two, because we won't be able to react in such a term, but if you see that it has gone above the 2% mark just for a month or two and then it drops back down again and it remains within an acceptable range after that, that's what I meant by saying that we have a medium-term price stability policy. Let's say in January you slightly exceed the 2% ceiling, then the other eleven months of the year you are below that ceiling, then I think it's clear that overall we have managed to do what we said we would do which was to keep prices from increasing at an annual rate of more than 2%, so we would have been successful in that case. Having said that, I also want to make clear that we don't just want to stick to a goal of 1.99% when we say it's going to be below 2%. We want to have sufficient margins so that we'll be safely within our objective range at all times. Now you said that there might be some sort of incident as a result of an external shock and which could upset that development, that pattern, but if you see afterwards that you are going back very quickly then I think that you are going to have more of an upset than you would if you had a more stable development without this sort of sharp upturns and downturns, and that is why we are trying to anticipate economic developments, to act in time and to take on board all possible impacts of our decisions.

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Mr García-Margallo:

Thank you very much indeed Mr Vice-President for being here and I'm glad you are. I would like to put a couple of questions to you. I have got a report which I have to draft. Given the instrumentation of monetary policy anchored basically in an open market system, would it be useful or not at all to have more integration of the financial markets and more coordination of the stock markets? If you say yes that would make the sort of instrumental panoply you have of monetary policy more easy. Are you going to keep financial decision making nationally or should there be a sort of supervision of financial policy at European level?

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Mr Noyer:

For us the most important thing definitely was to have an integration of the bond markets and short-term money paper markets, because these are instruments which are very useful for the proper workings of monetary policy and the payment systems because, as you know, in the implementation of our monetary policy, we do use mechanisms for feeding the market which is based on the presence of collateral. So we need a very liquid market, a very fungible one of debt title paper which could be used as collateral in the TARGET payment system and other systems (TARGET and its various component parts) so that you can exchange liquidity in real time and have a single interbank interest rate within the whole of the euro zone. We need collateral which is totally fungible and we appreciate seeing the unified nature of the market. Now the shares market is getting a bit further integrated, even though we don't actually use it in the same way. In the general logic of consolidation and creation of a single market and, therefore, of wealth, we don't need this directly although my feeling generally speaking is that it is in the interests of all the citizens of the euro area and the economy of the eleven to have an attractive financial market for the whole world - not just home investors, but those outside the euro area as well, so that these markets are visibly and clearly as single as possible. There might be various ways of doing that, you might have different stock markets if they are linked, interlinked electronically, or mechanisms which would allow free operations from wherever you may be and still get the same result. Now monitoring authorities. Well, the centralisation of these will depend on market developments and trends. I think it is good to have a greater unification of the rules as we have done in Europe on the banking side.

Some people have banking laws, rules for buy-outs, currency exchange, all sorts of things, all the main areas are covered and as unified as possible and we've got to see that as far as possible in Europe. So you may need a single authority or perhaps more simply greater cooperation between the already existing supervisory authorities. So what we've started doing under the remit of the Treaty in cooperation with the authorities and banking supervision, we have a Committee which provides coordination in this field, makes sure that bilateral notification exists and that various authorities which operate in several markets do cooperate. Maybe I am ranging too wide here because my competence in this sphere is not that great and I'm really speaking personally and off-the-cuff.

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Mrs Randzio-Plath

Before we now talk about growth and employment and the role of the ECB, before we get to those two areas, Mr de Gaulle.

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Mr de Gaulle:

Yes, Madam Chairman. A point of order. I'm amazed I asked for the floor and I was recognized but I had to wait until a lot of people who hadn't really been on the list got it, and I had to wait about one hour and a half. It's a typical example of the sort of transparency which exists in the European Parliament. You ask the European Central Bank to be transparent. I think first of all you have got to show it yourself.

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Mrs Randzio-Plath:

Sorry you weren't actually written in the list. I'm sorry.

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Mr de Gaulle:

But I did put my hand up. Oh it doesn't matter. OK. Mr Noyer, you tried to defend the modest nature of the euro zone in economic terms. I think you a bit underestimated the heterogenous nature of that zone because the monetary and economic policies of countries in the euro zone are very different. Take Spain. You see an inflation rate which is growing fairly swiftly with an industrial production which is also growing; France which is improving but fairly averagely; Italy where you can see economic stagnation. So sooner or later you are going to have to choose when it comes to monetary growth. When it comes to increasing interest rates you are going to have to choose between one or other of those countries. Spain has got an inflation rate which is very high and very low inflation rate in other countries. So how will you manage that contradiction?

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Mr Noyer:

We won't be choosing between the countries. In fact I don't even have to look at the inflation rates in various countries, I have to look at the overall inflation rate. What did the Banque de France do yesterday, last year? - it didn't consider whether the parts of the

Pyrenées had an inflation which was greater or lower than the Nord Pas de Calais, or whether the Brittany inflation rate was greater or lower than the inflation rate in Aquitaine. In the same way, we don't consider if the inflation rate in one country or another is different - at least not for taking our decisions, and I would assure you that the variation of prices between the north and the south of Italy, some parts of east and west of Germany, the north and south of France, and, as for countries which have not yet joined monetary union, the north and south of the United Kingdom, can be greater in fact than the average differences we see within the euro area taken from one country to another. So we have no methodological difficulty. It is not a question of choosing one country over another. We have a classic problem here of different trends from one town to another, from one region to another, and in our case from one country to another but conceptually it is all the same to us. We have to look at the overall aggregate interests of the area as a whole. Take some specific examples which you raised. I was very happy to note that in the case of Spain, developments have been recently progressing towards the European average, and that the rate of growth in Italy is tending to increase towards the European average. The most recent developments are really rather satisfactory and are tending more towards convergence. There might be some time lag involved, but in the various economies of the various countries over various and varying time periods, and depending on the cycle and the recovery, economic trends seem to be going in the same direction.

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Ms Lulling:

Many colleagues have raised issues with respect to conditions for prolonged non-inflationary growth. First of all I would like to make one comment, because we do have grounds for concern in respect of the Maastricht criteria, in particular the budget deficit, and even more the long-term debt of certain Member States, in particular Belgium and Italy. With regard to Belgium, I would like to ask Mr Noyer, is there no risk of slippage after this dioxin scandal and its costs linked to the two criteria I just mentioned, and also reform of the welfare state generally. I would ask Mr Noyer to give us a better idea of what he means by this reform. What about reducing rigidities in labour? What does that mean? Is he looking to laws on labour contracts, or leave? Are we looking to legislation such as exists in my country with respect to a sort of mobile salary scale, automatic adaptations in all directions if I would dare to put it that way, or where everything is indexed to prices all over the place? What Mr Noyer has said so far is too vague. I very much agree with Mr Noyer when he warns about the dangers of expenditure in the public sector, which calls up more than half of the GDP in the Euro area. Also, in the same paragraph he talks about the necessity of matching productivity gains with wage increases. I fully agree with him, but how is he going to gauge that? How is he going to measure these productivity gains, above all in the public sector, where, at least in my country, it is extremely difficult to adapt working conditions and wages to these sorts of criteria?

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Mr Noyer:

Thank you very much indeed for the question. You mentioned trends in deficits and public debt. I don't want to emphasise the case of a particular country too much, but you mentioned Belgium. Insofar as I know, we don't have any forecasts different from that of the Commission on this specific case and I have to say from the Member State itself. So it seems that despite the dioxin scandal and negative economic effects it will have on growth, specifically this year, the primary surplus target will be met. The deficit has remained the same and in fact improved —thereby improving the public debt situation as well. In some cases you have to imagine that this sort of case might give rise to a blip on public deficit trends and the Stability Pact to which governments are committed. Do bear in mind the existence of that sort of risk. That's why you've got to have reserves in order to be able to fight the risks from asymmetric shocks and in this particular case Belgium is being very, very careful with its public expenditure. I'm sure they can cover the expenditure this year for that accident.

Now, overall, talking about the welfare state and structural reforms, particularly in the labour market, but also in the goods and services markets, we are trying not to be too detailed in our recommendations for a very simple reason. First of all, the work has already been done by other institutions. Above all, the OECD has undertaken work that has been widely debated amongst Member States and there's a great deal of consensus. It gives country-by-country and in detail, the sorts of measures that would be useful and necessary, to reinforce growth and increase the potential for growth, so I think there's about 99 if not 100% agreement already on those sorts of analyses. We try to avoid being too specific also on recommendations for specific measures for specific countries because we think it is not up to us to say to the government, 'look you have got to do this, you have got to propose such and such a bill to your parliament and such and such a reform to your social partners'. I think that oversteps our responsibility. I think we have to remain more in the realm of the general.

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Mrs Randzio-Plath

You talk about analyses, positive developments in growth, OECD, etc. for the Euro 11, you seem to share those analyses as a point of departure. In your opinion, is there a threshold for non-inflationary growth where the European Central Bank would actually have to intervene, where you would be supporting this policy through your interest rate policy and then having to tread on the brakes? Do you have a threshold value which you would work with in that respect? I would very much like to know what that would mean. For example, going to social partners and calling on the governments to contribute to acceleration of growth, making recommendations to them in that direction? Is there any risk involved here for you in doing that? I would like to know, when you criticise the financial policies of certain countries, what does that mean? You were talking about using their surpluses to generate more internal consumption and therefore growth, or telling them to invest it. The investment rate in the Euro zone seems to be still too low. What are your thoughts on that and also your role in the macroeconomic dialogue? On 8 November we are going to be looking at this in Helsinki. What is the point of the macroeconomic dialogue? If you look at inflation rates and deficits we do have figures, but where it comes to investment and growth and all the rest we do not even have any benchmarking. Is it even possible for it to succeed and is it possible without political institutionalisation in some sort of pooling of economic governments?

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Mr Noyer:

I was probably wrong to refer mainly to the OECD, because in fact I should have started by saying that also the Commission has made a number of studies and is in the process of preparing a proposal for broad economic guidelines for next year that will certainly come here and will be discussed by the Council of Ministers. I know they have tried to greatly improve the study of the sort of structural measures that would help to foster growth potential and employment in each country, so the work that can be done inside the EU addressing the specific problems of the EU is certainly very, very important. Here also, from what I have seen until now, I think we would fully agree with the Commission, but it is really much more the responsibility of the Commission to propose precise measures to governments and to explain that before parliaments than for us to do so.

What is the economic growth level above which we would see danger for inflationary pressures and we would react? First of all, you should not interpret a possible move in the future in our monetary policy as wanting to hold and restrain the continuance of economic growth. That would mean simply that at a certain time, I don't like the term neutral monetary stance because I do not think anybody is really able to describe a neutral monetary stance, but the concept, more or less, is that at a certain time we would adopt a monetary position that was designed to assist the resumption of growth. Now if, and I hope rather soon, we revert to economic growth that is more or less close to the potential, we might wish to have a different monetary stance, but that does not mean that we would like to slow down the economy, not at all, but simply to avoid it having consequences in developing price pressures that would oblige us to react sharply with a risk at that time of creating problems for the continuation of economic growth. We have, of course, to assess risks at any time and find the best possible monetary stance to avoid the development of risks on one side, and also help the continuation of sound, non-inflationary economic growth.

Your question was also, is there a figure? Well, historically it seems that the potential on average that is the growth rate that could continue with the possible avoidance of excessive price developments, was around 2½% on average. Our conviction is that if a number of structural reforms are pursued, this could enable the potential on average to be higher, i.e. that it would enable higher growth without inflationary pressures (forgive my words, they are over-simplified), but one could imagine that more than 2½% without some accompanying measures would mean a threat to price stability and oblige us to react with some pre-emptive moves. One could imagine that a growth higher than that with some structural reforms would be tolerable and would not signal risks to price stability.

Now, for the policy developed by the social partners, I do not think I can add much to what I said earlier. They have, of course, to be aware of their full responsibility. The fact that the situation is different, as I said before, from one enterprise to another, from one sector to another, means that there is no general figure we can give. The rates of productivity growth are to be measured enterprise by enterprise. As for fiscal policy and budgetary policy, of course we are fully aware that a number of tax reforms that are either performed or planned by the Member States are part of the structural reforms that we are calling for, and so in a sense we can only compliment those governments that propose to their parliaments to take such a tax reform, as far as this decreases, for instance, the cost of employment for low skilled workers etc., and certainly this has to happen and must be backed and complimented. This being said, we think that when/if there are golden years where economic growth is very strong like for example what happened in 1988-92, at the time it was clear that in a number of Member States the measures were not taken that would have enabled those Member States to approach what now has been stated as a goal in the stability and growth pact, that is to come to a budget close to balance or in surplus. If this had been done at the time we would probably not have been confronted with deficits higher than 3% and a very rapidly growing debt to GDP ratio when the recession came in 1993. So, our message is that governments should be aware of that and take the opportunity of better growth, of stronger than expected receipts, to go further and quicker in the reduction of public deficits. But of course the exact measures in terms of what they want to do to address the problem of tax reforms that are needed and to increase the speed of reduction of deficits is certainly their responsibility.

As for investment, we have the impression, but of course this is also very much a decision to be made by the policy makers, by governments and parliaments, we have the impression that the rate of public spending overall in the Community and in the euro area in particular is relatively high and that within a given amount of expenditure, what really counts for developing a public policy is the choice being made between, for instance, investment and current expenditure. It seems to us that you can very well have within a ceiling (if you decide to have a ceiling on public spending and therefore the avoidance of public deficits), real policy choices between different sorts of expenditure, and that the choice to make more expenditure in the field of investment and less in current expenditure is probably also extremely helpful for higher growth in the long term. So I would completely agree with you, but without thinking that if you want to increase public spending for investment that that necessarily means either to increase expenditure and/or to increase the level of the deficit.

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Mr Abitbol:

MEPs cannot carry out their work properly if they do not have a document in their own language. I would like comment on the basis of a text in the French language, but I cannot understand this text at all. I wonder if next time the ECB would be so good as to give me documents at least in my language? I think a lot of other MEPs would agree with me with respect to their own respective languages.

My question is about the hostility to the principle of the single currency which existed very strongly in some countries. In France pretty much half of the French did not approve the creation of the Euro. It is a fact that the Euro wants to continue a sort of *"franc fort"*, the strong franc policy which gave low growth and a lot of unemployment. Will the Euro follow on this " *franc fort*" policy? The nascent Euro is a Herculean effort and the press has saluted it as such, but will it continue that way? We seem to be more flexible when you compare it with the dollar and in France and Germany I think we've benefited from the strength of the dollar. The Euro seems to have been fairly flexible, is that just something which is a short term tactic and in the long term you are going to go back to the rigid " *franc fort*" policy? Are you going to continue with the flexibility policy? Remember we lost a lot of jobs through the " *franc fort*".

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Mr Noyer:

I cannot give you any figures for the problem to which you refer, but you talked about the costs involved in the past when it came to growth and, on the other hand, jobs. I do not think that this is necessarily specifically linked to the external value of the franc and am convinced the opposite is the case. I think at a given point in time, what gave rise to problems in the EU and the European monetary system was the fact that we had monetary crises which could have been due to erratic movements of third currencies. Sometimes when there was erratic movement between the dollar and European currencies, there were small "tectonic plates" that gave rise to tensions within the European monetary system. It was a natural market reaction. Sudden changes in interest rates? Central banks did that to try and make sure that the system did not break down, but it did also flag the necessity that when there was this basic political decision to create the euro, that also included within it the fact that they wanted to get rid of these sorts of risks after we set up the euro. It was a political decision and at the end of 1998, immediately afterwards, when there were international currency tensions, there was no effect internally within the euro area. Interest rates continued to converge, currencies were close to their central parity rates which were established for the definitive translation into euros and all these tectonic costs were avoided because there was a political strategic decision to create the euro. At the moment the landscape is fairly peaceful and there is no risk of these tectonic tensions because national currencies do not exist anymore independently. We have the euro, there is no internal tension and trends are not influenced by the costs we have had in the past between the small currencies and the larger currencies, which were greatly protected.

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Mr Abitbol:

I seem to remember that last autumn the currency tensions were pacified because the dollar was so gracious as to rise at the time, not because of what you said.

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Mr Noyer:

Well the experience of the past shows that a sudden increase or a sudden drop in the dollar can both give rise to tensions within the system, not necessarily affecting the same currencies at the same time, but anyway, sudden swingeing changes outside can give rise to tensions within and give rise to reactions. That's gone. Other than that I would just say that we now have the euro which you know - and it is established in the Treaty and we have a new European Central Bank to implement the Treaty - is firmly rooted in price stability. On that basis, the euro has potential for appreciation which should I think become manifest as and when we get to stronger economic growth, and that will not have negative economic consequences.

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Mr Lipietz:

Well given that we are continuing this dialogue between all of the authorities, you said, quite rightly, that each authority tries to convince the others of its opinions. I would just like to ask you to shed some light on recommendations that you have addressed to other authorities and then ask a question about your own intentions. Regarding the recommendations you were making to their organisations, well first of all you talked about budget deficits and it is parliaments who fix the budget deficit and not the government, so you have recommended to parliaments that there should be a zero budget deficit or a surplus in the years to come, whereas the stability pact says that there should be a budget deficit of no more than 3%. Do you not think this could have a deflationary effect and negative effects on employment? You have also recommended to the social partners, and you mentioned earlier that there should be decentralised determination of wages and there should be growth and salaries equal to growth in productivity. Now you have mentioned that there is a lot of heterogeneity between the various sectors, and clearly there will be some sectors where productivity increases twofold whereas other sectors are stable. Do you think that at the end of four or five years that the workers in those sectors should have twice the salary rise of for example hairdressers?

The question that I would put on your policy in the Central Bank is if you have established an objective of about 1.5%, I take that rather than 1.99%, inflation, given that there is about 2% of a discrepancy between the consumer price index and the industrial price index, do you not think that that kind of policy would have a negative effect on employment?

Finally, you talked about policies for sustainability and I'm very happy to hear that, but how do you think the Central Bank can contribute to sustainability? Do you think that we should have lower real interest rates for loans, for example, to railways so that we can meet the commitments we entered into in Kyoto?

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Mr Noyer:

Regarding the fact that deficits are defined by parliaments, well the growth and stability pact does not only establish a limit of 3% for deficits, it also very specifically lays down a general rule so where you have normal growth developing over two or three years the target should be a balance or a surplus, those are the exact words used in the growth and stability pact which was adopted by all of the Member States. Now I would just like to let you know what my personal conviction is. I am a member of a generation that had a lot of opportunities. From our parents we inherited an excellent public financial system, demographic conditions that are very easy, it was very easy for us to finance our parents' pensions, and all of that despite the fact that the generation which went before us went through terrible tests and tragedies which we did not experience at all in our generation. What we are going to be leaving to the next generation is a very difficult demographic situation, accumulated social and public debts, whereas we have lived in a period where there have been no major disasters in the world and a fairly stable economic situation. I think that we have considerable responsibility there vis-à-vis the next generation and the European Central Bank takes that into account. We react in part as citizens and we feel that it should not just be left to authorities, which will have to take political decisions over the next 10-30 years. We have to ensure that they are given a manageable situation so that we do not have very low growth or dangerously high inflation levels and I think that is part of our responsibility as the European Central Bank. We must have a long-term vision and luckily we can do that because we are not constrained by very short-term preoccupations, and I think it is part of our duty to help governments and parliaments to take these decisions and to take into account these issues such as demography and the responsibility we have to future generations. I think it is unacceptable that we should simply leave that as a legacy to our children.

Regarding the decentralised economy. I think that if you take what I said literally then, yes, it would be acceptable to have different developments between different sectors. The reality, however, is, as we have seen happen in the past, that prices would go up more quickly in some sectors compared to others because the productivity gains will not be uniform throughout all the sectors if you compare, for example, the car industry and hairdressing. It could be found unacceptable to have different wage developments because of different productivity gains, so what I said should not be taken too literally. Depending on the sectors, that relationship between price developments and productivity gains cannot all be determined in a purely mechanical way, so you have to take the analysis a step further and look at sectors which are exposed to national and international competition, which sectors are less exposed, and we know the way in which economic operators and social partners can effect wage development and price development depends to a great extent on the amount of competition. On the other hand, I do not think the fact that production prices in some sectors are going down is necessarily a sign of deflation. We have seen in areas such as information technology and electronics over the past few years prices decreasing simply because it is quite a young industry, because you have a huge amount of technological progress and therefore gigantic leaps in productivity and those productivity gains have been passed on to the consumer in the form of lower prices without that creating a risk of deflation. For example, the fact that the price of mobile phones is decreasing does not mean that there is a danger of deflation. It is linked to the great and very fast technological developments where the consumer is benefiting from the fact that the industry is developing so rapidly.

With regard to the question on sustainability and whether it will be possible to have different real interest rates for different activities, I think no, not as a result of monetary policy, but if you were to take, for example, the idea of promoting certain sectors where economic profitability is difficult and whether we should manipulate interest rates to address that system, whether budgets or elsewhere, I do not think that is the most efficient way of doing it. I think if there is an economic benefit to be gained from doing that, you should do it either by regulatory measures in some cases or by a clear subsidy for a non-market activity. If there is something in non-market activity that is of benefit to the general public then it should be financed in this way, but I do not think that trying to give subsidies by manipulating interest rates is the most effective way to take action because there would be indirect mechanisms that would be more difficult to manage and more expensive.

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Mr J. Evans:

Can I compliment Mr Noyer on the clarity of his introductory statement. He said that it came from the standard vocabulary of the European Central Bank and I would be grateful if he would consult the dictionary in order to give me some further definition of some of the expressions that he used. I thought listening to his introductory statement I had a very clear idea of the message that was coming from the Bank, that is that there were imperfections in inflexible market structures within the Euro zone area, that there was a need for continued wage moderation, that there needed to be, as he described it, substantial and sustained action taken and accompanying comprehensive structural reform to increase flexibility in labour and product markets and more decisive methods, he said, to break with deeply rooted habits and alleged acquired rights. Now that gives me a very clear impression of what agenda he feels needs to be pursued in order that we see growth within the Euro zone area. But as he answered questions, not least to you Madam Chairman, he seemed to leave me with the impression that if nothing changed we might still see a situation of growth of the order of about 2½% and I am bound to say I am rather concerned by that because it certainly will be my impression that unless the issues of structural deficits, with the welfare state cost of the present time, and the other matters that have been identified in terms of inflexible market structures are addressed then there is a risk for the Euro zone area itself and for all of us who are within the European Union. I wonder if he could just clarify that conundrum for me. Is he saying that if we do nothing that we can look forward to 2½% growth, but if the weather improves we might do better than that, or is he saying, as I hope he is saying, that within the Euro zone there is action that needs to be taken, although, of course, as Vice-President of the European Central Bank he leaves it to governments to decide what that action should be?

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Mr Noyer:

First, I should have said that the historical average of growth is not 2½%, but between 2-2½%, that would have been more accurate. Secondly, I should have said that if nothing is don, it is possible that the average would, in fact, be lower than the historical average. If things are done, we may hope that it would be higher than the historical average, that is in one case going back towards 2 or even less, and in the other case going up towards 3 and maybe more, so I would fully agree with the way you have restated my judgement.

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Mr Bullmann:

Well this is just the beginning of the dialogue on the responsibility of the European Central Bank in the real economy and I think it is good that you have taken this step to talk about that real economy responsibility. One thing that has not yet been quite clear is your reply: your strategy for dealing with that responsibility which has been entrusted to the European Central Bank by the Treaty. It has to be done not by the Commission or by governments. I would like to know what strategies and what recommendations the European Central

Bank intends to use to deal with that responsibility. What about external shocks, rising oil prices, the possibility of an economic downturn in the US and the fact that we will be able to reduce unemployment in the long term if growth exceeds productivity gains for long periods. What is your recommendation to individual governments?

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Mr Noyer:

Certainly, we have to take into account all relevant economic data, all economic events; we have to take into account developments in oil prices. It is our judgement that in themselves developments in oil prices do not mean that there will be adverse developments for price stability, if nothing else happens. But, of course, the risk is that it creates what we could call second-round effects. We must remain extremely vigilant, because if it was only oil prices and the increase were to disappear after 6 months/1 year, it would not be a major cause for concern, exactly as the decrease of prices one year ago did not in itself represent a danger of deflation. The danger was that there would be second-round effects. This has to be taken into account. All shocks have to be taken into account. Concerning the objective, I would fully agree with you about the need for the highest possible economic growth and the need to foster employment. I think President Duisenberg has said several times that we fully share the view that I think is the view of your Parliament, that the present level of unemployment in Europe and in the euro area is absolutely unacceptable, and this explains in part the rather strong statements that I made on a number of policies. We have that in view and we think that all economic actors should make all possible efforts to help reduce the level of unemployment and take the opportunity of forthcoming stronger growth. Certainly all international events are part of the global assessment that we make. We know that the rates of growth, not only in the United States but also in all the international partners, do count. They have an effect on our own internal growth and economic development, and in some cases they may also affect the development of prices if the prices of imports or the pressures on exports or imports are such that they may have consequences for our development, so we fully take all this into account in our assessments.

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Mr Theonas:

In your introductory statement you seem to be very optimistic as far as the prospects for an upturn in growth are concerned, although you did say that that probably would happen next year. So for yet another year in a row we have to wait until next year to see real results. We have heard that one before. If we have an increase in growth, let us say around 2%, a little bit lower than 2% or even around 2½%, would that be a safe rate of growth? Do you think that with those sorts of low rates of growth increase that we are going to be able to deal with the problems of unemployment that you just mentioned in an effective way? Secondly, we see that there are lots of efforts being made now to concentrate capital into a smaller amount of "big hands". You see Michelin for example, which is now making many workers in France redundant, despite the fact that they are concentrating more power, they are making more and more profits and they are not in any economic problems. Do you think you can do anything to influence those company policies? Finally, with the policies that you have been mapping out, which I think are actually taking money away from real prospects for growth and development, do you think you can actually help growth potential and the creation of jobs?

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Mr Noyer:

The average rate of growth of between 2-2½%, yes, is sufficient to create employment, but of course it would be of the utmost importance to try to increase that rate of growth to foster more employment growth, and I would say also with a given growth rate to increase the employment content of growth, that is available through a certain growth rate. What I tried to say is that we are convinced that by making a number of economic reforms we may achieve a higher average growth rate without endangering price stability - a growth rate that is sustainable, that is feasible, for non-inflationary growth, of a sound growth, that this growth rate is higher if you increase the flexibility of the economy. We may have more growth with no more price pressures. That is basically the message that we give. So we turn to governments and parliaments and we say, if you make a number of these reforms, which we will not prescribe but which should be discussed with the Commission and between yourselves, but if you do make a number of reforms, it will be possible in the coming years to have more growth and more employment. It does not mean that with the track record we have had in the past there will not be some employment creation, but not addressing the enormous amount of unemployment that we have to try to get rid of, that is the message.

As far as mergers and acquisitions are concerned, I would like to answer indirectly. What is remarkable in the American economy is that it is so easy for a large number of individuals to create and develop new businesses that if suddenly in the United States the same number of jobs were to disappear as happens in Europe, the difference would be the number of newly-created jobs, the number of businesses developed by new entrepreneurs. Do you know that there are thousands, probably tens of thousands, of young Europeans who leave this continent to go to the United States to create businesses because it is so much easier to do that there and they create jobs in the United States instead of creating them in Europe? They have the ideas, the knowledge, the wish to create businesses, the wish to develop new jobs, but they have the feeling that they cannot do that here, because there are too many obstacles and it is easier to go to California or Texas and to do that thousands of miles away, and that is really the sort of thing that we have the feeling governments here should address to give more opportunities to these people who want to create new industries and services. Give them more of a chance to develop that on our continent and to create jobs here in order to address the unemployment problem.

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Mr Blokland:

I should like to express my appreciation of the very clear monthly bulletins which I receive at my home address in my own language and in very good time. These are very good documents and they contain a great deal of information and it is always very useful to have read the monthly bulletin before the next one arrives. Now my question relates to the Dutch situation. Mention has been made of unemployment and how we need to have more growth in order to be able to tackle unemployment. Well in the Netherlands we have a difficult labour market where there are a lot of vacancies. I mean sometimes you have 150,000 vacancies at any given time which cannot be filled and that affects SMEs as well. Now we have inflation which is fine at the moment. Public finances are in reasonably good order and the question now is what policy should we adopt in this situation? The Dutch Government recently decided to relieve some of the burdens. Now the economic operators said that this meant that there was a danger of interest rates then going back up and that is perhaps going to create divergent growth levels in Europe. Now before the euro in the Netherlands we would undoubtedly have thought about revaluing the guilder but we no longer have a good method to apply in this situation. I mean the best thing would be if economic growth in the rest of Europe were better and the Dutch would not simply be left as an island but because we are an island the tension is created. So I would like to hear what you think, Mr Noyer. How can we deal with this situation where one country is an island and where a lot of tension is created? How can we resolve this?

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Mr Noyer:

Of course there is no easy answer to your question which is a very important question. I would say mainly two things. The first one is that the Netherlands is clearly one of the countries where the sort of economic reforms that we are recommending strongly have been pursued more than on average in the Union or in the euro area, so it is no surprise to us that the level of unemployment is much lower than the average in the Union and that the growth rate is higher. And I recognize that, to a certain extent, there is a price to pay for that success, that is that at a certain time it may appear difficult to continue without pressures. But the second answer that I would give is that the Netherlands is one of the regions that are advanced in the cycle, performing better, but also have helped the recovery to develop in Europe. It appears that in the months to come the difference between the growth rate in the Netherlands, the rate of job creation and the average of these two in the euro area will be reduced because all the regions will converge with the Dutch development. So we may hope that will calm down the pressure a little on the Dutch economy.

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Mr Radwan:

Well as a new member of this Committee I get the impression that the ECB is going to be responsible for a lot of things in the future but not responsible for its own targets so what I mean is that a lot of national responsibilities are going to be shifted to the ECB. However I would be grateful in the future if you could be more specific. Perhaps if you could give us some kind of a ranking how you feel the various Member States are meeting the targets for employment and other areas? Then secondly Italy was allowed to deal with its budget deficit in a certain way, how do you see that in the ECB?

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Mr Noyer:

We have the feeling that it is our responsibility to give our analysis as frankly as possible to the developments that appear in economic reforms or public finances in the Member States in a rather general way, but we are not really willing to enter into details because we have the feeling that all the policy makers would find that we are really going beyond our responsibility and addressing things that they should address in another way. Fortunately, in the European Union institutional framework there is a body which is fully responsible for that and that is the European Commission and they are making reports on the performance of Member States compared with the broad economic guidelines. They make proposals for economic guidelines and economic reforms and this is absolutely crucial in the European process to have that sort of, not the pleasure of ranking for ranking, but to help all Member States to try to have the best possible performance and globally really attack the unemployment problem. On the deficit problem, we are extremely happy to see that since those projections of much lower receipts than expected, that would have resulted in a more significant deficit, it appears that the growth rate would not be as low as was feared by the Italian authorities and that the result should be that finally the level of deficit should be very close to the original target. Well maybe all these stories could have been avoided but finally the result would be more satisfactory than one might have feared.

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Mrs Randzio-Plath:

That brings us to the part on the international dimension and the euro. Mr Goebbels is first on that.

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Mr Goebbels:

Thank you very much, Chairman. Well since the European Central Bank is still a fairly young institution it probably still has to make its presence felt on the world scene. Nevertheless I do get the feeling that the Bank is perhaps a bit too timid in terms of certain global macro-economic trends. The IMF, for example, has been preaching more growth, has been saying that Asia is now finding its way out of the slump so that we see that some major economic powers in the world such as Japan are now coming out of their crisis. Of course one factor going the other direction could be the excessive value of the Yen. The G7 met at the end of last week talking about what to do with the reserve being made available by the United States. For example I haven't heard anything about the European Central Bank and the role it could play in that context. I do think that it's clear that Japan can exit its present crisis and I wanted to know if the European Central Bank is willing to help it do just that, that is to work with other international financial institutions in order to avoid a future increase in the value of the Yen?

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Mr Noyer:

Yes well I will answer yes on both counts. First of all President Duisenberg was at the G7 meeting so he actually signed the final statement that came out of that meeting saying that there was a concern shared by all the G7 countries including the euro-11 as a group of countries and they also share the concern on the danger of a too rapid increase in the value of the Yen, the impact on the recovery of the Japanese economy which you mentioned, all of those things, we agree on all of those issues. And yes to the second part of the question as well. That is that he also was a signatory to the second part of the statement that came out of the G7 meeting which said specifically that the Central Banks of countries concerned, that's basically three Central Banks, are willing and ready to work at the international level in order to try to avoid any adverse consequences. I don't think that I can say anything more than that right now but the main reason for which I am very, very happy to be grilled by your questions here, I'm not saying I would have preferred Mr Duisenberg to do it, the main reason that it's me and not him is that he's in Washington.

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Mr Katiforis:

Mr Vice-President, you seem to be able to speak and understand French quite well. Despite that allow me to address you in English in the interests of the inter-penetration of cultures. Indeed I would like to follow-up on Robert's question. If you could comment a little bit more on the "communiqué" which seems to be interesting in many respects. First of all the news presented by the general statement, not by the "communiqué" (as was said in the financial press), that the Bank of Japan has responded to domestic and international pressure to ease monetary policy to weaken the Yen enabling Japan to win an unexpected expression of concern from other groups of the seven governments. So my first question is then: how does that square with the doctrine of the independence of Central Banks and their sovereignty over monetary policy? And are we witnessing here the emergence of a power centre in monetary policy which is capable of overruling Central Banks? Now please don't tell me that the consitution of the United States says this, and the Treaty says that, because all that we know but in fact are we witnessing the emergence of a power centre in monetary policy which is capable of pressuring a Central Bank and making it in fact swallow its words and change its monetary policy and would you expect that to happen to other Central Banks in the course of time? And then, regarding the "communiqué" itself, the "communiqué" which says, as you mentioned right now, that the group of seven shares Japan's concern about the potential impact of the Yen's appreciation for the Japanese economy and the world economy and you added, I heard it right now, that the three banks are ready to take action to sort of head off any undesirable developments in the markets. Now on what analysis do they base their presumption to know better than the markets and how does that again square with the theory that Central Banks have so much insisted on that in fact the exchange rates are made in the market and not by Central Bank officials?

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Mr Noyer:

On the first question it is of course the responsibility of independent Central Banks to make their independent judgement and their independent decisions. The fact that the Bank of Japan has made certain judgements on the situation and has explained in a certain way what it might do, I think is related to the fact that foreign exchange developments have an influence on the monetary conditions so that even if it is a little delicate - I can admit that - but it is clear that if there was again a very strong development in the external value of the currency, this would to some extent run counter to the monetary policy that it has followed. So I am convinced that the Bank of Japan has made a judgement that is very well phrased and balanced. The "communiqué" doesn't say what the journalist says in his comment that there is an incomplete consistency with the monetary assessment. On the possible cooperation, as we say on exchange markets, well I think the only answer that I may give is that there is a long standing history of signaling or actions by Central Banks at certain points in time. The main effect is sometimes simply that Ministers of Finance and Central Banks signal that they believe the market is making a mistake on the assessment of the fundamentals and that helps the market to correct itself. There have been a number of cases over the last 12 or 15 years when that has happened and I think the G7 history is full of these events when sometimes the market overreacts at a certain point in time and the simple fact of a strong statement says clearly you are overreacting and that it may reverse. The consequence is that the operators realise that and change their views and the market moves in the other direction by itself. But it is very difficult to comment on this sort of thing in advance. You can only really comment with hindsight.

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Mrs Randzio-Plath:

That brings us to the point called miscellaneous questions and transparency.

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Mrs Peijs:

Mr Noyer, I have two questions for you. I have been rapporteur in the Parliament on cross-border payments. On 14 th August the regulation came into force but we haven't really seen very much change in the market. Computer systems have not yet been adapted so charges are being levelled on both sides automatically because the information is not going through. Now it is the responsibility of the Central Bank to ensure that the payment systems work efficiently, what is the Bank going to do? At the moment there is talk of this citizen's target system. Now I wonder are we actually going to see this coming on line because I think payments is an extremely important issue for SMEs and they are after all one of the main creators of jobs in the European Union so payment and the cost structure is very important. Secondly, we are going to have this currency kit brought out for frontloading. Now what is the difference between frontloading of coins and frontloading of banknotes? Mr Duisenberg told us in the past that there was a legal obstacle to frontloading so I would just like to know, has that been dealt with and if so, why is it only related to coins rather than banknotes?

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Mr Noyer:

On the first question of trans-border payments I have said earlier that we fully share the opinion on which you have reported to the Parliament and that much progress is needed there. We have the feeling that it had to take some time because all the networks were organized on a national basis. So we can understand that it has taken some time. What is absolutely needed is that work is done and progress made so that as soon as possible the difference in costs between payment processes at the national level and from one country to the other are lowered to the lowest possible level and, if possible, disappear over time. We have thought that it was reasonable to set a deadline for that objective at the horizon of 2002. Maybe we are being too prudent but we try also to be realistic, and maximum pressure from the European Parliament will certainly also be helpful. We have in our report tried to explain how the banks could organize to lower these costs and ensure a level playing field. We will have to go into further details. We have said that we intend to monitor the process. Of course, that would be mainly pyschological pressure, but we think that if we point to precise changes and reforms in the structure of processing the payments and the structure of the fees that are charged to the customers, that may help, that will make the task of banks if they want to resist your pressures and our pressures more difficult. We think that keeping continuously the pressure on the banking industry, pointing at the reforms in the technical organization that would be needed, should help to obtain that result. That is the main goal. There is certainly more to be done over the months to come in terms of going into further details and we are fully prepared to come back to your Committee with more details, with the help of the specialists if needed, in order to exploit completely or to discuss completely that very important topic. On the frontloading I fully understand your question about the difference. In theory there is no difference, I could agree with that. No, the main problem we had is that if — and we have thought a lot about it - if we frontload it everything, all coins, all banknotes well in advance of the date, the risk that it is put into circulation in fact before the date would be high. What we have said is that either the European legislation says that it can be put into circulation before that date or if it remains as it is then nothing must be put into circulation before 1 st January 2002. Normally frontloading to the general public is not possible. Of course you can frontload to the banks, to the transporters, to a certain extent the companies, retailers if you are sure that it is not put into circulation prematurely, but not to the general public. But then comes the problem, the real problem, or the two main problems that have been pointed out to us. One is about the groups that have difficulties, how can they get acquainted with the new coins (given that it is more difficult to get acquainted with the coins than the banknotes) and isn't it possible to help them to prepare a little bit in advance so as not to be too surprised on the first days of circulation. And the second is a problem of the retailers. Of course they can have problems, because what will happen is that on the first day or the first days, everyone will go to the bank and will have immediately the banknotes. Now you and me as individuals can go to the bank, get the banknotes, we will go to the retailer and we will give a banknote to pay something that we will buy and we will expect the retailer to give the change in coins, but how can they have the tons of coins they would need, all of them, to give us the change? So it is true that in practice it is a little bit different. So the combination of avoiding prior circulation, that means not frontloading everything to the general public at least, and the fact that in practice there was a specific problem for coins, led us in the discussion with the Ministers of Finance to the conclusion that we could without risk of prior circulation (that would jeopardize the European legislation) accept some frontloading of coins a few days or weeks before the date, and the idea was for around 15 th December 2001. This is a combination which we think is feasible, and the Ministers of Finance felt that it was also appropriate.

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Mrs Peijs:

No legal problem for frontloading. Only not practical. You have to say yes or no. That's the most clear answer.

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Mr Noyer:

There would be a legal problem if we were frontloading everything. There is no legal problem if we frontload only the coins because you cannot put into circulation only coins, it would not work, so that we avoid the legal problem.

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Mrs Randzio-Plath:

I would like to thank Mrs Peijs for that question. We can also take some of those points aboard in the Torres Marques report and to underscore our commitment to that question. A personal example of this: I was called by an attorney today and she said that there would be problems in terms of cross-border cash payments if they actually get money in cash and then take it across the border physically to make payments because there was a case where 800 marks were taken from a Belgian bank and then 500 from a German bank, for example, and of course for the payment we could not accept that as the European Parliament. I think it would be a good idea to try to take those concerns onboard in the Torres Marques report as well.

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Mr Tannock:

Madam President, Mr Vice-President. Actually I wanted to speak in the previous section but I'll ask my question anyway. I've always been slightly surprised that the whole EMU project relies on the EU having an own resource spending limit of only 1.27% of GDP. I'm told by an economist friend that academic studies suggest that central taxation powers to raise at least 7% of GDP are required to achieve stability and even economic growth throughout a single currency zone. The USA for instance has a federal budget of about 20% of GDP which is often cited as a comparator to euroland. Can the euro survive without enormous regional strains and economic disparities without considerable higher central tax raising or spending limits than the current 1.27%, although this politically would pose enormous problems clearly to the Member States governments? Could you comment on that please?

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Mr Noyer:

I think that the answer is that in our European framework the stabilization process is organized in a different way. It is not organized only or mainly through the budget of the European Union but by a set of rules and guidelines given to the conduct of public finance by individual Member States so that in fact you can cope with that problem with a much lower "federal budget". So the fact that we have rules for managing public finance at the level of states that are accepted, recognized, as far as the evolution of the deficit is concerned means that we do not need to have such an important "federal" budget. I would like to add to that that when you have a big federal budget like in the United States part of it is really something that cannot address the cyclical developments because payments of public employees, the core of the public task is really something that has to continue and I don't believe that the difference between the United States and the euro area is so important.

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Mr Marinos:

Thank you very much, chairman. Now Mr Noyer told us that a couple of months ago banknotes and coins started to be produced. Now I hope that I am not mistaken in my information but I think that it has been decided that on the banknotes of the euros there is going to be one standard image and on the other hand there is going to be an individualized image to be decided by the Central Bank of each Member State, so I wanted to ask about the banknotes that have already started to be produced. Are they being produced by the European Central Bank or as a result of the monitoring of the European Central Bank and if so do they have national symbols on the other side? And second, I would like to ask if anyone has thought about the possible impact of transactions between let's say the Bundesbank and another Central Bank, let's say the Central Bank of Portugal which will have issued two different versions of the euro notes. Do you think people for emotional reasons are going to want to try to have "stronger" European banknotes such as German ones rather than so-called weaker ones such as Portuguese issues? And I have a third question and that is whether the European Central Bank has been thinking at all about the millennium bug, the Y2K problem? Do you think, do you agree that there is no problem as many people have been saying or do you agree more with the doom-sayers who think that nuclear bombs might be launched, or that planes might fall out of the sky as a result of computers crashing on the 1st January 2000? And my final question, in my capacity as a Greek member of Parliament, how does the ECB predicts Greece's future role in terms of the European Monetary Union? Do you think that since we are going to be giving our final application in March, will we have fulfilled the criteria, yes or no?

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Mr Noyer:

On that first question, the choice opted for by the ECB (Governing Council) was not to have a national symbol. All the bills will be the same on both sides so we don't have a recognition problem by the public. It is only on the coins that there will be a common side and also a national side, so our citizens will have to get used to having coins with different symbols on one side. Maybe that will be good for the numismatists amongst us and I don't think that for the banknotes there will be the problems that you were referring to. And the other issue you mentioned is the Y2K problem. We think that we have done our very best, the maximum possible, which doesn't stop us having continuous checks on our system, extra tests being done and increasing as much as possible the system security we have.

We are convinced that we do have a framework which would well meet the much higher potential need for liquidity from the banks which will take place just before and just after the turn from one millennium to another. The built-in mechanism designed to deal with any level of liquidity is flexible enough to deal with any level of liquidity demand. It is due to the specific nature of the system. It just happens that we , the Eurosystem, have a big stock of national banknotes The national central banks already have stocks of national banknote on their inventories for the next three years, since they are now producing euro banknotes. Therefore, their stocks are already higher than in normal times and those of other central banks. But it doesn't stop us from taking extra measures referred to. The decision to avoid having a call for tenders during the days immediately after the New Year to avoid all sorts of risks, and the decisions to close the TARGET system on 31 st to have some last tests and to safeguard all our data. On the last point you mentioned, all I can say is that if the Greek government was to decide, as I think they said they intend to do, to officially put forward their candidacy in the spring, we are going to produce our convergence report before next summer. Having all the data available, we will start analysing the candidacy and report to the political authorities, having assessed all the criteria exactly in the same way as the European Monetary Institute did for countries which were candidates in the first wave.

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Mr Schmidt:

I'm sorry that I wasn't here for the whole of the debate but I am rapporteur in the Employment Committee and it seems to me that the meetings overlap. That is not too good for us. I say that because I hope that my question wasn't put and fielded beforehand, but my question goes as follows. I would like to know what are the proposals for increasing our currency reserves in individual countries. I have read in the press and gleaned from that that so far Member States would have to have 50 billion fed in by way of monetary reserve into the coffers of the European Central Bank and I'm afraid it is going to be doubled, instead of being 50 we are now at 100, which Member States are going to have to deposit or lodge with you. So a couple of questions based on that. Should we be looking at such a huge increase in liquidity, is that possible that we have to lodge such great deposits with you? And what would it look like if we shared it out over the various Member States? If they had the same key as we have at the moment it would be easy to calculate but I come from a country where these things have been discussed very animatedly so if I could ask how much Sweden would be feeding in, I will ask you, the Bank, to calculate that out. I mean can you give us some information on that?

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Mr Noyer:

The basis for this lies in the Treaty. The Treaty says that an initial amount of up to 50 billion euros or foreign exchange reserves had to be transferred at the very beginning from the national Central Banks to the European Central Bank and then there is another provision saying that immediately after the start of stage 3 the ECB and/or the Commission must make a proposal for an additional amount or at least the authorisation by the EU Council for an additional amount to be transferred. So the first part has been done of course in direct application of the Treaty, actually the 50 billion were only around 40 billion because of the four countries not participating and it was done following the capital key and this key will be kept for the future. So, it is very easy, I do not have in mind the precise figures but it is very easy to know what would be the amount transferred for this first transfer by the Riksbank. Then we can come to the second move, the second transfer. This has first to be decided by the political authorities of the Union and then further implemented and decided by the Governing Council of the ECB. At that time if Sweden was participating, that would of course also include the Governor of theRiksbank. Now for the second move, the proposal made by the ECB, (and we had discussed this before with the Commission and agreed that only one proposal was necessary, to avoid a duplication of efforts) it was agreed that the ECB would make it. We simply said that for the time being it is really difficult. There are a lot of uncertainties, but it seems to us that doubling the initial amount, I think the capacity to double would be enough, but without prejudging that the political authorities may decide later on another increase. So we have taken that precaution and in fact it very much depends on the sort of intervention to be made. Of course it is not to be costly for the budgets of governments. It's only a transfer of part of the foreign exchange reserves held by the national Central Banks to the European Central Bank. The Treaty also says that interventions are executed by the European Central Bank. So in a way the foreign exchange reserves in the national Central Banks are a sort of reservoir, a back-up line. When there is a need for intervention, the ECB's reserves are used. The idea is that we could over time, if necessary, make additional transfers to the ECB in order to increase the capacity to intervene. It may be enough just to show the strength of the Eurosystem, and it might well be that we do not need to use the facilities every single time. But we must be prepared. That's the idea.

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Mrs Randzio-Plath

Just a small supplementary Mr Noyer. What's the point of having this money for intervention, if there is a currency back-up? Do you have some sort of concept behind the whole exercise, as some people have said it is going to affect of the market, of how you will affect the market? Do you have some sort of strategy if there is too much devaluation or too much revaluation of the euro? As of when will you start intervening? I know you have no remit for the exchange rate, but what about intervention? The various ways that you can intervene, are you just going to start intervening or how will you set about this?

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Mr Noyer:

We do not exclude to take part in interventions for two reasons. One is that foreign exchange developments can have consequences for price developments. And the second is that we may want to avoid developments in the foreign exchange markets at certain times that might have negative effects for monetary policy.

Intervention would be, in our view, mostly a concerted action on the markets. It has happened in some cases over the years that concerted action at a certain point in time between the main monetary authorities of the world has corrected developments in the markets or stabilized the markets, and thus avoided that the central banks would be confronted with the difficult question of deciding whether to move interest rates, in order to avoid the negative effects on price developments, upwards or downwards, of an excessive foreign exchange development. But this does not mean of course that we would wish to intervene every day - that would be quite exceptional. The markets must know that we stand ready to act, if appropriate, in conjunction with our main partners in the world, and they have to know that the threat does exist.

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Ms Villiers:

Would you be unhappy if the euro reached parity with the dollar and at what level does the euro have to fall to to affect prices within the euro zone? At what point will inflationary pressure caused by the fall in the exchange rate value of the euro start to put pressure on inflation within the euro zone?

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Mr Noyer:

I hope you will excuse me, but I do not want to comment on the precise level of the euro, but the most important answer I would like to give to your two-fold question is that we never look at the exchange rate in isolation. Of course the level at which it might appear as a threat to price stability would very much depend on the rest, so it is one of the elements that are part of the total picture. Exchange rate developments have an effect on price developments and they also have an impact on the overall monetary conditions. This is an important element that we have to take into account. But there can be no precise answer because there are always many other factors to take into account at the same time.

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Mr Lipietz:

I would like to ask you about the American policy mix which has been benign neglect for several years on the exchange rate. Inflation rate is very often much higher than 2%, or mostly higher than 2%. The real interest rate, negative for several successive quarters when they need it and, above all, budgetary policy, if you look at the long term now, since say 1985 or so, is either in balance or negative, the contrary of what you have in your written text, written in English, which contradicts what you have just said in your oral text now in French. Biased budget policy or in surplus is what you are looking to, obviously the stability pact looks to a balanced policy.

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Mr Noyer:

On benign neglect, I am amazed at the way in which the United States authorities for several years have regularly repeated one sentence, one comment, on the exchange rate - a strong dollar is in the interest of the United States. That is what they say, full stop, that is it. You have not heard anything else officially on exchange rate trends with respect to the US dollar from the US authorities for several years. The predecessor of the current Secretary of State started it and it is still the case. Now on US economic developments, I am looking at past events and I am amazed to note now, by now I mean over the last few years, the performance of the economy with very high growth rates maintained, without inflation kicking off. As for the precise level it is difficult to compare because price trend indexes are not always on the same basis. You have to go into thorough detail to compare their level and ours but they have a budgetary policy which has already gone beyond balance and is in surplus, with a monetary policy which is very careful. Much tighter now at the moment, but this is normal with an economy which has been strong over the last few years. The US authorities are trying to stop any excessive price increases. They use expressions different from ours. If you look at the budgetary and monetary statements of the respective authorities in the USA it is fairly consistent with what the Central Bank and the US authorities are saying. What we and the Commission are saying should be the same. There is less structural reform required in the USA than in Europe.Basically they have less rigidity in their economy than we have on the old continent. They are starting off from a situation where the creation of enterprises and the development of economic activity are easier to do. They have had fewer reforms to introduce to get to the same result.

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Mr Katiforis:

I would like to know if the tendency of the long term interest rate to rise which has been noticed recently, has been an element in the apparent decision of the European Central Bank to leave the short term rate unchanged and whether the estimates of the rate of growth which you have accepted have taken into account the rise in the long term interest rate which, of course, the Bank does not control, but it has to take it into account I suppose?

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Mr Noyer:

No we think that it is first due to the general development of long term interest rates in the world, because there are arbitrages from investors, including investors from the euro area , of investments in securities in US dollars, in euros, in other currencies, so that when there is a general increase in long term interest rates, mainly in the US dollar, there is a tendency also for other currencies to see an increase in their long term interest rates. Of course you will tell me, but the increase in the long-term rates in Europe has been a little higher than the increase in the US bonds yields, so that the spread has decreased. This is true and we interpret that as being related to the fact that growth in Europe is accelerating but that the growth in the US has stabilized at most, maybe it is in the prospect of slowly declining. But of course we monitor that very closely, because if it was partly, even for a small part, the signal that economic actors fear, that inflation could come back and that price stability would be in danger, then that would be a reason to react. Either we should be able to explain to the public that they are wrong and there is no risk to price stability, or if there is really a risk we should react, even if the risk is 6 months/1 year ahead. We should always react in advance. So this is, of course, something that we monitor very closely, one of the indicators in the second pillar that we regard as very important.

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Ms Randzio-Plath:

Thank you very much indeed.

Preparatory to the above exchange of views the Committee on Economic and Monetary Affairs of the European Parliament commissioned academic studies from the following experts:

- An analysis of the most recent reports of the ECB and an economic forecast based on the latest economic indicators, by Prof. Daniel Gros, Centre for European Policy Studies
- Options for the exchange rate management of the ECB, by Prof. Peter Bofinger, Bayerische Julius-Maximilians-Universität Würzburg and CEPR