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00:03 Benoît Bayenet: Bonjour à tous et merci d'être présent toujours aussi nombreux dans ce cycle de conférences du Conseil Centrale de l'Économie.

Donc ce débat publique que nous voulons ouvrir sur la gouvernance budgétaire mais de manière globale, c'est sur l'évolution des finances publiques dans un climat économique qui est toujours compliqué et de voir comment on peut coordonner l'ensemble des politiques monétaires et budgétaires.

Aujourd'hui, j'ai particulièrement plaisir d'accueillir mon ancien professeur de théorie monétaire à l'ULB, Peter Praet, docteur en économie qui a un parcours extrêmement riche puisqu'il est passé par le FMI, une banque privée avant de passer par un cabinet ministériel et donc aussi d'avoir cette expérience de conseiller, avant de passer à la BNB et de gérer une partie de la crise financière de 2008-2009 et de terminer au directoire de la BCE en tant que "chief economist".

C'est avec ces multiples casquettes que nous l'accueillons pour avoir son avis justement dans notre débat sur la gouvernance budgétaire européenne. Je rappelle à tout le monde que vous pouvez participer au débat en nous envoyant des questions dans le chat.

A la demande de Peter Praet, on va plutôt avoir une conversation donc je vais lancer les premières questions mais vous pouvez évidemment influencer le débat avec des questions dans le chat que nous pourrons demander à notre conférencier.

La première question, Peter, est par rapport à la situation que nous vivons aujourd'hui. Tout le monde s'inquiète évidemment de l'évolution des dépenses publiques parce que certes nous avons connu des chocs en termes de finances publiques mais celui provoqué par la crise Covid est exemplaire à plusieurs égards et donc évidemment inquiète parce qu'on ne sait pas très bien quand elle va s'arrêter et surtout comment après prendre des mesures.

Alors est-ce qu'il faut parler d'austerité, d'assainissement, deretour à l'équilibre?

Toutes ces questions sont évidemment posés.

Ma première question: quel est ton point de vue par rapport à cette évolution des dépenses publiques?

02:52 Kris Degroote: Quelques personnes ont demandé si on pouvait faire en anglaise. If Peter could speak in English, perhaps, it would be better because we also have some English speaking persons, which would be more easy. All the people can put questions in the chat, they cannot speak, the microphones are off.

It's a Webinar, so only Peter and only the persons of the secretariat are able to speak.

03:34 Benoît Bayenet: Donc chacun peut poser les questions dans la langue qu'il veut, a quoi on demande de répondre en anglais pour que tout le monde comprenne

03:43 Peter Praet: Thank you for the invitation and I see some very good friends, in particular Jan Smets, he's the specialist in public finances, so I will speak under his control.

I think, Benoît, what is very important to realize, and everybody knows it but I will say it, if you look at a little bit more than the last decade, public debt increased in many countries by something like 40 percentage points (pp.) of GDP. So that's a huge increase in a decade and it has nothing to do with the aging because we knew that there were some pressures because of social security, health care, related to aging, but this is due to shocks, which were unexpected. So I think it's very important to realize this. It's 40 pp. of GDP in advanced economies and who knows what will happen in the future. So when we talk about debt, public debt in particular, the notion that there may be some shocks in the future that may mobilize huge amounts of resources, I think we have to keep that in mind.

The second point: when you look at the situation, you see some countries with relatively similar situations, performing very differently. If you look for example at France or Germany, in 2007 or 2008, before the financial crisis, the debt-to-GDP ratio in France and Germany were similar at about 60% of GDP. Now Germany is suddenly 30 pp. of GDP-ratio below what we see in France. There are many reasons for that and I don't want to argue this and also many differences in the debt dynamic. I can take another example like Italy, which is now heading towards something like 160-165% of GDP of debt. So that's my first point Benoît.

The second point is that, yes, the GDP-ratios have increased but actually the service of the public debt has in many countries fallen instead of increasing. In spite of the huge increases in debt, debt services have gone down. If you take Belgium for example, the debt-service-ratio is 1,3-1,4 which is historically low. And from there you have a lot of stories, a narrative, that as long as the interest rate is below the potential growth, you know, the sustained interest rate is below potential growth, there is no limit actually to the increase of government deficit. Because the additional debt will be paid at an interest rate which is lower than the rate of growth of the economy so that the denominator, the debt-to-GDP-ratio falls even, depending on how far you go into your primary deficit. So, this notion that, especially for advanced economies, the interest rate is lower than potential growth, leads to another narrative, that you should really use this window of opportunity. I think that yes, there is an argument for that to discuss but on the other hand, and that's a privilege of age, everything can happen. So I will always say that yes, there are good arguments to defend that, but there are also good arguments to say that who know what will happen in the future. That's my first point.

07:51 The second point when we talk about the interest rate below potential growth: it depends on your safe haven status. If you are really considered, by markets in general, as a safe haven, as a country with very good fundamentals or if you're a big power like the United States. But who knows in the US what will happen in the next decade but if you are considered as one of these safe-haven-countries, yes, maybe the argument is stronger but if you are in another situation with a different history, with a different level of debt, you don't know how the spreads could evolve. So yes, the argument that the interest rate could be lower than potential growth, yes, there is some case to defend that. But I say be careful, who knows, but you at the same time you also have to take into account the risk premium which for some countries can jump as we are seeing for Italy, Greece and in other countries and also for Belgium in some episodes and that's something that for the future we have to discuss very carefully.

Now, if you look at interest rates, just to finish that second point on interest rates, it has to do with what is the normal interest rate. The natural rate has fallen for several decades now and you know the arguments, due to demography and some other factors. I say that's fine, that's something that is well documented. It may revert in the future, you know Charles Goodhart and others defend the point that the demography trend and so forth at some point will change…….a low interest rate and low inflation argue to the competition of China etc. I just want to make the point that the long-term real interest rate is a function of the potential growth of the economy. So the lower the potential growth, the lower the real interest rate because the interest rate can basically represent the return on capital plus the risk premium. But if you take the core of the interest rate, it's the potential growth of the economy. And the good news is that the interest rates, the normal rate has fallen but the bad news is that the long term growth has also fallen, to a lesser extent in most cases, that's true, but still there's a relation between. So, suppose with the Covid-crisis that the potential growth is going down further, you could say that's bad news and then you say the interest rate will remain low for a very long time, you could say it's good news. But it's not only good news when the rates are very low because it also reflects the weakness of potential growth. That's my point, I should have summarized it that way.

11:03 The second is what I mentioned before about the safe haven, that when things go bad, some countries like the US, a reserve currency country, and I hope in the future the euro, but it's not yet the case, for Germany it's the case. You know all this money flows to the safe haven countries and that pushes their interest rate down and that facilitates the adjustment to a shock, because their interest rates tend to go down because of all this money coming from everywhere in the World to find a safe environment. That helps, that's one of the reasons why many europeans want to develop the international role of the euro. It involves responsibilities of course to manage your economy when you're an international currency but when you have big negative shocks it can help to have an international currency but you have to manage it and of course politically also.

12:05 The third argument, I think, is monetary policy. A lot of people mention monetary policy as the key explanation of the low rates. As I said about fundamental factors, it's an important factor of course. When the ECB puts the interest rate at -0,5%, it has of course an implication on the whole interest rate curve. What I want to say here is that what is really new in the monetary policy here is that monetary policy has tended to compress risk premium in general and the question for the future, which I will discuss later, is how hard can the central bank compress risk premium, so the spreads actually? That I leave for a little bit later because that's a fundamental discussion.

You remember that the sovereign debt crisis that we had between 2010 and 2012, the premium that some countries were paying were very high. In the Covid-shock that we see now, in the beginning of the shock, the spreads were going up, even if the risk free rate was stable or even at some point going down because of the central bank's action, the spreads were going up... And this is a big difference with what we had in the previous crisis, is that the ECB started to intervene in national debt markets. We will continue to discuss that because this is a key for the future: how long can ECB do that? Because the ECB de facto absorbed via its quantitative easing policy about the equivalent of the Covid-increase of the debt. So the increase of the public debt has been broadly absorbed by the central banks. We will discuss that as a main theme in our discussion: how long can it last etc.

14:27 so I repeat that the interest rates are low for structural reasons, for monetary policy reasons, but also because of the risk premium which has fallen. And the risk premium has fallen, I would say, to a large extent but not only because of the policy of the ECB, intervening in national debt markets, but also, and this is an additional argument, because of the recovery and resilience funds which basically gave the signal that the community, the European Union, not only the euro area but the EU, would be ready to support the countries more than others, the countries that would be hit by this asymmetric shock to the extent that the shock is asymmetric then some european money could be mobilized, new money could be mobilized to support these countries. So, and that gave a very strong signal of cohesion and solidarity within the union and then the spreads started to go down very quickly?

15:39 so you see 2 phases: there was the ECB announcement and then there was the recovery and resolution fund. So the two effects combine and had a very powerful stabilizing effect on the dynamic of public debt by the compression of the spread, countering speculation when the Covid-shock came. That was extremely powerful, the question is of course for the future...

16:03 Kris Degroote: Peter, mag ik misschien even tussenkomen want een aantal mensen geven in de chat aan dat de verbinding toch niet zo goed is, dat de klankwaliteit niet zo goed is. Heb jij earphones of is er nog een mogelijkheid

Peter Praet: Het zal niets veranderen, dat is het probleem. Er zijn misschien te veel mensen online. Quel est la qualité?

Benoît Bayenet: C'est beaucoup mieux

Kris Degroote: Het is veel beter

Peter Praet: So let's continue. How long was the interruption, Kris?

Kris Degroote: Dat was toch een minuut of zes, zeven geleden toen de eerste berichten zijn binnengekomen.

Peter Praet: Ok, c'est comme ça, on n'est pas encore dans le 5G, mais, donc ce que je disais. What I was saying is about the spreads. This is a big difference between what happened in the previous crisis. It's that there are two factors. One is the ECB change in policy, because the ECB with the Covid-shock said "We will ensure that monetary policy is transmitted to all jurisdictions". So accomodative policy is transmitted to all jurisdictions so that had a very powerful signal on the markets, that the ECB would intervene if needed in national markets. This is a sort of revolution, we never did that in my time.

And the second, and that had a powerful effect on the spread and debt dynamic and on confidence actually, but the second, and this is also very important, the second impact on interest rates was the recovery and resilience fund which was basically a political signal of the Union to say that yes we care about asymmetric shocks and we are ready to mobilize European money and redistribute that to the countries that have been hit most by the shock. And more than the money that was used, this is important but more than the money, the money supported the credibility of the signal by saying it's not only words, it's deeds. You put hard money on the table and you distribute that money according to the severeness of the shock. Of course this is related to the pandemic period, so the Covid-shock and we will discuss what could be the future there. But it had a demonstration of a very powerful impact.

Now when you compare with the 2010-2012 shock, there may be big differences. For that shock, first, you know at that time we had huge imbalances across countries. I think it's important not to forget that important point, there were huge imbalances when the shock came. So there was a feeling, certainly among countries like Germany for example, that the adjustment process, when the crisis came, the burden of the adjustment process had to be beared by the deficit countries and this was in line, you know, with the experience. You mentioned I worked for the IMF, but that was a little bit the idea that it's better to be in surplus as a country than in deficit... So the adjustment burden is the responsibility of deficit countries, not the surplus countries and in the 2010-2012 crisis, that principle was applied. So you went into austerity, which in a way the consequence was that the fiscal stance at that time was very restrictive, in these years because you know the deficit countries had to squeeze, they had to have a contractionary policy, which I think was unfortunately needed, but the other side of the coin, that means that surplus countries had also to make some adjustments. That means a sort of supportive public finance to compensate at least to some extent the restrictive character of the construction in deficit countries, that didn't happen. And there was of course no European stability mechanisme to support the business cycle at that time. That was absolutely out of the question. And so we had a very strong period of fiscal contraction in '10, '11, '12 and even '13. And that lead to a recession of course, as you know, there was the sudden recession after the world financial crisis.

That was the first one and that put a very big pressure on the central bank to try to do all the job. The ECB became the only game in town, had to do the job of stabilization in crisis time. The problem you had at this time was that the interest rates were already very low and so the ECB at some point hit the lower bound. So the interest rates went to zero and so what do you do? The ECB says: "I need to stabilize the economy because you are in a recession, the inflation is too low compared to my mandate; I have to stimulate the economy but the interest rates are low". And that's how the ECB came, that was my time, with negative rates, with forward guidance, that means promises on future rates and with quantitative easing, that means buying directly in the market so quantitative easing, asset purchases and we are still in this period now.

The big difference, as I said before, is that at that time, when the ECB was buying mostly government bonds on the market, the ECB basically bought according to the weight of countries, what we call the capital keys. It doesn't matter, but the weight of countries, not the weight of public debt but it was just saying: "I want to buy in proportion to the capital keys", so the importance of the shareholdership in the ESCB in the central bank by countries, more or less. But that would not be according to the market proportion of the debt. So Italian debt as you know is much higher than in Germany but you would buy according to the capital keys, so much less than the market.

23:23 Ok, that's basically related to the treaty where there's a high suspicion. First there is... The treaty forbids, you know, to support countries specific countries' public debt. So that's forbidden in the treaty. There is also in the treaty a big trust, you know, faith in market mechanisms in general, so in market discipline in general and there is not this notion about destabilizing speculation or adverse feedback loops for markets. There is a lost of trust in market mechanisms in general to discipline countries in general in public finances. I cannot elaborate very much on that but basically the ECB cannot really intervene in markets.

So that was the situation then but as I say there was no sort of discussion about what we call today the policy stance. If countries are squeezing very much, and I think this adjustment was needed at that time, but it was not compensated by... in the surplus countries and even lesser by a sort of European mechanism of stabilization policy.

Now when you go in the present situation, when the Covid-shock came, and this is for me a revolution compared to the period when I was there, is that suddenly all the countries realized, and also drawing the lesson from the previous crisis, that if they wouldn't intervene very quickly, you could enter a period of total destabilization of the public debt of some countries like Italy and that would destroy the eurozone. That would be the end of the eurozone and there is a spectacular change in communication and policy. Between, some of you may remember when Christine Lagarde said: "we are not here to close the spread", in the beginning of the Covid-shock when the spreads were increasing already. She said: "that's not our business", which is true. That's the policy, it's the most related to the treaty actually you cannot take that into account. With the time of Mario Draghi we have invented the OMT, which was a special instrument, a condition instrument but with a whole procedure, that a country would ask for that first, the OMT. You would have to go with a program managed basically by the political body with the Commission made as a technical arm and on that condition, the ECB may, may, not even obliged, intervene in the bond market to support the country. If the ECB would have been satisfied about the program, you know, the sustainability of the public debt, which is a long procedure, which is absolutely horrific from a political point of view of course.

So that was the instrument so when Christine Lagarde said: "we are not here to close the spread" actually she was right in the framework. But very quickly everybody realized, I think everybody, including the hardliners in the governing council. There was maybe a little more difficult to accept but at some point, you know, everybody, political bodies, governors realized that if you would not do something then it could be the end again of the euro this time. That was the fatal blow and very quickly then the ECB came with its PEPP - pandemic emergency purchase program.

What helped is first that it was an exogenous shock. You have these huge imbalances that you had, you know, in the 2010-'13 big shock, '10-'12 big shock, you didn't have that so it's exogenous so it's not the responsibility of Italy that you had Covid. Everybody has a bit of responsibility because you are responsible of your health system but still it's basically an exogenous shock. Then everybody agreed this is a different situation. Be careful because for the future, nothing is granted. This is still exceptional, what is being done here. And this is the discussion for the future, when the pandemic crisis is over, are you going back to the old model, in a situation where public debt is much higher than before, or not? So you're still with a problem which is not solved.

28:12 so in the pandemic, I think the reaction was good but it's an exogenous shock and that policy is needed to the pandemic shock. So yes, the ECB started to intervene and then, as I said, the sudden wave of reaction, which was absolutely key, was the recovery and resolution fund which they gave us. Fantastic, I think, political signal of solidarity and also takes into account the asymmetry of the shock so you give more to Italy than you give to Germany for example and you're paying taxpayers later on, we don't know exactly how, will pay much later. And the European Union is using its' borrowing capacity, it's good 'safe assets' sort of name, to borrow cheaply on capital markets and it's extremely successful for the time being. The question and the risk, I should end, in the money which is spend via grants and cheap loans.

There is a mechanism of approval of the project, as I'm not going to describe all that, and there is a mechanism of surveillance where you don't give this money immediately. So, it's given different phases, you know, according to the realization of the different projects which have been introduced to the Commission and I think this is a very good mechanism but it's related to an exogenous crisis and it's normally going to end at some point. So that's for the recovery and resolution fund.

When we go in the future, to leave time for the questions, where does it lead for the future? Let's take the ECB and QE, and the quantitative easing policy. I think on the side of, first explaining what is QE. When interest rates are zero or we experimented with negative rates, how can you have monetary accomodation? So basically what you do, you make promises on future rates because you control the money market rates, the short end of interest rates, and you could say "I will give you interest rates - because that's my power - very low for a long period of time". And then you specify what are the conditions. It's related to inflation, which is the primary mandate of the ECB. And so, you say while inflation rate is going to be low, inflation remains too low, and I'm going to keep the interest rates at the present level, even lower maybe, until I see 2%, my objective realized. It's a bit more complicated but basically, it's what the ECB said. So, it's making promises. Now everybody says well inflation is going to be low in the long term, I'm not talking about the short term, because it's the medium-term objective. So, inflation is going back to 2% on a sustained basis. As long as this is not the case, I will keep my interest rate low and my monetary policy accommodative.

But the situation could change and as I say, I think it's a relatively low risk probability but it's not a zero probability that you get more inflation in the coming 3-4 years. I mean sustained inflation and the interest rate policy would have to change by the ECB. That's absolutely not something that is impossible. So you could say there is 80% probability that interest rates will remain low for a very long period of time but when you manage a situation of public finance and you are highly indebted then you have to take that into consideration and that's one factor of risk. If you have 60% debt-to-gdp ratio it's not the same than if you have 165% of gdp ratio. Some people will say "yes, but, you know, the treasure in Belgium or the treasure in Italy, or France have issued long term debt". But think about the situation...

32:41 the ECB would buy on the market the equivalent, more or less the equivalent of what has been issued and in exchange the ECB issued money, currency that means short term, short term debt. So you can imagine that when a country says: "no worry, if interest rates will increase, I'm protected because I issued my debt with 10 year maturity, so a fixed rate 10 year maturity". But if you take the consolidated position, the state plus the central bank, actually, and some people say that, it's a simple operation of conversion of long-term debt, which is bought by the central bank, which issues short-term debt currency and so the exposure to interest rate, the indirect exposure by the central bank of the state is higher. In some countries like the UK, the exposure is quite high and so, yes, they issue long term debt but to the extent that it's converted by the central bank into short term debt there is a risk because it's not as long as you think. If the central bank has to increase interest rates, its' profit and loss account, the profitability of the central bank is going to go down. That means their profit, which is distributed most often, there is a big difference. But it's distributed to the state and the public finances will be lesser.

So the public finances will have to bear the burden of lesser, what we call seigniorage, from the central bank to the government. If you look at the bundesbank in germany for this year the bundesbank I think used to give last year about five - if I remember - five billion euros to the treasury in Germany as profit from its activities. This year they decided to give nothing to the treasury because they want to provision against what I tell you now, the risk related to the policies of the Bundesbank. I know that market participants are looking at this increasingly to say: "how are the central banks resilient if one day they have to increase rates, what is their profitability and what would be the impact on the budget via the transfer of profits to the government?" I think, I mean, I am not panicking here, I think it's a shock that can be absorbed, it depends on the increase of rates at that time. So I'm not panicking but I think we have to look at the risk considerations. So I would not say dramatize that issue but I think this adds to the risk.

35:27 So, now let's think again about the intervention of the ECB in national debt markets . So the ECB in the Covid-shock we have seen a big increase of spreads in some countries and the ECB has decided that its QE, its quantitative easing policy, would also be geared towards supporting accommodative policies in all jurisdictions. I try to find, we want to ensure - I try to quote exactly - want to ensure that our accommodative monetary policy is transmitted to all jurisdictions. This is new in the in the treaty you know you never thought about this because in the treaty, basically is one size of policy must fit all. So you determine interest rates and if interest rates are too low for Germany they have to deal with that, they have to live with that. If interest rates are too high for another country, well there's nothing you can do. And what you could - not in monetary policy - what you can do is of course use your fiscal capacity, your national fiscal capacity. For example if you think interest rates are too low in Germany, well what can you do to try to compensate that? If you think for example that in Germany the fact that interest rates are too low and your your economy overheats, you know, there is an overheating problem in Germany, well they could use public finances if they want.

The idea of the treaty was that and if you look at another country when interest rates are too high, you have to try to use fiscal policy to support the economy because interest rates are too high for the country so use fiscal. And so the treaty was that you need some public finances because if there are shocks, you know, if you cannot live with the single monetary policy you have to use your fiscal for national purposes as an anti-cyclical, you know, counter-cyclical policy instrument. And as we know the countries didn't use the buffers, didn't create buffers in the good times, and when the crisis came they didn't have the means to do that and then the policies fiscal policies became pro-cyclical I mean as I...

What is the, do we need a stabilization policy at the european union level and the basic... has to look at that by monetary policy. The treaty didn't think about the situation where your interest rates would be zero and there would be increasing constraint on the central bank and so the debate now is open to say: do we need - and I go in the last phase which will lead to a discussion - what we have learned from the 13 last years, these episodes? Do you need to rethink the stabilization policy in the monetary union? Do you need a stabilization policy which is not relying only on the central bank?

For two reasons because first when the central bank is at the zero lower bound, you know, it needs some fiscal support because, you know, it gets increasingly limited in its stabilization purposes. So you need fiscal when the central bank is at the lower bound but even more than that, even if the interest rates will normalize, you could also think that the ECB as a whole would need a stabilization policy for the euro area as a whole. But in addition to that, would that stabilization policy also consider the situation of different countries, which would be a revolution. We are very far from that and the direction in which we are today, let me say for the ECB, is very uncertain.

Markets are, you know, writing a lot about: "when the pandemic instrument is finished is the ECB going to return to the old policy that we are not here to close the spreads". So that's the responsibility of countries, of politicians but not the ECB. And if there is a problem in a country, because of speculation because of that policy or whatever, then the country has to go via the OMT-procedure, which is basically going to europe and asking for a program and on that condition you know the ECB would intervene in the market, so you take the OMT-procedure. So that's one way, you go back to the old, or you try to develop a mechanism under which the ECB could still intervene in markets.

Now the ecb at one point, and this is really very speculative, but the ecb in its strategy review writes that financial stability is…

someone is trying to reach me I will just say no.

…that financial stability is a consideration in monetary policy and that if you read the strategy reach...

41:46 Benoît Bayenet: J'ai perdu Peter moi.

Kris Degroote: ja, Peter, ge zijt even weggevallen, we horen u niet meer.

Benoît Bayenet: Peter, on t'a perdu depuis 2-3 minutes.

Kris Degroote: Neen, we horen u niet meer Peter.

42:36 Peter Praet: the question is will the ECB, if there is a shock in a country, will the ECB in some circumstances continue the policy it's doing today? Do you hear me?

Kris Degroote: ja, nu ben je...

Benoît Bayenet: on t'a perdu depuis quelques minutes, Peter

Peter Praet: oui mais c'est revenu ou pas?

Benoît Bayenet: maintenant oui

Peter Praet: donc la question pour l'avenir... when the pandemic crisis is over, are you going back to what Christine Lagarde said: we are not here to close the spread and you go back to an OMT-mechanism, if the country is in trouble it has to go via the old procedure with conditionality and the OMT of the central bank or is it different this is very very controversial. In the strategy review of the ECB there is nothing on this but there is a controversial...

The new dimension which is financial studies where the ECB says we are going to look at the transmission of monetary policy if there are financial instability issues and under that provision you may at some point decide in the government that there are destabilizing market factors that may justify interventions in specific debt markets. But this is extremely controversial still today. Philip Lane mentioned, but for the Covid-shock only, the ECB would counter non-phenomenal volatility of shock and ensure the proper transmission of monetary policy in all jurisdictions. So that was in the Covid period. In the post Covid period, will the ECB have [a different] policy regarding market instability, which would include specific intervention in the market? this is very controversial today so when we put that in......significant risk factor so you have to build in your debt sustainability analysis......moral hazard is contained because if you say: well we don't care you know about our public finances because......in a sort of policy framework which guarantees that sustainability, and for that you need...

Kris Degroote: Peter misschien is proberen om de camera uit te schakelen? Het is toch moeilijk begrijpbaar

Peter Praet: I'm not sure it goes better but maybe it goes better

Benoît je te vois donc toi tu me fais signe si ça marche

Benoît Bayenet: ok, maintenant ça fonctionne bien. Peut-être reprend les dernières minutes, Peter, parce qu'il y a beaucoup de gens qui n'ont pas entendu et c'était coupé, la dernière démonstration, après Covid et la politique monétaire

46:27 Peter Praet: During the Covid period, but I say it is during the Covid period, the central bank, I quote philippe lane, said we will counter non-fundamental volatility of spreads. He, as other members of the governing council said: "we will ensure that the accommodative monetary policy is transmitted to all jurisdictions". So, will that continue or will there be something in the post Covid period... or do we go back to the old framework: we are not here to close the spread and if you know there is a problem in a country it has to go via a program and the ECB under the OMT will intervene. So that's if you go back to that situation that's one scenario you go back and you can have a transition of course but you go back to that. I think it's a possibility and I think that's part of the risk factor of the countries which are more indebted so you cannot just count that the policy of the ECB will continue.

Second, it is also possible that the ECB has more attention to market destabilizing factors. If you look at the strategy review of the ECB, it is written that for financial stability reasons the ECB will look at this transmission mechanism. So that's in the future and in the transmission mechanism it may be fragmented, it may be disrupted by speculation you know by excessive market movements and so the ECB opens the door, I think, to interventions to guarantee proper transmission of monetary policy. But you still have to define, that's very controversial, what would be the conditions under which the central bank in the future, when the Covid crisis is over, will or would or could intervene in national debt markets. It is clear that it would only do that if there is a convincing market destabilization process. Second, the ECB would certainly look at the fundamentals, that means also debt sustainability, and there would necessarily have to be a link at some point which is very difficult to design with the political body. But the ECB as an independent authority would always in the end decide what to do. But before you decide you want to ensure that if you intervene because you think there are speculative destabilizing movements in a specific debt market, if you decide to intervene -which as i said it's very controversial also legally - you want to ensure and be sure that debt sustainability would be guaranteed, which may need a program in a country and for that there's a link of course with the political body that means the eurogroup and the commission, that remains to be done.

49:57 Now when you talk about public finances in a country like Belgium in the coming years these are risk factors that you have to take into account. What the ECB does today does not necessarily mean that it does it later on because that framework is not specified. I think that's a key issue when you manage your public finances in terms of risk. Also, even if you borrow long term don't forget part of the long term is transformed into short term via the central bank, that was an argument I had before. So you are a little bit more exposed to interest rates via the P&L of the central bank.

The second I see is that the policy of intervening in national debt markets, so backstop, is specific to the pandemic crisis the framework post pandemic is not yet there and it's controversial. I think there is an opening by the central bank when the central bank says we are also looking in terms of financial stability for the proper transmission of monetary policy. The transmission can be destabilized by speculation but speculation may also be related to a debt dynamic which is unsustainable so you see and that's extremely controversial and that still has to be put in place.

So, when you put your public finances today, the trajectory of your public finances today, you have to take into account these factors. You cannot just say: well the ecb will intervene. The ECB, first, may say no and in any case they will keep ambiguity on interventions and the framework that we have today, post-Covid, is still the OMT-framework with conditionality and where many countries do not want to go through with that.

The last point is that, and that's beyond the national debt market, do we also need, especially when the central bank is at the lower bound - zero rate, do we also need a fiscal stabilization policy at the euro area level? So where there is a borrowing capacity, what we call a fiscal capacity, from the European Union to borrow money in bad times and has supported aggregate demand in bad times in recessions at the euro area level where you could also support some countries more than others and in good times it goes the other way. We are very far away from that. I think it's needed. I think a monetary union would need a federal budget much bigger than what we have today even if you include the recovery and resolution fund but i think the recovery and resolution fund is an excellent example, it's really a big change but it's Covid related. But if the money is spent wisely, correctly, I think it opens the door to a much better monetary union, institutionally I mean, than what we had before. If the money is not well used, it would be a catastrophe, it would go the other way. And so the commission has a big responsibility because the surveillance of how the money is being used is in the hands primarily of the commission and I think the countries are serious in this, so for the time being it looks good. But it's a long period of experimentation and we have some years here to see how it goes, how it's implemented in the recovery phase so I'm quite optimistic.

54:00 but in terms of risk management, when you take it at the country level, I think that we should not be naive to say: well public debt is high but interest rates are low because of aging, demography etc. and will remain low. The spreads and the risk premia on national debt are really made low because the ECB will intervene and because maybe europe will be mobilized if there is destabilizing speculation at some point in time in the future. So in terms of risk management, my only message, which is very simple, is to be cautious. I think the debt levels that we have in a number of countries like Belgium are quite high. I think they are sustainable of course but it's not without risk and i think the risk component is key so it's a risk management issue.

It's clear also that the quality of public finances will be of key importance: how you spend the money. And at the end of the day what you need to make debt sustainable is that you have sufficiently growth in the economy, so that means that the money has to be used in general to support the potential growth of the economy so that you get tax revenues that allows you to support your public debt in the future. And so when I see the debt dynamic in a country like Belgium, but I basically looked at the 'Bureau du Plan', when I look at this I say yes that is not fully stabilized by 2026, it continues to increase while the interest payments stay broadly stable at 1,4%. I think this is a debt dynamic which is a little bit worrisome. I would not say it's dramatically bad but I think it's worrisome, it doesn't give you sufficient safety. But you have to manage, for the policy makers, which is very difficult to do, you have to be very selective of course in your project. You have to be sure that your potential growth is supported and maybe you pray, you pray so that it works but it's a fragile situation frankly. And when I see that it even decreased a little bit over time, so it's not stabilized, I don't think that it's good.

I would not argue that you need austerity, you know, a very strong fiscal contraction, I would absolutely not argue that but I think it will be extremely delicate because there are many new demands in healthcare, in security, the climate change, and also the fight against poverty etc. and so the the fiscal position will be extremely delicate to manage politically in the future so it's not a comfortable situation.

The public in general, and I really conclude with that, the public in general has, I would say, a bit of fiscal illusion. Our rates are low, you can borrow cheaply - at zero rate, money anyway will be well used, whatever you do it's good because it supports solidarity or whatever, digitalization, climate, etc. And I think in a way it's good that people are not too worried today because we are still in the Covid crisis, we are not yet out, but on the other hand what I fear is when the hard realities will come back in '23 maybe or later, in '22, in the discussion on the budget suddenly people start to realize that actually the honeymoon period that we had where nobody cares about fiscal comes back with revenge at some point. That i wouldn't like so let's be reasonable and I think: manage the public's finance at best.

When you look at climate it will cost in public investment 0,5-1% per year in this decade additional per year which is huge if we are serious about climate and you cannot finance that in addition to what we did here. And so I think the situation remains fragile but i think it's sustainable with some wisdom.

58:39 Benoît Bayenet: thank you very much Peter. I try to summarize a lot of questions, there are a lot of questions about the level of sustainability of Belgian debt and there is a study of the Belgian central bank about a level of 120% of gdp. What do you think about that? Is there a risk of sustainability for Belgium with the debt?

Peter Praet: I think, to take a worse example, the italian debt is sustainable +/- 160% of gdp is sustainable. But it's sustainable under some conditions: that you don't have a big recession, that interest rates will remain relatively low and there are a lot of that sustainability analysis about countries. And yes, it's true that even a country like Italy with 160% of gdp the debt is sustainable but there are risks. So you're going into what we call the orange or red zone... When i was in the ecb - the staff of course - I did many simulations about debt sustainability of different countries and Belgium is certainly sustainable, but it's not in all scenarios and in some credible scenarios, not impossible scenarios, you get into very big difficulties. So for example in a country like Italy, what we calculated is when you are in a recession and when interest rates go up then it's the end of it, it's finished, you're finished. That can happen and that was happening with the Covid because we had a huge recession the spreads were going up because once markets said the risk is increasing and people are selling the debt, interest rates go up and you are in the recession and that's why, because we were very close to a catastrophe, a real catastrophe, the ECB and all the political bodies including in Germany decided to go the way we have seen which was very very good. I think that was wise and thanks to the experience of 2010-12 but we should not be naive and think that what happened in the Covid will happen in any circumstance. If you have for example a severe political crisis in one country, I'm not talking Belgium here, take a country with high public debt and that political crisis has to do with public finances that's different, you know there is no agreement to limit the deficit at some point and markets can be very very aggressive at some point and...

So for exogenous shocks you can be assured if there is a cyber attack that puts a big shock on banks and then on the economy in the coming years, I think the mechanism we discussed today can be put in place again. If there is a, think about a climate, a big shock at one point in time, there is a big climate catastrophe but if one country doesn't manage well it's public finances because lack of political consensus and you start from a high level of debt, then it's not guaranteed. So you have to preempt all these things before, I think 120% is sustainable but not sustainable in all conditions but in most conditions 120% is sustainable. My point is the quality of public finance: what do you do with the money and you have to be sure that the money leads to growth at some point in the economy because you need revenues at some point to support all the spending we need to do in the future including the aging the pensions and all that. So the quality is the key and if you have 120% gdp debt ratio with very high quality, for example you invest in education and you say 'okay for that I need more debt', I would say fine. The idea is a good one but I want to see results because as we know it's not because you spend more in one item, be it education or climate or whatever, that it leads to a higher quality of education or more skilled people coming on the labor market later on. So you have to be very granular. It's not enough to say 'I will increase spending in health care', you also want to look at the the efficiency of the spending. So there must be a control on that, it's not just to to fill some boxes by saying education. Absolutely education is good but it's about the quality and the outcome that you have in the end. Unfortunately it's very materialist but it has to lead to to a skilled labor force at the end of the day and that applies to all the items and I realize politically it's quite difficult but that's what makes that sustainable. It's the ability of a country to agree on public taxes and revenues and the deficit so that when you say 'I have a deficit', that money is well used and will lead to higher growth later on, that will enable me to service the debt. I think the countries that bet that rates will remain low for a long time and gamble that if something happens, europe will be there or the central bank will do what is needed is naive and dangerous.

1:04:56 Benoît Bayenet: thank you there are also a lot of questions about investment. The question: investment in public expenditure is very important, what do you think about the possibility to exclude from european rules, fiscal rules, the amount of investment? is it possible to define very clearly an investment concept?

Peter Praet: yes, I mentioned education but you are quite right you can include climate related investment for example or digitalization. There is a Bruegel paper that is being presented at I think the euro group today actually in Ljubljana and I advise those who haven't seen it to read it. They propose here to have some off budget, it would not be under the stability and growth pack rules. Say it was for the climate crisis and you want to prevent a bigger shock later on so the efforts are so huge that you need to spend more and that would be in a special budget.

I understand the argument and I must also say that, as you know, there are elections in Germany coming soon, in about a bit more than a week, and some parties also think about off-budget spending. For me it doesn't make a big a big difference to be off-budget because it will be the public debt anyway. The difference perhaps is that it's something you can monitor specifically. But when you talk about climate and investment in climate it's so huge in terms of the range of measures that you could take that I unfortunately remain a little bit skeptical and I personally am quite worried about this issue about climate because it's a necessity and we are very late. And you need to mobilize a huge amount of money but also big changes in taxes and regulation. So it's not only a question of money but also if you want to make changes in behavior. You need to change taxes of course and regulation and also mobilize money, private and public money which I think is a huge task, very difficult to do and we don't know the impact of climate policy on the potential growth in the coming years.

Personally, I see it like Jean Pisani-Ferry, I also advise you to read a very good piece on that I broadly agree with all what he writes. I think there is probably a negative supply shock because if you have a machine, you think it will be there for the next 10 years and then suddenly you say it's obsolete, I have to change it with new capital. It's what we call a negative supply shock so it pushes the firm to a stress because the amortization is faster than what you thought so governments may give subsidies or not. It will affect your P&L of course and does it lead to higher productivity in the country in the next three four years? It may be good for climate but it not necessarily leads to higher gdp growth that will give you tax revenues to finance all this.

So yes, I know digitalization may go the other way but there are so many uncertainties that again I go back to my principle of prudence, that you have to be very selective in what you do with your money. Yes probably you will have to do something in climate which is very well identified but as benoit was rightly saying: what is an investment today? And there are so many choices. That's not my expertise but when I see huge money to subsidize electric cars, frankly I don't know, that's a huge subsidy, that's a big change, I don't know if it's a good investment for the future. I have no idea, that money could perhaps be much better used in other things but I don't know frankly and there may be plenty of these sort of questions in the coming years. What is for sure is that the regulatory tax uncertainties and even fiscal budgetary uncertainties are likely to increase because of this new change in policy which is in the making and needed. And I come back to my easy point which is to be careful.

1:10:04 Benoît Bayenet: and what do you think: is it possible to imagine that in europe it's possible to finance climate investment in the same way as the recovery plan, with euro bonds and so on?

Peter Praet: yes, well it's already the case today that the RRF is not a crisis instrument. It is a little bit because we are still in crisis, but the main idea there is for the future. It's a recovery plan so, yes, it's already being done. Can we do more? I don't know if we can do more. So that's the question... I'm sorry i have eight minutes, Benoît

Benoît Bayenet: Kris, do you see other questions?

Kris: oui, une question un peu radicale, on peut dire : un certain moment, ne faudrait-il pas songer à annuler une partie des dettes détenu par la BCE? Si cet argent est consacré par exemple à la transition énergétique, pour un moment limité ou une période limitée?

Peter Praet: the arguments have been explained before. It's because we don't have much time and this has been debated very much in France and there have been so many papers explaining why this is an illusion again, unfortunately, if that would be possible. I think one way of seeing that is that the ECB in its portfolio of government debt that it has bought could reinvest this portfolio for a very very long period of time, so you just keep it on the balance sheet of the ECB. The ECB could do that. The problem is: if the ECB has to increase the rates at some point, the impact on the economy will be there because, as i said before, the long-term debt is actually converted in money in short-term debt. So if you say the long-term debt that you bought is even longer, longer, longer, the other part of the balance sheet of the central bank is short-term debt. So the day you have to increase the rates will have full impact even if you reinvest for a long time. I don't say that in market dynamics it cannot make a difference of course, but structurally it doesn't change anything. In other words, the public debt is in the balance sheet of the central bank on both sides: it's on the asset side in long-term debt and you can lengthen that but it's on the liability side with the money that you issued in the market and the day you have to increase the rates, you will have to increase the rates on short-term money if i can say. So the volume will still be there and if you have to withdraw the volume because you want to tighten the policy, you will have to do that. So it would not make a difference in my view. It can make some difference via announcement effects. For example if the ECB would say I'll stop my reinvestment tomorrow, yes, it will have an impact on the markets, of course, on market dynamic but structurally it would notmake a difference in terms of debt sustainability.

1:14:16 Benoît Bayenet: il y a une question très précise qui demande 'pourquoi est-ce que les banques centrales sont obligés de rémunérer les réserves des banques commerciales?'

Peter Praet: That's the other way, you can tax the liquidity of banks and ruin the banks so there is perhaps something you can do but it will have an impact on the banking sector if you do that. They're not very profitable nowadays so I'm not so sure. I like these questions because I would love to say you're right and there is an easy way. But I think be careful, frankly, don't go into illusions and, as I say, if you use the money wisely, and that's a big question of course, if you use the money wisely, the 120% of gdp is okay, it's not a problem, but when i say wisely, unfortunately, it's not an ethical concept. Unfortunately, it is an economic financial concept also, well, you need to do both of course, but it means that you need at some point to have a positive impact on gdp which would give you some revenues for the future.

And so with the climate, a number of spending will probably not increase the potential growth rate. It will mean a better environment and in the longer term it it's good for gdp even because people are healthier but for a number of years it will not be revenue enhancing, it will not give you revenues. So I think the situation remains extremely delicate so you have to be very parsimonious and I can understand that you take some room of maneuver because you have to front load some of the investment, I agree on that. That's why I say one has to be careful also not to fall in the austerity debate and you have to think carefully but you see if you want to make more investment you cannot just say you can do everything: more investment, better pensions, better health care. Hard choices will have to be made but I don't exclude of course cuts in some of the spending and an increase of taxes. That's possible and as you know, with climate you can increase CO2-taxes and redistribute that. That of course will be done. It's very difficult politically.

I really have to stop, friends, dear participants, sorry

1:16:58 Benoît Bayenet: merci peter, en tout cas, merci beaucoup pour ce débat, je sais que tu as une contrainte à 11.30h. En tout cas, nous allons le diffuser sur le site, pour aider ce débat sur les finances publiques. Je rapelle en même temps à tout le monde qu'à partir de maintenant, le site est ouvert, donc les gens peuvent faire des propositions et alimenter le débat. Je sais que Peter, de toute façon, si nous avons besoin de le réentendre, il nous dira oui et que ce sera un plaisir en tout cas de le rencontrer à nouveau. Je souhaite à tout le monde une excellente journée. Je remercie encore évidemment Peter pour cette intervention.

Peter Praet: et désolé pour les, the noise, quelques interruptions, so sorry for that.