



THE BANKER'S COMMENT BY JEAN-PIERRE PATAT

A former central banker looks at the news

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Figure of the month: 100 billion euros; the total for EFSF aid to Spanish banks, with 20 billion as the part guaranteed by France: no impact on public finances. unless...

Faced with the structural divergences in the euro zone: enforced solidarity or tighter integration within a "hard core"?

From the beginning, the euro zone has included far more countries than was the initial intent of those who conceived it. Whereas a smaller zone might have been able to tend towards more optimality, several countries have shown increasing structural divergences from the others. There is a large range of « structural » indicators: education; expenditure on R&D; creation and implementation of patents; labour markets; employment figures; size and efficiency of administration; businesses' microeconomic, legal and fiscal environment; tax evasion and so on.

Clearly, four countries, Portugal, Italy, Spain and Greece, have registered more mediocre performances in these areas than have the other countries. This divergence between the two blocks is at the very heart of the crisis in the zone whose survival depends on a lessening of this divergence.

For this, two approaches are evident - the French one and the German one. The French are asking for the setting up of powerful solidarity mechanisms able to make a lasting impression on investors. The Germans think that such instruments serve to deny structural divergence problems and would in any case do nothing to cure them. They propose deepening federalism, believing that we can do without those who will not undertake such a step, a proposal that does not aim to simply « drop » the divergent countries. Quite the opposite, since these latter countries will be the most eager to become part of the "hard core", but in making this choice they will bind themselves totally to implement these structural reforms, so indispensable for ending the potentially mortal differences within the zone.

The German proposal may be tactical; nevertheless for her it has the coherence and the vision of a future that we cannot keep at a distance for much longer. Even if the implementation of this move towards increased federalism were not to be immediate, a clear and firm declaration of that kind by euro zone countries would, contrary to what the French believe in their desire for immediate measures, convince investors and markets.

Word of the month: eurobonds.

Eurobonds! We might well wonder what bites the French to make them hang on to this idea. There is of course this recurrent tendency to think that those responsible for the crisis are not those who manage their affairs badly but those who manage them too well. This persistence, in any case, shows a certain incoherence and it is built on an illusion. The incoherence of asking for the mutualisation of the debts when one refuses to ratify the European budget treaty and dismisses the « golden rule ». The illusion that the markets would rush to scoop up these eurobonds and that their issue rates would be low. But investors would know full well that in this mix there will be some good elements plus many that are a lot less so, some expensive elements and some cheaper ones. What is more, you can bet these new instruments would not benefit from a top rating.

The euro zone at the centre of the world.

They were saying the euro zone was out, left to one side and marginalised. Wrong! Our situation seems to be at the heart of the world's economic environment. The Japanese, Chinese, Indians and Brazilians are lamenting our fate and its supposed consequences on their growth, and they urge us to act. The English accuse us of nothing less than compromising the results, which had been promising, of their exemplary economic policy. Most touching are the Americans, who have giant memory lapses concerning sub-primes, Lehman Brothers and Fanny Mae, and who are having trouble implementing a sizeable banking reform that is inversely proportionate to the number of pages of the legislative document. From a "moral standpoint" they are fearful of the situation of our banks and, more discretely (and no doubt this is at the bottom of the whole thing) they fear the euro's weakening.

Euro zone: credit is not too dear; it has broken down.

The ECB has left its base rate unchanged at 1%. Commenting on this decision, one journalist, talented though he is, deplored that fact that the institution is always late to react. Stereotypes are hard to kill! All indicators show that European economies are not suffering from rates that are too high, but rather from the banks' reluctance to lend to businesses and households. To lower rates again would change nothing, except for making banks even more reluctant to lend at derisory rates on the interbank markets.

They give the example of the Fed. Let's talk about that. The US Central Bank has nothing left up its sleeve except for a third "quantitative easing" that the markets pretend to await, but without real conviction. The efficiency of the preceding experiments in fact served to feed market speculation. One more thing; in the US, with a Fed Fund rate nudging zero, the prime rate (that given to the best businesses) stands at 3.25%. In France, with an ECB rate of 1%, good businesses can borrow in the short term at less than 3%. So?

French savings? Clearly insufficient.

The importance of French household savings is recognised. Their level of saving, at 16.2% of available income, is barely below that of German households. Some though do not hesitate to stigmatise what they call "rentier behaviour", invoking Keynes in hoping for the « euthanasia » of these savers, forgetting that the persistent French current account deficits shows an insufficient global level of savings in the country.

Some would hope to see households participating more in financing the public debt, thus reducing dependence on non-residents. But once again, let us get back to Keynes; since overall savings in France are insufficient, the question is if it would be better that "national savings" served to finance public debt rather than businesses?

Financing by non-residents incites budgetary discipline while it is not desirable to over extend the share of non-residents in financing businesses.

The biggest problem is therefore to know how we can ensure that our savings finance more the productive sector, sole creator of wealth. Even if only a modest step, it would be a move in the right direction for the French authorities to double the ceiling for sums invested in tax-free industry savings books...