



Interview of François Villeroy de Galhau, Governor of the Banque de France,

with The Wall Street Journal

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French Central Banker Vaunts ECB Pragmatism

“We must be predictable for markets, but not pre-committed by market expectations,” says François Villeroy de Galhau

Bank of France Gov. François Villeroy de Galhau, shown on Dec. 5, said “European monetary policy is a yardstick of predictability and stability and this is very important also for supporting economic activity.” Photo: Bloomberg News

Last week the European Central Bank extended its asset-purchase program to the end of 2017, but at a lower rate of €60 billion a month from April onward instead of €80 billion. Bank of France Governor François Villeroy de Galhau sat down with The Wall Street Journal to discuss the thinking behind the move.

On being pragmatic

François Villeroy de Galhau: When I stress pragmatism, we shouldn’t be pre-designed as dovish or hawkish. Our duty is to decide independently and according to economic analysis. We must be predictable for markets, but not pre-committed by market expectations. If you look at last week, many people described the ECB as being stuck between more of the same on one side and tapering on the other side. Our decision was neither of them.

Could QE be reduced further?

It’s not black and white, we never said it’s zero or 80 billion. Clearly we will do at least 60 billion.

Negative rates

What I have been saying constantly about negative interest rates; they are useful but they are only one tool among others in our tool kit and they obviously have limits.

Recovery and inflation

We are confident about the eurozone recovery; moderate but firming. We are confident in our progress towards the inflation target. The deflation danger has vanished and if you look at the inflation figure we are at 0.6% in November, probably more than 1% at the beginning of next year and our forecast is 1.5% for 2018 and 1.7% for 2019. So, diminishing the levels of monthly purchases is showing signs of progress towards our inflation target. Maintaining our presence in the market corresponds to the fact that we still need to be active towards our inflation target.

Political uncertainty

Clearly in a very uncertain world, European monetary policy is a yardstick of predictability and stability and this is very important also for supporting economic activity. For next year we have an electoral cycle throughout Europe, so we say clearly: in this uncertain environment economic actors know where monetary policy will be, which is a very strong advantage for them and the economic recovery in Europe.

Credibility

We are making progress towards the 2% target. And we repeated in last week's announcement that we would continue our purchases until the end of next year or beyond, if necessary, and in any case until we see a sustained adjustment in the path of inflation consistent with our inflation aim. We decided to maintain an active presence on the market, but we design the volume of this presence according to this economic situation and the point we are towards the inflation target. So 60 billion in our view is the adapted volume.

Basel Committee

I am more confident than some weeks ago. We have made good progress in Santiago [Chile] in the last meeting of the Basel Committee towards a global agreement. If we can reach it in the coming weeks it will be good news for everybody; for banks themselves because it means stabilizing the rules of the game eight years after Lehman, and this is needed. A balanced agreement would have a positive economic effect.

French Central Bank governor warns on increasing deficit

Bank of France Governor François Villeroy de Galhau has a warning for the contenders in France's presidential election who are promising fiscal stimulus to jump-start the economy: pursue deeper economic reforms and stop relying on debt to pay the bills.

"Reforms are the priority to accelerate our growth and employment, more than fiscal expansion. If I had one message, it is this one," Mr. Villeroy de Galhau said in an interview with The Wall Street Journal.

His call for fiscal discipline comes as candidates across the political spectrum—from leftists to Marine Le Pen, leader of the far-right National Front—say they would seek to free France from the strictures of European Union budget rules.

François Fillon, the center-right *Républicains* candidate who polls show will probably win the May election, has pledged tough overhauls of pensions and labor laws that European officials have repeatedly prodded France to undertake. But part of his program is also based on offering deep tax cuts and foresees a deficit climbing to 4.7% of economic output next year, well beyond the 3% European limit that France is committed to meet.

Mr. Villeroy de Galhau said that kind of trade-off between reforms and deficit spending would harm France's credibility and overburden future generations with debt, which is already nearing 100% of economic output.

"The respect of the 3% target is important for our credibility in Europe," Mr. Villeroy de Galhau said. "You can implement reforms without increasing deficits and you have many examples of that across Europe."

Mr. Villeroy de Galhau's concerns about France are part of a wider problem faced by policy makers at the European Central Bank. The ECB has ramped up stimulus in the last two years with a massive asset purchase program and record low lending rates, but governments haven't kept their part of the implicit deal to repair the eurozone economy.

As the cheap money flows through the eurozone economy, Mr. Villeroy de Galhau said the bloc still lacks a "collective economic strategy," as some countries keep budgets in check and overhaul rigid laws that hurt growth and others, including Germany and the Netherlands, pursue fiscal expansion.

"Monetary policy shouldn't be the only game in town. Everybody agrees in the principle but we should now implement this principle," Mr. Villeroy de Galhau said.

There is growing evidence that France is lagging behind the eurozone recovery. Last week, the ECB kept its 2017 eurozone growth forecast at 1.7%, but the Bank of France cut its forecast for France to 1.3% from 1.5%.

"French growth is slightly under the eurozone average and this is a call for reforms," Mr. Villeroy de Galhau said.

Despite Mr. Villeroy de Galhau's tough rhetoric, he indicated the ECB is fully committed to maintaining its stimulus measures in a coming year with large political risks, including German elections as well as the French presidential and legislative votes. At last week's meeting, the ECB said it intends to reduce monthly asset purchases in its quantitative easing program to €60 billion from €80 billion, but extend the program from March to the end of 2017.

"For next year we have an electoral cycle throughout Europe, so we say clearly: in this uncertain environment economic actors know where monetary policy will be," Mr. Villeroy de Galhau said.

The ECB said it could even increase the size and duration of the program if the outlook becomes less favorable. For Mr. Villeroy de Galhau, the guidance means that the ECB has flexibility, and he suggested €60 billion is the lower end of a possible range.

"It's not black and white, we never said it's zero or 80 billion. Clearly we will do at least 60 billion," Mr. Villeroy de Galhau said.