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# THE BANKER'S COMMENT BY JEAN-PIERRE PATAT

A former central banker looks at the news

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**Figure of the month:** 124 billion dollars. The Chinese trade surplus over the last twelve months - in a dizzy free fall since 2008 when it stood at 297 billion dollars.

## A new European agreement. Is it the right one?

Let's start by listing what, in our mind, is positive. Real budgetary coordination should finally come about; a coordination which, let it be said in passing, would already have been in place had we respected not just the letter but also the spirit of the Growth and Stability Pact. The European solidarity mechanism, viewed by many as dead and buried, will now endure. Its management being consigned to the ECB guarantees its seriousness. Boldly treading into the politically incorrect, we will also find the clarification of the "British case" positive and, if we may go even further, this clearing up ought to have concerned all the EU non-euro zone member States whose presence will not, it is already apparent, facilitate negotiating final texts.

On the down side, this agreement is singularly lacking in inspiration for the future. Was this not the chance, in parallel with a restrictive element, to reformulate the Lisbon commitments, to turn the continent into the most competitive zone in the world and devote 3% of GDP to research and development? The less than warm reception by markets might well signal their concern faced with this lack of vision. Some say the goal is wrong: budget deficits are being attacked, whereas the crisis is one of balance of payments. It cannot be denied that supervising the balance of current payments (missing from the Stability Pact) is necessary; that said though, in reality it is public debts and the burden they bring to bear upon States that concentrate problems of sustainability (Spain is paying lower interest rates than is Italy).

Several French analysts and politicians bemoan the silence in respect of the ECB's interventions and the refusal of eurobonds: two moves, it must be said, that were meant to multiply the crutches for ill-managed States. Talking of the ECB, we repeat that the measures it takes stem neither from the Germans, nor from some community decision, but from its Board. It is likely that the Frankfurt institution will continue, perhaps even increase, its public debt purchases on the secondary market. However, these operations will nowhere near achieve the size of those practised by the Fed. Not least because unlike the Fed (which buys back fungible bonds only from the American Treasury with which it is in permanent dialogue), the ECB is a multinational institution, and the euro zone's public debts are not fungible. This is a fine distinction not perceived by those who incessantly evoke the "American example".

## French external trade. Price competitiveness improves slowly, but the return to equilibrium is not for tomorrow.

With France's external trade deficit of 71.6 billion euros over the last twelve months, i.e. 20 billion more than the preceding period (a little over 10 billion of which were down to energy price hikes) it is hard to be optimistic. Even so, it seems that our competitiveness is improving lately. Calculated on the basis of unit labor costs, there seems to have been a 3 point improvement since 2008, after an 8 point drop between 2003 and 2007 (source Banque de France and INSEE). In parallel, the share of our deficit vis-à-vis the euro zone in our global deficit dropped from 47% to 43%, and the deficit vis-à-vis Germany from 23% to 18%. Vis-à-vis the totality of our trading partners, following a considerable fall between 2002 and 2008 (14 points), we have moved up 5 points and find ourselves at roughly the same level as when the euro was created at the start of 1999. This is not as good as Germany with its 6 points gain in 12 years, but better than Italy with its loss of 5 points. A return to balance is not at hand, even so. A recent study confirmed that "made in France" items (the "big contracts") mainly exported beyond Europe are selling less well. We may at least hope for the reduction, even the disappearance, of a deficit that should not exist vis-à-vis our euro zone partners.

## Debt sustainability. Are we looking at the right numbers?

A recent study by the Lisbon Council places France in a poor position among euro zone countries for debt sustainability. This is questionable. Total public debt at 90% of GDP is a lot, but may we dare venture that in talking of sustainability this is less important than the annual cost of servicing the debt, which has not varied for several years at 5% of GDP (the debt increased but rates went down and the average duration was lengthened). What's to say that this 5% has become "unsustainable"?

## G20. Some progress despite all.

Eclipsed by the European debt crisis, the G20 meeting gave support to the sceptics in their negative judgment of this gathering's outcomes. Note the difficulty of getting 20 countries with different priorities to come and work together, and even more so of getting them to agree a list of commitments more substantial than the communiqués emerging from many G7s: China's pledge to revalue its currency by 3% de facto and to improve the flexibility of its currency regime; promises by countries with budgetary margins to let slide deficits should the economic situation deteriorate. Of course, there is no obligation to stick to these agreements, apart from "peer pressures" which, over time, we have seen become increasingly effective.

## Expression of the month: AAA.

S & P's threat to downgrade the whole euro zone sovereign debt, including the six countries with a triple- A rating, has stricken those who believed themselves safely graded with the best. After all though, some say, why should the euro zone have a better rating than the United States? Certainly, the latter do little to reduce their deficit (unlike euro zone members), however they do have the dollar. S & P's shock announcement has at least one merit; it reminds us that, unfortunately, in a monetary zone the dark deeds of some do not have repercussions on them alone; like it or not, they touch all the rest. Lest we forget, EFSF resources are de-facto underwritten by the zone's six triple-A countries.

## The "domestic saving" trend is spreading.

Following the Belgian and Italian States which appealed directly to households to finance a (small) part of the public debt, it is now the Ile de France region which is thinking of undertaking the same venture. "We trust our citizens more than we do the markets" one elected official declared, adding that "savings are plentiful in France". In fact, no! Not as plentiful as all that! Our large balance of payments deficit shows that in fact they are insufficient! What the State will take from national savers means that much less for financing investments in the productive sector, which will then need to appeal to non-residents. There is no miracle.

Each month, Jean-Pierre Patat, Honorary Director-General of the Banque de France and a TAC advisor, offers his own point of view on the economic and financial news, with total editorial freedom. Email : jppatat@tac-financial.com
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