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THE BANKER'S COMMENT BY JEAN-PIERRE PATAT

A former central banker looks at the news

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Figures of the month: 3.7% of GDP, the US trade deficit. Beyond the figure, are we aware that the richest countries (G7) as a whole are heavily in deficit with the rest of the world?

The European Central Bank

Laudatory remarks regarding the ECB activities over recent weeks seem to have done little to dissipate misunderstandings on the Institution's nature and mission. With no wish to appear to be giving lessons, may we deliver a few thoughts on the subject?

- ECB and Fed: different just where they are thought to be similar; similar where thought to be different. The urgings that the ECB imitate the Fed, by massively buying up Government bonds, ignore the fact that the Fed purchases uniquely bonds from the US Treasury, which are perfectly fungible, and not bonds issued by Texas or California. Whereas the ECB being multinational cannot make massive purchases of bonds issued by disparate issuing States. By providing its huge 3-year refinancing line to banks, the ECB cleverly overcomes this fundamental obstacle, putting them between her and the States. What is more, regrets that the ECB is not performing as would the Fed in buying Government bonds directly on issue are totally baseless. No central bank, be it the Fed, the BoE or the ECB, subscribes to Government bonds in primary issues, as all such operations are made on the secondary market.

- The ECB's mandate has little need to "evolve". Yet that is what is hoped for by those who think that the Bank's mission should henceforth include maintaining financial stability. Is it not evident that she has been doing just that for some years now, and without betraying her mission? The buying of Government bonds is fully compatible with the mandate. The ECB already had such bonds in her assets, by the way, before the crisis. As for the inflationary risks that these operations would incur, it seems that the ECB's executives, who rightly consider these risks as more than theoretical, have put an end to the continuance of sterile discussions with the holders of the most orthodox views and – thanks again to the 3-year facility to banks – have closed all debate. To lend to banks is the basic charge of any central bank, and even the haughtiest sticklers have yet to find anything to say against an operation which, despite its being somewhat beyond the norms, is a potential trigger for faster monetary creation, by facilitating banks' purchases of public debt - since States thus fund themselves from banking credits.

Let us wager that debates are only on hold and that the ECB is not, for all that, treading a smooth path.

France: a "northern" country that is said to consume too much?

Getting back to the competitiveness of the French production sector, data from the French National Institute for Statistics, the Banque de France and the IMF seem to show that things are not so bad. To be sure, our wages costs rose by 13 points more than did Germany's between 1995 and 2011; however, French productivity in the manufacturing sector is said to trend at 2% above that of the German sector, something that makes the performances of the two economies quite similar as far as competitiveness is concerned. But there is even better news. The World Economic Forum (not always favorable to France) has used information mainly from the OECD and the IMF to analyze factors of competitiveness beyond pricing, in particular the environment more or less favorable from which the productive sector might reap advantage – thanks to education, the job market, the functioning of the goods and services markets, readiness for innovation and the financial system. A first outcome of this study is that the so-called "peripheral" countries in the Eurozone have very poor scores. A second is that France falls within the grouping of good results, comparable to those countries referred to as "the north" (Germany, the Netherlands, Austria, Finland) with only one slight downer for the job market. While rejoicing in these achievements, we might also ask ourselves whether the cause of our trade deficit might not result from the fact that the French consume too much vis-a-vis our productive capacity, handicapped as it is by deficiencies in two key factors concerning production: the amount of work (low employment levels cancel out the favorable effects of demography) and investment in innovation. In consequence a structural deficit.

Gold sales by central banks: a criticism that "flops".

In its last report, the French highest public audit jurisdiction comes down on the Banque de France's sale of part of her gold stocks in 2005. This on grounds that the State was in some way cheated because the sales were conducted at price levels well below those of today. Let us not forget that all European central banks carried out such sales at that time on the advice of the IMF and that everyone applauded it then, as an indicator of good management. For the reason that, in fact, the proceeds of such sales go not into State coffers but are used for investments providing higher earnings, in this case for buying US T-bonds. In 2005, with a Fed rate above 3.5%, this sale permitted the Banque de France (and other central bank) to substantially improve her profits and hence the dividend paid to the State. Today, with Fed rates close to zero, a comparable operation would earn next to nothing. Finally, bear in mind that for the Banque de France and other central banks in the euro zone, holding gold among their assets, with worth now calculated at an exceedingly high level, allows them to add some comfortable reserves to their bottom line; something that may be useful in case of losses on Government bonds…

Expression of the month: an "oldies' pact".

That is what the European budgetary pact has often been called. This critical appellation has been taken up by a researcher from the Paris School of Economics who seems not to realize that it is today's "youngsters" who will inherit the high debt levels incurred by present day "oldies". In referring as a model to the massive devaluations operated by the USA and Great Britain in the 1930s, he neglects to say that it was accompanied by a destructive unilateral protectionism. What is more, he finally suggests that the euro zone's road to salvation would be to export its unemployment to poor countries by means of a devalued currency.

Good old doctor Soros: always full of good advice.

M. Soros never misses a chance to deliver his preoccupations about the euro zone to anyone silly enough to proffer a microphone. His vocal reconversion regarding attacks on financial excesses clearly does not prevent him from being ready to pick up good business on the back of the zone. Disregarding the fact that a now hackneyed comparison with the errors of 1929 requires at least a minimum of economic background (they were made by the Fed and, as far as we know, central banks are not making the same mistakes nowadays), his latest criticisms on the return to those "errors" are of course part of a sly strategy involving seemingly innocent sound bites.

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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