

The Banker's Comment - Jean-Pierre Patat

A former central banker looks at the news

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



Figure of the month: 12th, the French GDP (purchasing power parity) world ranking according to the IMF. To ponder, or to put into perspective.

Does the franc zone need to change?

“France is open to any changes in the franc zone” declared the French minister of finance during that institution’s annual assembly.

With France, the franc zone comprises 15 African countries and is characterised by a fixed exchange rate (albeit modifiable) of the CFA franc versus the euro while CFA-euro convertibility is guaranteed by France with a monetary issue proportional to growth in foreign exchange reserves. It’s a kind of sophisticated currency board which provides the advantage for the African countries of a currency that is convertible into all other currencies (via the euro) without risk of exchange rate crises and with a guarantee of funding for current payment deficits through an “operations account” open on the French Treasury in which the African central banks place 50% of their foreign exchange reserves.

Undoubtedly, the franc zone has allowed the African State members to have, at all times, an inflation level far below that of other countries on the continent. The diagnosis is less clear regarding growth, and its detractors accuse it of not favouring growth by sterilizing part of the foreign exchange assets. But other factors - political crises, civil war, and bank timidity - also help undermine activity.

The franc zone overcame prejudice from the IMF as well as a banking crisis and survived the switch to the euro once our partners had understood that the Banque de France, although playing an essential technical role, is not involved politically in its functioning. Within African countries it is defended in economic and financial circles, accepted by their governments and criticised by the many economists and intellectuals who perceive it as a brake to growth and a remnant of the colonial past. Apart from destroying it, means for change are limited: a fresh reduction of the percentage of foreign exchange reserves deposited in the operations account; parity for the CFA’s rate with the euro within a fluctuation band (very complex). However, a good move would be to reduce the imbalances and barriers between the West African and Central African parts of the zone, where two different CFAs are issued and are not directly convertible one to the other.

The African countries in the zone suffer from political ills far more than they do from the arrangement with France, in particular from an unfortunate speciality in which a man or a family confiscates the presidential functions for a lifetime.

Names of the month: Schäuble and Sapin.

Talk about laugh! Once the German minister of finance had disclosed the arguments, difficult to contest, that he put to Mario Draghi on the consequences of the zero rate policy on the balance of financial institutions and returns on savings, he was called to order by the French minister of finance, Michel Sapin, who loftily called upon him to respect the independence of the ECB. It is understandable that certain governments, over-indebted and incurring many new expenditures financed by debt, are delighted by these so derisory money rates; but one must not become ridiculous in trying to defend them. Respecting the independence of the central bank does not imply forbidding all criticism of what it does. The ECB managers, including the top man, do not hesitate to comment upon, to criticise even, the actions of governments on some occasions. And so much the better!

Job reductions in banks: true and untrue reasons.

2000 positions wiped out at Crédit Suisse, 6000 planned for by the Royal Bank of Scotland, several hundred in France by BNP Paribas and Société Générale. And that’s not the end. The reasons invoked? Zero rates, negative even, which eat into profits, and the increasingly tight regulations, especially with strict requirements re equity. There it becomes less convincing. A BIS study shows that in judiciously restructuring its liabilities, a build-up of equity can lower debt charges. On the other hand, obstacles at the “universal bank” may have repercussions on results and eventually on jobs.

A former central banker’s self-examination.

The former governor of the Bank of England, Mervyn King, has just published a gloomy pessimistic book on the planet’s economic and financial future. Having delicately and implicitly criticised the ECB and its president regarding a quantitative easing which he views as inefficient and potentially dangerous (let it be remembered though that Mr King was one of the first to advocate such a policy and to implement it eagerly), this former leader of the English central bank focuses on differences in balances of payment with, on the one hand a group of countries in deficit (the USA, the UK, the “peripheral” Eurozone countries) and, on the other, the excess balance countries, such as China and Germany. As a good Anglo-Saxon, it is on these latter that he concentrates his criticisms, in particular on Germany (“crazy”) hinting that the Eurozone needs winding up to allow those countries in deficit to get back into balance by adjusting their exchange rates. It should be noted that in the time that elapsed between now and the writing of King’s book, those “peripheral” countries have all (excepting Greece) gone back into an excess of balance of payments. Note also that the German “model” based on exports is that of almost all European countries, whose growth stands strongly (very strongly!) on exports, and the one exception to this “model” is... France! France is also the sole country in the Eurozone, with Greece, that has deficit external accounts. Lastly, let us note that the high depreciation of the pound sterling, in conjunction with the financial and economic crisis of recent years, has been in parallel with a clear deepening of the United Kingdom’s current payments deficit.

The 3% limit for deficits, still criticised.

Some economists on a recent platform argued that we should drop the reference to the “structural” deficit for public finances to appreciate the conformity of the European countries’ budgetary policy to the rules of the stability pact. We can accept that as the ways in which this figure is calculated suffer from a lack of consensus. We concur less with the alternative method recommended: to abandon the 3% rule and link the authorised growth of public expenditure (not including unemployment insurance and exceptional expenses) to the States’ potential growth plus the 2% inflation rate targeted by the ECB. That makes a pretty nice gift to States with, notably, inflation close to 0% and showing little sign of going back up to 2%, not to mention those “exceptional expenditures” which it will be tempting to invoke even if they are not exceptional. But they must be living on another planet if they are surprised to hear described as “strict” a move to make a ceiling for deficits of 3% of GDP. A simple rule, simplistic some will say, even idiotic according to a former president of the commission; however, it is a rule that is clear and it is anything but “strict”.