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THE BANKER'S COMMENT - JEAN-PIERRE PATAT

A former central banker looks at the news

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Figure of the month: 1.75%, the new rate for Livret A savers. The formula that the government itself had come up with was 1.50%. Typical franco-French.

A federal budget for the euro zone?

The crisis, and especially the most recent development of common policies with European budgetary agreement, has resurrected the criticisms of those who believe that in creating the euro its conceivers had set up a wobbly system, with the monetary pillar unsupported by a budgetary one.

At its creation, the euro was in fact far from moving in an institutional vacuum, especially a budgetary one. At the risk of becoming boring, I repeat that the Stability and Growth Pact, had it been correctly respected by all countries, would have been able, like a federal budget, to play the role of shock absorber for crises in allowing more fiscal flexibility at times of economic lows.

The pact was gutted of substance by several countries, France among them, who interpreted the 3% of GDP limit for the deficit as a mere cruising speed!

Now it's a federal budget that is being demanded by some, and that's a totally different affair. A federal budget is not fed by resources from federated States; rather it is fed by its own taxes with which it meets its assigned expenditure. Some suggest transferring taxes on businesses together with the costs of unemployment insurance to it. Why not? This would make it highly reactive to the economic climate.

We should nevertheless remember that this would suppose standardising the rates for selected "federal" taxes and the benefits for all countries. In brief, creating a federal budget is not a question of making a simple addition to the euro structure, rather it is one of making a considerable step towards a political federalism because there can be no common budget without government to steer it. Are we ready for this? All seventeen of us?

Our German partners have joined this problem by proposing a deepening of federalism between those countries ready to do so, thus dropping the holy principle "all or none". Is this the path to follow, or is it "old fashioned federalism", as some have described this suggestion?

The drop in the price of gold, an early sign of recovery?

Since September 2012, the price of gold has dropped around 10%, standing since then at around 1,650 dollars an ounce. Let us start by considering the difficulty of relating evolutions in the price of the yellow metal to anything. For a long time, it was correlated, negatively, with the dollar, a correlation seriously undermined for some years past. The link with inflation against which this investment is supposed to offer protection is not proven. At the start of this century the price of an ounce of gold was 260 dollars and many analysts thought that in future it would be useful only for jewelry. Clearly, one can make a link between the increase in gold prices of recent years and the climate of anxiety created by the crisis, one could even evoke the extremely low interest rates on financial investments. Can one though truly explain a phenomenal hike for an investment that has seen its value multiply by seven in 10 years? Getting back to the drop over these last months, some observers parallel it with the significant price rise for steel, deducing that a recovery is in the offing. Let us hope so, even though prices for zinc or copper remain subdued, and that in consequence a reason can be found for the lowering of gold prices that really coincides with a significant improvement in the European climate and especially that of the euro zone.

Cyprus, a symbol of excessive enlargement of the Eurozone.

The difficulties for the Cypriot economy and its confrontations with European institutions show, to a level of caricature, the damages of enlarging the euro zone on the sole basis of the so-called "convergence criteria" (budget, public debt, prices, long term interest rates) which fail to take into account indicators of competitiveness like the balance of payments. In 1999, in starting the monetary union with 11 (which had seemed impossible barely two years before) and in moving to 12 soon after, the zone's leaders were assuming that stabilising anticipations of inflation and aligning interest rates along the lowest would create a framework able to favour the setting up of needed structural reforms in countries whose low competitiveness was obviously known. We now know that this was not really the case and we pay the price today. Cyprus is a tiny part of the zone, but the nuisance capacity arising from its problems is not in proportion to its GDP, since a monetary union is not a club; rather it is a group whose solidarity is fusional, something that some evidently do not realise.

Name of the month: Jens Weidmann.

It's not a well-known name, but we cannot resist bestowing this honour of the month upon him. Jens Weidmann is President of the Bundesbank. For some time we have not heard this institution's leaders grumbling about the ECB and its actions. This was just a delay. Mr Weidmann violently opposed the project for European banking supervision being entrusted to the ECB, invoking the "Chinese Wall" principle which is supposed to forbid a central bank in charge of monetary policy from being concerned with banking control out of fear of a conflict of interest. As far as he is concerned, the ECB's independence is threatened by this project. No less than that. We wonder whether the leaders of the Bundesbank have ever heard talk of "financial stability", which is at the heart of the crisis we are encountering, and of its demands. Demands that send to the wall principles that in any case are arguable.

Oil does not lead to happiness.

That's the remark that springs to mind when one looks at the "performance" of some African countries that are huge producers of black gold. Angola, under support from the IMF, is ranked 148th of 187 countries for human development (UN source). Nigeria, where the manna of oil has been harvested for several decades, only just reaches a 60% literacy level and the human development index puts it 156th of 187. The award goes to Equatorial Guinea with barely 700,000 inhabitants; if one also considers the size and longevity of its oil resources, the inhabitants should all have diplomas. Again, 10% are illiterate, life expectancy is 50 years; the GDP is 14,374 dollars by capita: by African standards that's a nice figure, but it is pure illusion, with wealth confiscated by 5% of the population, while the human development index ranks the country 136th out of 187.

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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