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THE BANKER'S COMMENT - JEAN-PIERRE PATAT

A former central banker looks at the news

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Irresponsible central banks.

The IMF, the OECD, governments, economists, journalists, compulsive deflationophobes all, are unanimous in approving the policy of the great central banks. The Fed, the ECB, the Bank of England (all stuffing the financial planet with central money) are unanimous. As far as the ECB is concerned they even figure that it is somewhat backward compared to its American counterpart and that it could do even better; why not purchase government bonds? A most ungrateful attitude towards its president who is trying to please the markets and stand out from his predecessor, the *dogmatic* Trichet.

Nevertheless, it is the IMF itself, fearless of contradiction, that is pointing out the perils for financial stability of an excess of global liquidities that favour speculative operations and not at all distribution of credit to the private sector (see later). Markets speak for themselves. The Dow Jones is nearing historic records, the Nasdaq has never been so high. And when one sees the Italian State borrowing at a lower rate than the US, when one sees the French State (whose management of public finances is criticised in Brussels) borrowing at 1.6%, it becomes hard to convince anybody that the wonderful management of these countries counts for something. This without considering the impact of accommodating monetary policies on international commodity and food prices, with worrying parallels in the past between the price rises of these products and the Fed's announcements of new quantitative easings.

That said, the Fed does sometimes seem to be aware of risks taken, and its policy (most careful) of reducing bond purchases contrasts with the ECB's gung-ho attitude. But, some will say, growth is weak and unemployment high in the euro zone.

Right – but apart from the fact that growth is not weak everywhere in the zone and ignoring the tenacious scepticism of the author of these lines regarding the capacity of monetary policy to stimulate economic growth, increasing the risks of a financial crisis does not replace the need for reforms to overcome obstacles to growth in certain countries.

So? Will the ECB be responsible for a next financial crisis?

The Rooseveltian dream.

It's a dream that's pretty common in France and a minister brought it back by invoking memories of this American president with his New Deal and the famous dams of the Tennessee Valley Authority. Never mind the fact that, although the New Deal brought undeniable advances in social laws that were sadly lacking in the country, it had only a limited impact on growth - growth that only really came about with re-arming. They talk of a great development programme for "infrastructures" in Europe, funded by debts of course, but it will suffice, they tell us, that Brussels agree that the financing of investments and debts incurred be excluded from the budgetary deficit and the total of the public debt. How come no-one ever thought of this ingenuous solution before? Apart from the fact that Europe doesn't seem to be too short of infrastructures, we feel that public intervention would be better targetted in helping the private sector which is better suited for choosing appropriate investments and, above all, in sorting out expenditure to respect the undertakings made long ago in Lisbon to devote 3% of public spending to R&D.

BRICs, yuan; a Quixotic war against the dollar.

The BRICs have decided to create a regional monetary fund to challenge the IMF. China is trying to develop the international use of the yuan (CNY), and what is more, Paris, London and Frankfurt are squabbling over the prize that could well be the issuing of bonds in Chinese currency. Does this signal a programmed end for the dollar and America's monetary domination? Of course not. Despite the coining of an acronym, the BRICs are not exactly a unit. Issues in CNY today are worth 900 million dollars versus 9,000 million in USD. Following the BNPP mishap, which showed the dollar's still unbeatable power, a reply to these illusions is found in the ECB's latest report on the euro's international use – a prestigious currency, but one whose issuer lacks the strategic and political power of the US, just as important as economic power in this respect. The euro stagnates as a reserve currency at a level of 24%, with 64% for the dollar. Above all, while the European currency used to be level with the dollar for international bond issues, these are now lower by a third than those issued in dollars.

Name of the month: Didier Marteau.

He is not a central banker, nor a minister, nor is he a renowned communicator. But he's "my" man of the month. A professor at the French businbess school ESCP, he has the rare talent of smashing into all the present-day commentaries on the accommodating monetary policies of the Fed and the ECB – and that is refreshing! No, he writes, those central bank operations do not create money (the "printing press" so dear to our analysts); rather they create central money (or monetary base) and this abundant creation has no effect on the distribution of credit by banks, which depends mainly on demand and not on a preceeding accumulation by banks of a mattress of central money. Certainly, the action of those central banks does have some happy effect on bond yields for public debts, perhaps it even creates an effect of wealth with the upward swing on the stock markets that it stimulates, but without doubt these are its sole contributions to growth.

Fixed or variable rates for home mortgages.

The Bank of International Settlements foresees a greater use of variable rates for mortgages which thrust any risks of a higher rate on the client, as opposed to a fixed rate where the bank is obliged to manage this interest rate risks. In the United States, variable rates are common-place. French banks are less enthusiastic about following a route which might well be the source of plenty of contention with a clientele thinking they are being twisted. Over time this writer has found several positives for variable rates, which render monetary policy efficient more quickly; however, the financial crisis of recent years convinced him that their toxic effects are a lot worse than any technical advantage they may provide. Let's add too, that with today's very low rates, variable ones would hold little attraction for anyone.

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 views, with total editorial freedom. Email : jppatat@tac-financial.com