



JEAN-PIERRE PATAT'S MONTHLY CHRONICLE

A former central banker looks at the news

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Figure of the month: 898 billion: the ECB's outstanding re-financing on June 25th, a jump of 45% over one week mainly resulting from long-term intervention.

Regulation reforms in the USA and Europe. The problems are not the same.

With no less than five sections: regulation of financial institutions, market regulation, client protection, strengthening of measures used by authorities for crisis management, and lastly the international facet - the financial reform project as presented by the Obama administration appears wide-ranging; greater in any case than the measures recently adopted by the European Council. Europe is "lagging", according to some derisive media. They are wrong, because the problems are not of the same kind.

In the United States it is a question of filling gaping holes, even though several control bodies exist which often overlap but without much efficiency for all that. They try to correct the initial weakness by creating a new controlling body, the National Bank Supervisor, which should oversee chartered banks and the multitude of establishments which do banking; however, thanks to confused American jurisprudence, these establishments can exercise this profession without any regulation or control. What is more, a Supervisory Council for Financial Services has been created, charged with detecting risks for the entirety of the financial system. Nevertheless, this has not put an end to the fragmentation of controls. It is the Treasury that will head the National Bank Supervisor, whilst the Fed, whose responsibility has been extended to cover risky establishments, will continue to supervise the Bank Holding Companies. It also appears that the FDIC will continue to carry out supervisory missions.

In Europe, it is a question of improving co-ordination for the activities of bodies which as a whole work quite well, but within national frameworks, thanks to an in-built European System of Supervision which would be mainly concerned with cross-border establishments. Additionally, a European Council for systemic risks has been created.

We do not believe that the Fed will be strengthened by this project. Its field has been widened, but the National Bank Supervisor cuts into its responsibility which should have been universal. And, whilst in Europe the Council for systemic risks will be headed by the President of the ECB, in the United States it is the Treasury which will head the Supervisory Council for Financial Services, with the Fed being only one member among other regulators, without even the title of Vice-President.

Fatal inbreeding.

In the USA, the professional track record of those who at some time in their life have carried public responsibilities in financial and monetary matters could perhaps explain, better than would a long accusatory speech, how the system cannot avoid the most diabolical drifts: Paul Volker, private financier, became President of the Fed, then went back to an investment bank before returning to public office. Paulson was State Secretary at the Treasury between two spells at Goldman Sachs. The same wanderings for Robert Rubin ... and, to cap it all, Greenspan has been hired by a large hedge fund for which, apparently, he has earned a great deal of money in the markets despite their devastation. May we permit ourselves to prefer our own technocrats, in particular the one in Frankfurt, rather than these men, whose closeness to the markets and their excesses has marked the past and serves to ensure for them a richer future than is offered by public service.

Expression of the month: Great Loan.

A French specialty, dusted off. Not to finance the debt (!) as some newspapers naively headlined it, but to loosen a funding constraint on investments. After all, why not, when one realises that a tax increase can only bring home the bacon if it is both massive and antisocial (a VAT hike). But we must not forget that loans have to be repaid! Nor that the necessarily "referendum" aspect that such an operation can take will induce the government to load it with "sweeteners" damaging for the future. Let us remember the wonderful "Giscard loan", indexed on gold, and which had to be repaid at ten times the amount borrowed!

Commission because the system grants one Commissioner per country, whereas a dozen members only would allow for more efficient management. The Lisbon Treaty had envisioned a reduction of numbers. Unfortunately, so as to get the Irish to vote yes, the Union is backing away from that wise move.

Public finances: the crisis maelstrom and the deficits explosion are masking France's calamitous situation.

In general, and if one is to believe the OECD, France's situation in the years to come might not be as bad as that of its partners: in 2010, our public debt might "only" represent 80.5% of GDP, as opposed to 83% in Great Britain, 93% in Belgium and even 81.5% in Germany. Alas! The full particulars of the deficits show that what we are, actually, is the continent's dunce. The so-called structural deficit, built up following thirty years of disastrous management, reaches at least 2.5% of GDP. Yet it is virtually zero in Germany, low in Belgium and Austria, whilst Spain, the Netherlands and Finland still boast a surplus structural balance. Even Italy, with 1.5% of GDP, is doing better than us. In such conditions, it is hard to understand why the Minister of the Economy asked our partners to put to one side that part of the deficit resulting from the crisis in order to build up respect for the Stability and Growth Pact. That proposal reinforced our image as a "humbler" country (at least in this domain) and its implementation would have rebounded on us like a boomerang.

Organised deflation in the Baltic countries.

Down 20%, down 10%, down 50%; those are the reductions decreed by the authorities in Latvia for the minimum salary, pensions and teacher salaries. Agreed, their public finances were registering a colossal deficit, but can one be sure that such a high dose of oxygen will not completely asphyxiate an economy already suffering a recession of nearly 15%, bringing about a fatal chain reaction? We know what happened in France in the 1930s, with the "Laval" deflation and its component of lowering civil service salaries. Nevertheless, these measures are approved by international organisations, but the lucidity of these parties, as seen in the past, is not always exemplary. And now Lithuania, and perhaps soon Estonia, will adopt this organised deflation. Let us not overlook the fact that the banking system in Scandinavian countries, especially that of Sweden, is heavily engaged in the Baltic States.

Korea, a forward indicator?

For the second consecutive quarter, South Korea has registered low but positive growth in its GDP, an exploit and an exceptional one within the OECD. Considering that 60% of the wealth created in that country stems from exports, this might well be an encouraging sign for the evolution of world trade. Prudence, even so - other countries such as Germany, also heavily dependent on exports, have yet to see improvements.