



**Interview of François Villeroy de Galhau, Governor of Banque de France**  
**BFM BUSINESS Good Morning Business– December 9, 2016**

**STÉPHANE SOUMIER**

Good morning François Villeroy de Galhau and thank you for coming in to see us today...

**FRANÇOIS VILLEROY DE GALHAU**

Good morning Stéphane Soumier.

**STÉPHANE SOUMIER**

We've got about 15 minutes together. I'd like to start with the forecasts that the European Central Bank has published for France...

**FRANÇOIS VILLEROY DE GALHAU**

No. It's the Banque de France that has published its forecasts as part of what we call the Eurosystem, which is a genuine federal system, a collective system made up of the European Central Bank and the 19 national central banks, but in which the Banque de France plays a very active role. I'd just like to point out that it is a federal system that works in Europe. That's quite interesting. We publish our independent projections twice a year...

**STÉPHANE SOUMIER**

Let's take a look at the figures then.

**FRANÇOIS VILLEROY DE GALHAU**

Let me just stress that word [independent]. So, to sum up the main messages, growth is holding up in France, but it is still a bit low compared with the average for our European partners. We're below what our best-performing neighbours are doing. We'll probably be at 1.3% in 2016 and 2017, and there should be a bit of an acceleration after that...

**STÉPHANE SOUMIER**

Compared with around 1.7% for the euro area, is that right?

**FRANÇOIS VILLEROY DE GALHAU**

For the euro area, yes, we're expecting 1.7% in 2016 and 2017, which is good news – growth in the euro area is not only being confirmed, it is also tending to accelerate; and we then expect 1.6% for the years 2018 and 2019. That means there's a solid foundation of growth in the euro area and it's up to us, in France, to see how we can pick up our pace.

**STÉPHANE SOUMIER**

Why is France lagging behind a bit with its growth rate?

**FRANÇOIS VILLEROY DE GALHAU**

When a car isn't travelling fast enough, as is more or less the case with the French economy, there are two possible scenarios. If you're not at full throttle, you have to step on the accelerator. That, you could say, is the role of monetary policy. What we decided on yesterday was how to support European and thereby French growth by stepping up our monetary policy. But when your engine is already at its maximum limit, then you need to tune it to make it more powerful.

That's where the problem with the French economy lies – we're stuck at a slower pace of reform than our neighbours. Germany, Spain, the Nordic countries, and even the Benelux countries, a lot of our neighbours are showing that, within the framework of the European social model – because we all share the same model – there is a way of implementing reforms that deliver more growth and more jobs. That's the main concern for our citizens. And several of the European countries that I've just mentioned have achieved full employment. So having growth...

**STÉPHANE SOUMIER**

While our unemployment rate, I've looked at your figures, our unemployment rate is still 9.5%.

**FRANÇOIS VILLEROY DE GALHAU**

Our unemployment rate is falling, which is good news...

**STÉPHANE SOUMIER**

9.5%!

**FRANÇOIS VILLEROY DE GALHAU**

But it is not falling enough. We should get below the 10% threshold for unemployment according to the international definition – what we call the International Labour Organisation definition - in 2017. That's good news, but clearly we need to do more. The other bit of good news is that, when we look at our neighbours, it is possible to have more growth and more employment within the bounds of the European social model. And I think the vast majority of our citizens are attached to it.

**STÉPHANE SOUMIER**

There's one figure that I think is going to be in the headlines, because it's as much a political as an economic issue. It's that you think France will not get its deficit down to 3% by the end of 2017. Is that 3% public deficit figure still important?

**FRANÇOIS VILLEROY DE GALHAU**

According to our current projections, we will fall slightly short of the 3% target. We should get down to 3.1% in 2017. And yes, the 3% figure is important, Stéphane Soumier, because 3% is the basis for maintaining our credibility in Europe. We've been promising for years to get down below 3% which is the upper limit set under European rules, what we call the Stability and Growth Pact. If I can, I'd just like to make more of an overall comment about France in Europe...

**STÉPHANE SOUMIER**

Go ahead.

**FRANÇOIS VILLEROY DE GALHAU**

Today I am absolutely convinced - and I say this as someone who spends a lot of time with his European colleagues and at European meetings – Europe needs France, Germany needs France, even more so now in the wake of Brexit. But to be listened to in Europe we have to be believed. So meeting the 3% target, getting below the 3% figure, is the basis for remaining credible in Europe. It is therefore in our collective national interest, and this applies as much to the current government and to the current budget, as to future governments, regardless of who they are. The Banque de France is not there to take sides in politics because, as I said before, the Banque de France is independent. But getting below that 3% - let me give you a few figures - means making EUR 4 billion of savings. And EUR 4 billion of savings means cutting spending by 0.3%; that should be achievable.

**STÉPHANE SOUMIER**

Money's free now, Mr. Villeroy de Galhau – and we'll talk about that in a minute – you're doing what you can to make sure money is free, so ultimately why not use all that free money to stimulate the economy? That's what a lot of economic institutions are saying today.

**FRANÇOIS VILLEROY DE GALHAU**

It's true, money is free, but the debt that stems from deficits has to be paid back. Do you know what's been happening in France? Look at what's happened in just a single generation. In 1980 French debt was at 20% of GDP. Now, just a generation later, we're at close to 100%. That means we've multiplied by five the size of the debt burden we're leaving to our children. If we had had a lot more growth and employment than everyone else, then that would have been fine. But that's not what happened. Look at the two countries that are, unfortunately, the champions when it comes to deficits and debt: France and Italy. They're also the two countries that are lagging behind in terms of growth and employment. So what will work in France and Italy is more reform. In contrast, in other countries – and this is what the European Commission and other international organisations are saying – in other countries that have got their public finances in order, that have reduced their deficit and even got rid of it altogether, as in Germany, then yes, there is room for fiscal stimulus, and it needs to be used.

**STÉPHANE SOUMIER**

Does that mean that we're being completely reckless with public spending at the moment? That the spending floodgates are being opened up, and that's why we've gone from 2.7 to 3.1% for 2017?

**FRANÇOIS VILLEROY DE GALHAU**

No, not at all, because we're still forecasting a reduction. The deficit is projected to narrow between 2015 and 2016, but the pace is too slow.

You mentioned public spending; again, let's compare ourselves with our neighbours: we have the same social model, which is great. It's a social model with a lot of public services, with less inequality than in the United States. Look at the electoral debate surrounding Brexit or Mr Trump. This European social model stands for something. It's a good response to globalisation. But our problem in France is the cost of this social model. In France, it costs us 56% of GDP. For our European neighbours, that figure is 47%. The difference between the two is around EUR 180 billion. I'm not saying we should save that much overnight, just that that's where we need to look if we want to make our public system more efficient.

**STÉPHANE SOUMIER**

As regards monetary policy, you have injected almost EUR 1,700 billion of new money into the system, and this programme is to be extended with an additional EUR 540 billion, is there no limit?

**FRANÇOIS VILLEROY DE GALHAU**

We are doing what is necessary to achieve our objective. You know that the Eurosystem, which we were discussing earlier, takes collective decisions, and does so independently of any pressure or lobbying, and above all with a view to meeting the objective assigned to it of slightly positive inflation, a target of 2% in the medium term. Yet, for the moment this target is not being met. Therefore the decision we took yesterday shows that we are highly flexible and pragmatic. You might remember that a few days ago commentators were saying that “the European Central Bank is going to be stuck, what will it do? There is the problem of Mr Trump’s election, Italy, market constraints, etc.”

Yesterday, I believe that we gave three clear messages: the first is that we are reducing our volumes of monthly purchases. The figures that you are quoting translate into monthly purchases at a rate of EUR 80 billion until the end of March 2017, which will then be brought to EUR 60 billion thanks to signs of progress. European growth has been confirmed at 1.7% and is strengthening as we said earlier, and the risk of deflation or negative inflation, which is a fatal disease for the economy, has receded. I believe that we have defeated deflation thanks to our monetary action.

Secondly, we are showing determination; we are remaining active because we haven’t yet reached this inflation target of 2%. Inflation currently stands at 0.6%, and is set to rise in the coming months to stand at close to 2% by 2019.

Lastly, the final component of this decision, which I believe is very important, although it has been less widely stressed, is that we are providing visibility up to the end of next year with our commitment to make monthly purchases of EUR 60 billion for the next nine months...

**STÉPHANE SOUMIER**

Yes, indeed.

**FRANÇOIS VILLEROY DE GALHAU**

We are in a period of great uncertainty with numerous shocks this year: financial market turmoil at that start of the year, Brexit in June, the election of Mr Trump in November, and next year the electoral cycle in Europe. Amidst this uncertainty, the euro is a mark of stability and monetary policy is a mark of visibility; we are saying to economic players: “you know what to expect in terms of the cost of financing and lending volumes until the end of next year”. This is a very clear signal that we are sending to them.

**STÉPHANE SOUMIER**

Just quickly, because I have two other important questions, yesterday markets went into freefall when they saw that volumes were being reduced from EUR 80 billion to EUR 60 billion; then after the phrase “yes, but we will continue”, they went back up. We get the feeling that we’ll never see the end of this monetary policy, Mr Villeroy de Galhau – we will see what the US Federal Reserve, which is starting to raise its rates slightly, will do, but we have the feeling that you are propping up a system that has reached its limits.

**FRANÇOIS VILLEROY DE GALHAU**

No. First, let me remind you that the Federal Reserve already raised its rates a year ago and will probably raise them further this month, but our decision is taken fully independently, including vis-à-vis US policy, and is taken in respect of the situation in Europe. As regards the latter, it’s not the markets that decide, we consider the current economic situation, as it actually stands.

**STÉPHANE SOUMIER**

Yes, but aren’t they sending a signal that they still need you, desperately?

**FRANÇOIS VILLEROY DE GALHAU**

It’s not the markets that need us, it’s the European economy, i.e. firms and households, via the financial system. What counts is the financing of the real economy and today we are reducing monthly volumes because there are a certain number of signs of progress, but indeed, until we are close to our 2% inflation target, we will remain active with our monetary policy. And for a simple reason; it is not because certain players depend on us but because this monetary policy is effective. All the estimates, including those of the German Bundesbank – which isn’t seen as the most outright supporter of this monetary policy - show that this monetary policy contributes between 0.3 and 0.5% to European growth per year and the same amount to inflation. This may appear a little abstract but, between 0.3 and 0.5% of additional growth in France translates into around 100,000 jobs creations each year. It is very important that monetary policy contributes to this. But it isn’t the only game in town – it’s the accelerator we mentioned earlier - and, in parallel, we have to continue to work on the power of the engine.

**STÉPHANE SOUMIER**

A word about the Italian banks. Are you resigned to let the Italian government bail out the banks that need to be recapitalised, whereas the aim was to cut the cord?

**FRANÇOIS VILLEROY DE GALHAU**

The current European rules allow for, in strictly delineated cases, the possibility of state intervention provided that the other creditors and shareholders have been duly called upon. Italy, to date, has favoured market-based recapitalisation for the main bank to which we are referring, i.e. Monte Dei Paschi Di Siena, which as you know is the oldest bank in the world.

**STÉPHANE SOUMIER**

Indeed, we realise that it is nevertheless complicated.

**FRANÇOIS VILLEROY DE GALHAU**

I think that they are still studying this scenario. If they decided to move to a public recapitalisation plan, under these European rules, this would not be ruled out but would be the decision of the Italian government under the oversight of the European supervisor. We have made considerable progress. You mentioned cutting the cord. We have set up in the framework of the European Banking Union a single supervisory mechanism, in which France participates but which is established in Frankfurt, and which supervises with the same strictness and the same rigour all European banks.

**STÉPHANE SOUMIER**

Last point. Yesterday, the Constitutional Council approved, in the framework of the Sapin II Law, a provision that upset a vast number of savers and that also immediately impacted life insurance plans: the possibility that you will have, you François Villeroy de Galhau, via the regulatory bodies, to freeze our savings for six months in the event of a sudden rise in interest rates.

**FRANÇOIS VILLEROY DE GALHAU**

I am glad that you've raised this question because this has been presented in an excessive way. First, it is an exceptional measure, in the event of a severe crisis. Second, it is not up to me alone but also to the *Haut conseil de stabilité financière*, which is a collective body chaired by the Minister of the Economy and in which independent economists will decide on the action to be taken. And its aim is simply, in the event of a severe crisis, with the withdrawal of some savers' funds from life insurers, to be able to protect other savers. It is vital to avoid certain policyholders becoming trapped, with their funds no longer protected. Therefore, contracts between savers and their insurance companies are not being called into question. Returns on life insurance policies still remain amongst the most favourable. They are over 2%, which is very good in the current low interest rate environment. And I would like to draw your attention to one point: this type of measure, which sets out to protect the interest of customers, has existed for banks since 2013 within the same *Haut conseil de stabilité financière*. Nobody discusses it because it hasn't needed to be used but is a protective measure that exists in the event of a serious crisis. Its aim is obviously not to freeze people's savings in normal times.

**STÉPHANE SOUMIER**

Many things are odd in our financial world today, Mr Villeroy de Galhau, but it is extremely strange when savers have to guarantee insurers' risks. Usually, it is the other way around. Is it because insurance companies have taken too much risk at a given time that you need to implement such measures?

**FRANÇOIS VILLEROY DE GALHAU**

No.

**STÉPHANE SOUMIER**

Are they still taking too much risk with current life insurance returns?

**FRANÇOIS VILLEROY DE GALHAU**

No. It is not a matter of savers guaranteeing insurers' risks. It is quite the opposite. We must ensure that, in the event of a severe crisis, certain more intelligent and better informed savers – i.e. the biggest savers – do not come out better off at the expense of the great majority of savers. But, once again, we are talking about an exceptional severe crisis. Like all protective measures, it is not designed to be applied and is supposed to act as a deterrent. Furthermore, life insurance policies remain a very advantageous instrument and I believe that the right direction - as you were saying about the soundness of insurers, which is what matters to me as a supervisor – is a gradual decline in life insurance returns. This is what has been happening up to now. They need to continue to

align themselves with the interest rates we were discussing, which is once again a very favourable level of interest rates for the economy.

**STÉPHANE SOUMIER**

And the very last question; what do you say to business leaders who are hesitating at the moment, is it the right time to invest?

**FRANÇOIS VILLEROY DE GALHAU**

I have the greatest respect for entrepreneurs...

**STÉPHANE SOUMIER**

Yes, but that's the point...

**FRANÇOIS VILLEROY DE GALHAU**

You know me...

**STÉPHANE SOUMIER**

They need visibility.

**FRANÇOIS VILLEROY DE GALHAU**

No, they have to decide themselves whether or not to invest. But what we are saying to them, with our projections and yesterday's monetary policy decisions, is that we have a solid growth outlook in the euro area. At the same time, we haven't revised down our growth forecast in spite of Brexit and despite all the shocks we mentioned. Therefore the euro area remains very robust and confidence-inspiring. Moreover, we say to them: "if you wish to invest, you will benefit from the most favourable financing conditions ever". One of France's advantages, which we rarely mentioned, is that it has a sound banking system, some of the highest lending volumes in Europe – to firms and households – and the lowest lending rates in Europe. There are, thanks notably to the actions of the Eurosystem, favourable investment conditions; it is true.

**STÉPHANE SOUMIER**

That was the Governor of the Banque de France, François Villeroy de Galhau, on BFM Business this morning.