CHATHAM HOUSE

Chatham House, 10 St James's Square, London SW1Y 4LE
T: +44 (0)20 7957 5700 E: contact@chathamhouse.org
F: +44 (0)20 7957 5710 www.chathamhouse.org

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Transcript

Achieving Sustainable Growth: Fiscal Consolidation and Financial Market Regulation

Dr Wolfgang Schäuble

German Federal Minister of Finance

Chair: Dr Robin Niblett

Director, Chatham House

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Dr Wolfgang Schäuble:

Ladies and gentlemen. Let me get straight to the point: As a result of recent crises we have learned that the dream of self-regulating and stable international financial markets is elusive, that financial markets, like all free systems, need rules and boundaries they cannot set or enforce themselves effectively.

As academics as well as practitioners have begun to question the efficiency of financial markets, policymakers have begun to strengthen the role of the state. The understanding is growing that financial markets work well in general, but they do not always act rationally, since human beings do not always act rationally. Like human beings financial markets need institutions, need rules and boundaries to act responsibly.

The objective is to find a new balance between financial markets and the state. Financial markets need a regulatory framework that above all increases transparency, reduces extreme leverage, and limits excessive volatility. Only the state can provide such a framework. In times of global markets only the community of states.

But strengthening financial markets to make them more transparent and less volatile is a laborious process. The G20 have embarked on this process. Indeed the G20 have already decided on a number of crucial reforms to strengthen financial markets: Above all, they have endorsed a new capital and liquidity regime for banks – Basel III. They are also set to endorse a new regime for systemically important financial institutions that will comprise additional capital requirements and measures to improve the resolvability of SIFIs, including global active ones. Most G20 nations have also introduced smarter compensation and liability rules that will help reward long-term success, not short-term profit maximisation, thus reducing volatility.

Despite these achievements, I see an increasing danger – not so much of 'regulatory fatigue' – but of 'regulatory parochialism'. Not only within the G20 but in Europe as well: One example is the Financial Transaction Tax. It is short-sighted parochialism which is currently keeping us from implementing a European Financial Transaction Tax. If an FTT were introduced in all of Europe – which of course includes UK - it could help reduce volatility further, not least because it could make leveraged trading less profitable.

I am also in favor of an FTT because financial market participants need to convincingly demonstrate to taxpayers and their fellow citizens that they are willing to contribute to clean up the mess they helped to create. One way of doing that is through the FTT. With a reference to President Obama, the FTT might be the only thing standing between banks and the pitchforks.

Above all, the current demonstrations against financial market participants show that the FTT can play an essential in peace-making between different parts of the society.

To stabilize the international financial system we need to overcome such parochial behaviour, increase transparency and reduce volatility: We need to make dark pools and over-the-counter-trades more transparent; regulate the shadow banking system - including hedge funds - and confine the risks posed by the extensive leverage of some modern financial instruments, including Credit Default Swaps. We also need to make the assumptions of rating agencies more transparent and wean markets away from their influence. States empowered rating agencies so that they could point to policy errors earlier than financial markets and thereby smoothen market reactions. But the opposite has happened.

Don’t get me wrong here: This does not mean that an obsession with the market should be replaced by an obsession with ‘statism’. One extreme is just as bad as the other. But I am deeply convinced that for financial markets to contribute positively to society – and function efficiently – international financial market policy must refocus financial markets on their primary role, which is to serve the real economy. Clearly, not all of the products offered by the financial industry are necessary to fulfil this role.

We need to limit ’irrational exuberance’ as well as ‘irrational gloom’ of financial market participants more effectively, i.e. we have to limit excessive leverage and perilous volatility more effectively. To do this, regulation must restore the link between risk and liability, reward and responsibility of financial market participants and institutions.

The core lesson from the past crises is that highly cyclical, credit-fuelled growth, which is driven by the financial market, does more harm than good. Instead, we need to create the conditions for lasting and sustainable growth: Sustainable growth defined as steady, environmentally-friendly and socially-compatible growth propelled by the industry and productivity of the real economy and not by an overleveraged financial sector which can cause erratic volatility and massive distortions.

A growth model focused on the real economy has more advantages than a financial sector driven growth model, which generates high growth rates when the economy is running well, but fails in downturns without government support to prop it up.

This takes me straight to the crises within the Euro area: Weakened national economic fundamentals were not the only reason for the dramatic worsening in Portugal's, Spain's or Italy's refinancing conditions. Indeed, events in Europe demonstrated again that modern financial markets can increase volatility. We saw how the Euro area was at a risk of being torn apart by the tremendous speed at which the situation of the European bond market was deteriorating. Seen in that light, our task, policymakers' task, is to reduce financial markets' potential for making crises worse.

This does not mean that we must abandon interest rates as a disciplinary mechanism. On the contrary, governments need the markets: Markets can force governments to do the right thing – although too often too late and too suddenly. No, putting all the blame for what went wrong on financial markets would be convenient, but far too easy. In the Euro area, excessive government spending has led to levels of deficits and debts that are unsustainable and endanger economic welfare. Euro area governments need to demonstrate convincingly their commitment to fiscal consolidation but also to increasing competitiveness to restore confidence of markets as well as their citizens.

And there is no disagreement about the fact that Europe, and above all the Euro area, must improve the link between its countries' national fiscal and economic policies. It is essential that the European Monetary Union's institutional structures are indeed capable of obliging Euro members to adopt a budgetary and economic policy that reflects their responsibility for the common currency. European Monetary Union won't succeed if a number of countries persistently run deficits and weaken their competitiveness at the expense of the Euro's stability.

But what we are faced with is more than a sovereign debt crisis of a few spendthrift countries in the Euro area. We are faced with a fundamental shift in financial markets' attitude towards public debts: Debt and deficit levels which might have been tolerated only a few years ago are now considered to be too high and unsustainable. That is perhaps because markets – as well as citizens – have come to realize that for more than two decades, economic policy in industrialized countries has tried to avoid recessions by sacrificing fiscal prudence and monetary rectitude in the process. When financial markets crashed, central banks, particularly in Anglo-Saxon countries, cut interest rates. And when growth declined, governments plundered the public's purse to make up for the private sector's reluctance to spend freely.

Monetary and fiscal lavishness led to a series of debt-financed asset bubbles. As these financial bubbles burst in the last three decades, it became even more difficult and expensive to contain the fallout on the real economy. When the last of those debt-financed bubbles burst three years ago, governments had to up the ante and use massive fiscal stimuli and central banks had to take resort to unprecedented measures of easing monetary policy to avoid the breakdown of financial markets and an ensuing depression. For example in Germany we suffered a loss of 5.1 percent of GDP in 2009, we had never thought that would be possible in the times after World War II.

To be fair, those measures have been necessary to avoid a depression. But too often governments have promised they would consolidate when times were good. They rarely did: Debt and deficit levels kept creeping up. As a result governments' credibility with financial market participants is at an all time low. Markets and citizens have become increasingly suspicious that governments would not honor their debts. As a consequence markets demand higher risk premiums, i.e. interest rates. And they withdraw their confidence at a whim today, already when governments only appear not to take credible immediate action to place their debts and deficits on a sustainable footing.

But governments are faced with a predicament. There is little political or market appetite for more fiscal and monetary stimuli. On the other hand markets and citizens do not crave tighter fiscal and monetary policies either, for fear of their economies heading back into recession.

So, what do we do? There is a feeling that politics is at wit's end. There are those who argue that fiscal consolidation, a smaller public sector and more flexible labour markets will lead to a decrease in consumption in these countries in the immediate future. But there is a trade-off between short-term pain and long-term gain: I would argue that an increase in consumer and investor confidence and a shortening of unemployment lines will in the medium term cancel out any short-term dip of consumption.

Governments and central banks have used up much of their fiscal and monetary firepower. We will not spend our way out of the current predicament, nor will it work to lower the debt burden by inflating the problem away. I think it is no accident that unemployment in the US has remained stubborn despite all the efforts by the Federal Reserve and the United States government to promote growth. Loosening monetary and fiscal policies in the short-term while promising monetary and fiscal tightening in the medium-term might have worked in the past. Today however, as market reactions demonstrate, it lacks credibility with investors as well as with our citizens.

Governments' public debts and deficits are too high because their public sectors spend too much, get too little and their economies lack competitiveness. That is why immediate fiscal consolidation and structural reforms in highly indebted countries are of the essence. Not – as *The Economist* recently implied – because of a German penchant for Lutheran self-righteous rectitude, but because it is best for indebted countries and their long-term growth prospects.

Only material and immediate measures will regain lost credibility of highly indebted countries and demonstrate to markets and citizens alike that their governments mean what they said. Only when highly indebted governments stop living beyond their financial means and start lowering deficit and debt levels today investors and citizens can be convinced of the sustainability of debt and deficit levels tomorrow.

I am not deluding myself, however and neither should you: It will take not months but years, before these efforts will bear fruit. As regards the Euro area, given the time necessary to bring public deficits and debts down to sustainable levels, we will have to provide strictly conditional financial assistance to highly indebted and less competitive member countries. In essence we are buying those countries the time they need and shield them against the excessive volatility of financial markets so that they can put their public finances on a sustainable footing and improve their competitiveness. But such solidarity has its limits, it can only accompany a country's reform efforts, not replace them: A member state has to be willing to deal with the root causes of its problems itself.

I am convinced that, if we stick with our policy of fiscal and structural reforms, we will restore confidence and put the economies of the Euro area on a sustainable footing. We will prevent the debt crisis of some countries from becoming a crisis threatening the Euro area as a whole and in turn the world economy. And while – in the case of Greece – a further restructuring of debt might be necessary it is not a panacea. Without fiscal and structural reforms Greece's deficits and debts would reach unsustainable levels again.

Now, there are some, who are not satisfied by the way European politicians are dealing with the crises; who are now calling for the supposed structural faults in the European Monetary Union to be corrected once and for all by building up the fiscal and political union. That is an approach that does not reflect the genesis of European integration. Europe moves forward one step at a time. And it will do so in future as well.

But there is time for small steps and there is a time for bold steps. And the time for bold steps is now. Governments in the Euro area need not just to commit to fiscal consolidation and improved competitiveness and governance, they have to deliver. And they will. We will strengthen economic and fiscal governance in the Eurozone by means of an enhanced Stability and Growth pact. Where this proves to be insufficient we will find ways and means to reconcile a member's fiscal and economic policies with his responsibility for the Eurozone's stability.

Ladies and gentlemen, to sum things up: To regain credibility with markets and citizens, immediate fiscal consolidation and structural reforms in highly indebted and non-competitive countries are of the essence, even as the returns on that investment are one, perhaps two election cycles away. But markets too often react too late, too suddenly and too violently, and when they do so, they do not aid but hurt the real economy and our citizens. To curb these aberrations, financial market policies have to increase the transparency and reduce the excessive short-term volatility and inordinate leverage in financial markets in turn leading to sustainable growth of the real economy and contributing to European prosperity and global stability in the process.

Thank you very much.

Robin Niblett:

Thank you very much Dr Schauble. Thank you for those remarks. I'm sure we will have a lot of questions here around the room, and I'll turn to people in a second. While you're gathering your thoughts let me just quickly pick up some of the main points I think I heard you make there.

This interesting idea that at the beginning financial market regulation is going to require a relative, a relative at least, strengthening of the state compared to the past. As you said, not going all the way against markets but a strengthening of the state. You laid out the financial transactions tax as a potential example of that strengthening, regulating shadow banking systems, anything that will prevent a continuation of, as you said, credit fuelled growth, which is not sustainable.

But as you also noted, there is a political side to this and you had this phrase that was quite good: 'Politics may be at its wit's end'. Your view clearly is that you cannot spend your way out of the crisis. I think your comparison of where the United States is as compared to some European countries I think may be something people want to return here, with that stuck perhaps in US unemployment at a higher rate which you said may be linked to this idea of short term loosening with the promise or the threat of medium term tightening.

And then a little maybe throw away at the end of your presentation, but I'm sure it will capture quite a bit of our discussion, your comments about the need for some greater fiscal discipline and maybe fiscal union within the European Union or the European member-states within the Eurozone in particular.

As you said, time for small steps and bold steps, today may be bold steps. And in particular this idea of an enhanced Stability and Growth Pact, which again we can come to in a minute.

So let me see if I can draw in some questions around the room and I will return to one or two others if I need to. I've got a couple of points I want to make sure we don't miss myself.

Question 1:

You've described the financial transactions tax, opposition to it as parochial. Many would argue that a European based financial transactions tax would itself be parochial. What evidence do you have that the derivatives business will not just move to markets outside the Euro area? In particular Asia.

Question 2:

I would like to ask Dr Schauble if we have a financial transactions tax, in an era of free capital movements, and it's imposed only on some countries, would you would expect to happen.

Wolfgang Schauble:

I think it's always a problem if you make tax regulations and you think about how can you fight evasion. And if you count as your outcome, unless you have it in all places of the world set in place, you will not do it. You will never get any result.

I'll give an example. UK and Germany negotiated in parallel with Switzerland on the taxation of some income. Of course, there was an argument even from our partners in Switzerland: 'Oh, if we make a treaty with UK and with

Germany on this, then it will move to Singapore,' or somewhere else in the world. Nevertheless we got it. If there's a long way to go, you have to start. If you wait until everyone will have it, you will never get it. Firstly.

Next point is, if you look at... I started my professional career as a lawyer in tax matters. If you think about how is a system for taxation, you always need taxes for all what government has to do. People don't like it, but of course you have to pay taxes.

If you look in the system, what do we take as a basis for taxation? Normally we take income and normally we take transactions. It's the normal way, it's a value added tax. We take on all transactions. There's one, there's one, you it's the exception, the financial services. Why? There's no answer.

There's systematic and there is not. The only answer is of course it's even more volatile, you can evade. Therefore I would always be in favour to get a global agreement. Therefore we try to get it in the G20. Until now we didn't get it. Now we try to get it in Europe. I hope we will get it. I am not quite sure. I know we have 27 member-states and opinions are different.

If not, we will look about whether we will do it in the Eurozone, but in a common currency you can do it even as a minimum, unity you can't do it. I would prefer to do it in Europe. But I would offer a bit.

If we would introduce it in Europe – all Europe, European Union – it wouldn't take a long time until United States entered into it themselves. Because the pressure of people is increasing. Look at the demonstrations. Don't think that will stop. I am quite convinced it will not stop.

And the question will be even for our way of democracy, whether politics, democratic, authorised political decision-makers – governments, parliaments, who else – whether they will be able to rule or whether they are reigned only by markets.

By the way, if you think about taxation, you always have to have in mind not to make the wrong incentives. If you make a system of taxation in a way that it is much better to make profits in financial services than in any other way of business making and real economy. You can see the outcome. You can see the outcome. If you think about the right incentives for a balanced economy, you need modern services, of course. But if you rely too much, concentrate only on a special kind of services, you create a dependency which creates you a lot of problems.

If you look at the United States' problems, I will tell you I am totally convinced that we Europeans need a strong United States. Any problem in the United

States is not in our interests. I am very worried about what's going on in the United States; [inaudible] a lot of last October… Federal Reserve spent about 600 billion dollars. The outcome was poor in the labour market and in economic terms. It's the very reason you can find it.

Therefore, my answer is let's start in Europe. We in Europe can go, in some ways we go ahead in history. It's not the first case that Europe is going ahead. And if it sees the advantages, we never doubted in Europe to go ahead in the global world. But in that way I think it's an argument not to decide. And I would argue we should think about, if we go ahead I tell you, a lot of other parts of the world economy will follow us in the short term.

Robin Niblett:

Can I tack on the end of that point you made, and we talked here about parochialism and not waiting for others to do things and taking your own steps. What do you think, what does the German Finance Ministry think of the UK Vickers Report?

If the priority is to reduce volatility, to perhaps reduce excess profits, to avoid a dependency on a financial sector, the UK is taking some pretty bold steps in terms of separating out investment and retail actions in UK banks: Is that something that Germany is going to be supporting as well in its own country?

Wolfgang Schauble:

We are working on common decisions to fight volatility with other instruments as well. The financial transaction tax is far away the only instrument to solve the problem, it's quite clear. If you would only rely on a financial transaction tax, that would not be sufficient.

We have had different systems in our banking system. In Germany, we have a very specific situation of the financial sector with a huge number of small savings banks and mutual co-operatives that are small. In any small city, even village, you have such a savings bank and so on. And they have a lot of, huge participation of the retail market.

And therefore we have a few big banks and global players and even Joe Hagerman is always saying in Germany, it's the only global player and it's a poor, a little global player, the Deutsche Bank, and it's not sufficient for the German economy. Okay, maybe.

But if we come to regulation and we have the system that banks were allowed to do all kind of business but in a very specific German way – by the way, if we look what has to be done, I think the most important thing is to have regulation and transparency on all participants. Not only of the financial institutions in the real system, but all shadow banking must be transparent and regulated.

Maybe you can find a regulation to say in financial institutions are not allowed to give loans to shadow banking and that you have to regulate or to make transparency for all innovative products. And by the way, maybe you know, last year Germany in an isolated national decision, we forbid by law the naked short selling. We were hugely, very much criticised by our partners in Europe. Some of them followed us, and now they are trying to ban all short selling.

When I had to take the decision on the naked short selling, my decision was, what is the real economic sense of this, of the instrument? And what is the possibility for abuse? My judgement was the potential for abuse was much higher than the real economic sense, therefore I took this decision.

Question 3:

Dr Schauble, in 1997, I went with a committee to Frankfurt to hold discussions with Mr Pohl, President of the Bundesbank. At the time, he was very concerned about the subsidies that your federal government was paying to integrate the East. In the process of this I laughed and I said, ‘Wait until you join the Euro.’ At which point he said, ‘In no way will Germany responsibly join a Euro.’ And I said, ‘Well have you told Mr Helmut Kohl that?’ and he said, ‘On many occasions.’ He then proceeded to tell us what was likely to happen, and quite frankly with the hindsight we all now have, I realise he was totally prophetic.

I wonder if you would care to comment on who was right – Helmut Kohl, who for political reasons took Germany into the Euro and therefore created the foundation for this total disaster that the continent faces? And would you also perhaps tell the meeting here when you expect the German people and their representatives in the Bundestag to say ‘enough is enough’ of their taxpayers' money going to subsidise southern Europe.

Wolfgang Schauble:

You will not be surprised of my answer. I have seen a lot of things in my life, since I have been a member of parliament since... a long time. I have been member of Kohl Government in the 80s. And I negotiated twice with the GDR. I was responsible from '84 to '89 for the negotiations between Federal government of Germany with the government of Honecker of the GDR. And then I was responsible for the negotiations with the free elected government of the GDR under German reunification. Therefore, I know a lot of things.

And I tell you, Pohl was against the introduction of the German Deutsche Mark to the 1 July [inaudible], especially to the rate we introduced it. And I tell you if Kohl had not decided to do so, maybe you would still enjoy the Cold War and the division between East and West in Europe and the Iron Wall which was created by Winston Churchill, the Iron Curtain. Therefore I think we were right and Pohl was wrong. Pohl was wrong. First answer.

Now it's the Euro. But there's a relation between it was... and the relation is quite easy. If you ask any statistic, who takes the most advantage from the common European currency, it's Germany. It's the German economy. You have to know it. It's sorry for UK, you have not the advantages.

Of course you are right, a lot of my fellow citizens are not happy on this. But one of the problems is, and you have to know it, since we are human beings it's in human history all the time, what you have, what you undisputedly have is not as important compared to what you miss. Therefore if I tell, in a speech in Germany, ‘Oh, we have such huge advantages from this common European currency! It makes us strong, we have...’

Oh, well. Why should we waste our money for Greece? If I tell you you can't have the one without the other. It's difficult to explain but it's the truth. Therefore I am totally convinced that it was the right decision. Maybe it would have been better if we would get more political union in the 90s. German government at that time, I was part of this, was arguing for this, working for this. We didn't get it. We were not as much supposed from UK as we wanted to be, but nevertheless, okay.

Now it's time, because we have seen for ten years, the European currency has been well done, stable currency. The internal value and the external value of the European currency is quite good, about the British Pound... I forgot it. But if you look at the real figures, it's a success story. The European currency is a success story.

But of course, the structure is weak. And now the structure is questioned and disputed and we have now to build a better political structure from office to policy, because the problem about this new in history, we said we'd build a common currency without a common fiscal policy.

And now we have to build some... and now we will get it, ten years before we would never have got it. But if you wait, it's the same with financial taxation. If you wait until you have all, you never will get something. You have to start and then you go on – that's the very principle we made the process of European integration in the very beginning.

I tell you, in the early 50s, we tried, the founding fathers and founding mothers of European integration... yeah of course, you have to be politically correct. Be careful. They wanted to build a political union. We failed in the French Assemblee Nationale, 45. And the decision was, let's go on economic integration.

And of course, in the expectations of political integration will come up, step by step. That's the way we built integration. And in this way, we have a lot of problems. In the daily work, bureaucracy and it's really awful.

But, compared with other parts of our history, it's... yes, of course. It's a real success story. We could overcome the Cold War. Didn't you have any idea in the 70s and 80s how to overcome? We did it! Without European integration we never would have got it. So in the world of globalisation, I'm totally convinced we have to go on in European integration.

And of course, we will always ask for all in Europe, because of course we respect the decision of any nation, this is quite clear. We will not widen the gap between 17 and 27, of course. Never. But now we have to do what we have to do in our responsibility, for the world economy, for even the economy in UK in our Euro area. But we are convinced that we have to go forward and not back.

Question 4:

I'm very interested in what you just said, that you couldn't have got the kind of integrated Europe that you might have wanted to have a few years ago. Now you can get it because the case has been made. Some would say, you've got the next week to get it. That to convince the markets that there is a real commitment behind the Eurozone in this crisis, everyone knows there has to be German support for whatever the solution is on Sunday.

And to get that support, you have to have a commitment to a vision of a kind of fiscal policy which some people worry is not consistent with decent economic growth in the Eurozone over the next few years. You discussed this in your speech, but I think if you could address the concern that the kind of solidarity, the kind of fiscal union or more integrated Europe that Germany is now in a position to obtain, in return for the solidarity at times of crisis, is not consistent with decent economic growth. At least in the next few years.

The rebalancing, the retrenching, is only one direction. It is only by the countries on the periphery, and as you know we're not just talking about the public sector rebalancing, it's private sector imbalances in those countries too. And many economists just look at this and see what's on the other side. Where does the demand come from?

Wolfgang Schauble:

I think maybe we disagree in the fundamental question whether we can solve the short term problems by instruments which we say they are wrong in the medium term. And that's what I tried to figure out in my introduction remarks.

And if you look at the experience the United States has to suffer actually in the last couple of years, and to now, you see we are... When I started as finance minister two years ago, and when we tried to reduce our huge deficit – we have huge deficits in Germany as well – our deficit is about, oh about 80 percent of GDP, it's not so that we are below 10 percent, about 80 percent.

I was hugely criticised and questioned by a lot of, even by my very friend Christine Lagarde, French Finance Minister: ‘Oh, you are destroying growth!’ Tim Geithner came over to Germany last year and said, ‘Oh, you Germans with your theory and your thinking,’ and so on, economists, you have written this. And I said, ‘No, we will deliver. It's a possibility for growth, for deficit reduction.’ And when Tim Geithner came over this year in June to Berlin, that oh, we will try to make your fiscal policy a little bit more German like, because we have better growth figures than the average in the Eurozone and even than UK, including our policy of deficit reduction.

My conviction is, my veritable conviction is that one of the reasons why we better overcome the crisis we suffered the last years, and I told you the figure from 2009, 5.1 minus in GDP. It's not a joke. The very reason is we built confidence by investors and consumers in Germany. Maybe it's different in other nations. German people, if they lose confidence, they don't spend money. Neither for investments, neither for consumption. Therefore, they built confidence, it's the better way to get...

Of course we need, and we are ready to help the periphery countries to get growth. I would be in favour that the European Commission proves its efficiency in concentrating in developing for growth and infrastructure and all that. There's a lot of ideas you can make. We are ready to do whatever is possible to help and to regain competitiveness. Of course, they need structural reforms.

I tell you another story. Without some pressure, you will not get the necessary political decisions. In the 90s, when we started to build the European currency, it was much discussion in Italy because there were a lot of people who were... And Italy was a little bit a problem with the figures needed to be a member of the Eurozone from the very beginning.

To join the Euro from the very beginning, Italy took a political leadership in that time and they reduced their deficit in a way no one had expected. Sometimes you need pressure to get political decisions. It's in Germany no difference. Therefore my answer is of course we have to look and to give solidarity. We have not to neglect our responsibility for growth, but even if you think in growth in a global way, don't forget we have a total different demography in Europe compared to other continents.

Therefore a globally sustainable growth, we have to make clear that we need not figures like other continents need, urgently need to close the gaps, the global gap, because we will not succeed in closing the global gap. We will be very sorry on what we celebrated with the Arab spring, for example.

Question 5:

European leaders promised a comprehensive plan at the beginning of this year. And it was presented in February and March and it proved to be a damp squib. And then in July, they also held an emergency summit that was supposed to deal with Greece, that unravelled from the word go. And now you're saying that there will be bold steps taken this weekend.

How can you convince sceptical observers of this process that you will really come up with bold steps? That will in particular deal with Greece, and also quarantine the effects of some sort of default on the rest of the Euro area?

Question 6:

You made a comment I think a lot of people would agree with wherever they stand on the Euro, that the lesson from the last crisis is that highly cyclical credit fuelled growth does more harm than good. You seemed to be blaming both the borrowers and the intermediaries when you made that comment. What role do you think there was for the creditors, the people who had the money and supplied that credit in responsibility for the crisis? And as the largest creditor in the Eurozone, what responsibility does it now play on you to help solve it?

Wolfgang Schauble:

I just wanted to answer these questions with the answer by dates, not by promises. But what we need is we need, I think, first of all we need for systemic banks all over Europe, in the Euro 27, enough capital. That's what we are doing and I will get, I think we will get a decision from the European authority.

Second, we have to use the enhanced EFSF in a flexible way and in the most efficient way. I think we will get it. It's not... the room to manoeuvre is limited, but we will use the manoeuvre room. Then we will need a solution for Greece which could be understood as sustainable. It will take a lot of time for Greece, but we have a... we are waiting on the Troika Report to give the official answer, the official reaction.

And as soon as we have the report from the Troika mission, we will look at what they say to the sustainability. And then we will see what we is needed for a new programme. But a new programme for Greece is needed with some kind of reduction... and we will see what.

And then, of course I think member states which are not in programme, in programme we are actually as Ireland and Portugal. And for Greece we have a special programme with loans from the other Eurozone member-states. But we have two other member-states which are a little bit in the centre of some diversity in financial markets, I forgot which member-states these are. But these member-states should announce, in a credible way announce the necessity for deficit reduction. Especially in some member-states for structural reforms to enhance competitiveness and economic growth.

And the fifth point is we need a better governance for the Eurozone and that will include the necessity of many changes, especially relating to the Article 1 of the Lisbon Treaty which is related only for members of the Eurozone, because we were not asked for UK to do things that UK does not like to do actually. It's a pity, but we have to be respected.

Robin Niblett:

And the role of creditors? Intermediaries must reform, debtors must reform: what are the creditor countries doing to contribute here to the change?

Wolfgang Schauble:

Creditor country, who is a creditor country? We are not. Our debt is about... The issue of imbalances. No, I don't think that makes really sense. What we are always saying is as long as a surplus is related to competition, and not to any other measure, you must not punish. If you rely on competition, you must not punish the successful. Otherwise you should create another system.

I know the argument where a deficit has to be a surplus, otherwise there is no deficit, but my answer is, as long as we have competition, we should enhance and rely on competition and not punish whichever. We accept it to come to a solution with the European Parliament in the dialogue in the so-called ‘six pack’, but it's totally clear there is no symmetry between deficit and surplus.

Robin Niblett:

But as you said, you're competitive because you're inside the Eurozone. In a way, you're all the more competitive because a country like Greece maybe isn't. And it's inside the Eurozone. So your competitiveness, does it have an element of artificiality to it?

Wolfgang Schauble:

No, I don't think so. I think the level of competitiveness in Greece is not a consequence of its membership in the Eurozone. That's not true. Of course if Greece would not be a member in the Eurozone, they would have the instrument of devaluation. But I think every member-state who joined the Eurozone took the decision at the time to increase its competitiveness. That is the very story of the German reunification from 1990.

If you have a stable currency which is convertible, the pressure on your competitiveness is totally different. But if you want to be successful in the globalised world you have to be competitive and therefore it's better to join for Greece, not for UK. It's up to your decision. You don't need it. But some member-states decided to become members of the Eurozone because they wanted to get more pressure for competitiveness. And to give up would mean that they will not try to become competitive. That would be a very wrong sign.