BANCO DE **ESPAÑA**
Eurosistema

Communication

11 February 2024

Interview with the Governor published in the Cypriot newspaper Politis

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I would like to start with a frequently asked question: When can we expect a rate cut?

Right now, more important than calendar-based guidance, is understanding under what circumstances a rate cut would be warranted. In this regard, it is important to acknowledge that the disinflationary process in the euro area is now well advanced. This process is expected to continue in the coming quarters, with the latest Eurosystem projections seeing inflation easing to around our 2% objective in 2025 and 2026. And our confidence in the staff projections has increased notably, since the forecast errors have been very small and even negative in recent quarters, meaning that inflation figures have been somewhat below projections. Monetary policy continues to be strongly passed through to financing conditions and is dampening demand, with the risks to the growth outlook remaining tilted to the downside. All in all, we are now more confident that the next interest rate movement will be a cut. In any case, given the high level of uncertainty, our decisions will continue to be based on the data and in particular on our assessment of the inflation outlook, the dynamics of underlying inflation and the strength of monetary policy transmission. In March we will have more information available including, in particular, a new comprehensive macroeconomic projection exercise. The projections will be key to assessing, first, whether we can be sufficiently confident that our 2% medium-term target will be achieved, taking into account the associated risks, and second, the rate path that is compatible with reaching our symmetric target.

Uncertainty is becoming the new normal. How much more difficult is it going to make monetary policy-making?

Monetary policy under uncertainty is a classic question that has two standard –although opposite- theoretical responses: On the one hand, the Brainard attenuation principle suggests that policy should exhibit conservatism in the face of uncertainty. On the other, robust control theory states that if shocks are persistent and second-round effects materialise it pays to be more aggressive to keep longer-term expectations well-anchored. My own practical synthesis based on recent experience is that: there is no general rule requiring monetary policy to be either attenuated or more activist in contexts of uncertainty; monetary policy should not be paralysed in the face of uncertainty as central banks need to remain pre-emptive and forward looking; and risk management approaches become crucial and entail pragmatism and judgement. All this can be boiled down into our current data-dependent approach.

There have been recession scenarios in the euro area that have not materialised. Do we finally have more resilient economies? Are we in a position to deal with a new crisis?

Comparing the state of the European economy now and just before the Great Financial Crisis, we have, on the plus side, improvements in the EU economic and financial architecture, including procedures for macroeconomic imbalances, the upcoming new fiscal rules, advances in the banking union and the capital markets union; solid implementation by all EU banks of the new global prudential regulations stemming from Basel III, including the application of the macroprudential tools; and, crucially, the political and technical capacity to react promptly to shocks, as exemplified by the coordinated national fiscal responses to the COVID-19 and energy crises, and the setting up of the NGEU funds.
On the minus side, we see (a) fiscal vulnerabilities in many parts of the EU have increased, leaving less policy space to react to new shocks or to finance public goods or structural investment needs; (b) the structural reform agenda and the deepening of the single market have been lagging behind, resulting in slowing productivity gains, in comparison with other economic areas; (c) and we lack a much needed central fiscal capacity, sufficient progress towards a capital markets union and a fully mutualised European deposit insurance scheme, which would together boost both public and market confidence and also contribute to greater risk-sharing in the euro area, thereby helping to reduce potential fragmentation episodes.
All in all, I think we are better prepared because we have learned from experience, but clearly much more can be achieved both with national and European policies to provide more prosperity to citizens and resilience to our economies.

The Spanish economy could be described as an economy in miniature for the euro area. Based on your experience in Spain, what should we expect for the euro area?

Against a backdrop of weaker global and euro area activity, in 2023 the Spanish economy showed notable resilience compared with other European economies, owing, in particular, to a sectoral composition more geared towards services – in particular, tourism, which has remained very buoyant - and less trade exposure to China (whose recent deceleration is one of the main factors behind the global economic slowdown) than in the other euro area economies. The Spanish economy has also benefited from significant population growth, driven entirely by immigration flows.

As regards the euro area, despite short-term weakness, Eurosystem staff projections in December saw growth picking up to 0.8 per cent for 2024, and to 1.5 per cent for both 2025 and 2026. The projected gradual road to recovery would rely above all on private consumption, buoyed by the rise in households' real disposable income in an environment of rising wages and falling inflation. External demand is also expected to perform positively, although its contribution to growth will be limited by euro area exports' loss of market share. However, uncertainty remains high and the risks to economic growth remain tilted to the downside. In particular, the war in Ukraine and the tragic conflict in the Middle East are key sources of geopolitical risk.

Spain and Cyprus experienced a severe banking crisis in 2012-13 and needed the financial support of the ESM. What is your assessment of the banking systems in both countries today?

I think it is abundantly clear that the international financial reforms implemented over the past decade have given rise to a healthier, more capitalised banking sector that is more resilient to various types of shock. In Spain, these reforms also came in tandem with a programme of far-reaching restructuring in the sector. And indeed, the Spanish banking sector has shown notable resilience to the various extraordinary shocks of recent years, allowing profitability, solvency and credit quality to actually improve. And this has also been the case for the banking sector in Cyprus, where I would like to underline the role of the Bank of Cyprus under the leadership of Governor Constantinos Herodotou.

In any event, as I said earlier, uncertainty over the economic outlook remains high. It is therefore crucial that financial institutions deploy prudent provisioning and capital planning policies, to ensure that part of the observed increase in their profits is used to bolster their resilience, leaving them better placed to bear any losses, should the worst-case risk scenarios arise. And we must not forget that the short and medium-term challenges resulting from the recent period of extraordinary crises do not make tackling the banking sector's structural challenges – such as those linked to the management of climate-related risks, digitalisation and growing competition from technology firms – any less urgent.

You are chairman of the Basel Committee, a forum for formulating common global rules for banks. The implementation of Basel III is underway. We are facing new challenges: climate change, digital transformation and the onslaught of artificial intelligence. New risks are emerging. Do we need a "Basel 4"?

The key priority at the global level is full implementation of Basel III, as consistently and as soon as possible. That is the only way we can address the fault lines detected as a result of the GFC. Nonetheless, new risks may emerge and there are structural challenges that the Basel Committee needs to continue monitoring and addressing as necessary. For example, some traditional risks such as liquidity risk may interact with, and be reinforced by, structural trends deriving from digitalisation and social media. However, the appearance of new challenges should not prompt us to jump to the conclusion that a full overhaul of the Basel framework is needed. Sometimes the solution is already within the already available toolkit of regulatory, supervisory and managerial tools. Robust evaluation of already implemented reforms is needed to identify whether there are gaps in our framework.

At the recent World Economic Forum in Davos, you proposed the idea of a "Basel Committee" as a model for regulating artificial intelligence through the adoption of common global rules. Is your proposal being followed up?

The point here is that there is a clear need for more international cooperation in the domain of AI. At the same time, we are seeing some fault lines in the multilateral order based on rules in many dimensions. Despite this, in my view, the international cooperation in the financial domain is not suffering as a result. Quite the contrary, it has been strengthened so far as a consequence of the pandemic and heightened geopolitical risks. I think we can all benefit if we leverage on this experience in other areas where clear global public goods are at stake.