

**Committee on Economic and Monetary Affairs
of the European Parliament**

**Introductory Statement
by Mr. Lucas Papademos
candidate for Vice-President of the ECB**

Brussels, 22 April 2002

It is a great pleasure for me to appear before your Committee for this hearing which is part of the process of my nomination to the Vice-Presidency of the European Central Bank. I am extremely honored to have been proposed by the EU Council for this position.

In my introductory statement, I will first focus on the objectives and the role of the ECB. Then, I will address a number of issues and principles relating to the conduct of monetary policy, including its communication and accountability.

The Treaty clearly states that the primary objective of the ECB is to maintain price stability in the euro area. The unambiguous priority given by the Treaty to this objective partly reflects the inflation experience during the previous decades and the economic and social benefits that price stability entails. These benefits are appreciated by the European public, which at times has suffered the consequences of inflation, including the costs of restoring stability lost as a result of misguided policies. The assignment of price stability as the primary objective of the ECB also relates to the fundamental role of monetary factors in determining the price level in the long run. Monetary policy conducted by an independent central bank can effectively provide a nominal anchor to pin down the price level.

Price stability is not, of course, the only important economic policy objective. Attaining sustainable and non-inflationary growth and a high level of employment are other important goals. The ECB is required to support the general economic policies in the Community with a view to contributing to the achievement of these goals, provided that price stability is not jeopardized. In my view, the maintenance of price stability and the attainment of sustainable growth and high employment are not conflicting but complementary objectives in the long run and, in general, over the medium term as well. The monetary policy strategy of the ECB takes into account both parts of the ECB's mandate and contributes to the achievement of the real economic goals of the Community.

Let me briefly elaborate on the previous two statements. There is broad consensus that maintaining price stability contributes, through a variety of channels, to establishing conditions conducive to output and employment growth in the long run. In addition, it protects society from the arbitrary redistribution of income and wealth resulting from unanticipated inflation, thus fostering social cohesion. But, maintaining price stability over the medium term can also help, in general, to limit undesirable output and employment volatility. The contribution of monetary policy in stabilising output and employment fluctuations over the medium term depends on features of the central bank's strategy as well as on the credibility of its commitment to price stability.

The ECB's monetary policy strategy with its forward-looking, medium-term orientation and its quantitative definition of price stability contributes to the stabilisation of output and employment in various ways. Monetary policy decisions do take into account the evolution of output and other real variables in assessing inflation prospects. The medium-term orientation implies a gradual response to certain shocks, particularly on the supply side, to avoid inducing undesirable large output fluctuations. And the definition of price stability helps anchor expectations, influencing favourably short-term inflation – output dynamics.

Thus, monetary policy can contribute to the attainment of the Treaty's wider objectives in parallel with the pursuit of its primary goal, in the long run and over the medium term. Monetary policy, however, can not influence directly potential growth and long-term employment creation. The bulk of empirical evidence supports the theoretical proposition that money is “neutral” in the long run. Sustainable output and employment growth can be effectively pursued by policy measures and reforms which increase productivity and improve the functioning of labour and product markets. Improved productivity and labour market efficiency in the euro area will also enhance the effectiveness of monetary policy in achieving its primary objective and will reduce output volatility.

The effective pursuit and maintenance of price stability requires that the ECB should be fully independent in its decision-making. Independence is essential for safeguarding monetary policy from political pressures to focus excessively on the short-run economic situation. It is also required in order to fend off requests to focus on objectives that monetary policy cannot effectively achieve or to accommodate the undesirable side-effects of other policies on financial and product markets. Moreover, in a monetary union, independence also shields the central bank from national pressures in its conduct of the single monetary policy which aims at ensuring price stability in the euro area as a whole.

In all these cases, interference would undermine the central bank's medium-term orientation and its ability to maintain long-term price stability. For all these reasons and because the empirical evidence clearly shows that there is a positive correlation between the degree of central bank independence and the effectiveness of monetary policy in securing low inflation, the ECB's independence was enshrined in the Treaty. The European Parliament, in particular, has advocated and supported the independence of the ECB. Like all other members of the decision-making bodies of the ECB, I am committed to act in accordance with this important principle.

Independence does not imply that the ECB is not accountable for its policy decisions. On the contrary, transparency about policy actions and accountability for its performance to the European citizens and their representatives in the European Parliament are necessary both for enhancing the effectiveness of monetary policy and for legitimising the ECB's independence. Moreover, a fruitful dialogue between the ECB and all relevant economic policy-making bodies and institutions of the Union (e.g. the Commission and the Eurogroup) is also essential. An exchange of views and information between the ECB and other policy-making bodies about the economic situation and prospects and a better understanding of the fiscal and structural policies to be pursued in the Union provide useful input for monetary policy decisions.

Transparency about policy decisions is a vital ingredient of monetary policy-making. By explaining and justifying policy decisions so that they are clearly understood by the public and the financial markets, we can influence the expectations of economic agents in a way which facilitates the transmission of policy effects and the attainment of policy goals. On the whole the ECB communicates actively and extensively, through a variety of channels, with the aim to ensure a high degree of transparency about its policies. It provides ample information for the assessment of its performance by the European public. Its accountability to the European Parliament involves not only presentation of various reports but also a continuous and active dialogue between this Committee, the President of the ECB and other members of the Board. I believe it is important to enhance this constructive dialogue.

Since its establishment the ECB has achieved a high degree of price stability in the euro area. This was accomplished in an environment marked by large supply shocks and high volatility in foreign exchange and financial markets. More recently, the ECB has succeeded in managing and coordinating the smooth changeover to the euro, a historically unique and complex undertaking. These achievements make us confident that the ECB will continue to meet its objectives and

perform its tasks efficiently in the future. In my new capacity I intend to use my professional experience and devote all my energy to the success of this effort.

In my introductory statement I have chosen not to speak in my native language so as to underline the supranational character of the ECB and to facilitate communication. I would like, however, to finish with a quote from Aristotle regarding the value of money. In his *Politics* (Book I, 1257 B10), he states: “Οτέ δε πάλιν λήρος είναι δοκεί το νόμισμα και νόμος παντάπασιν φύσει δ’ ουθέν, ότι μεταθεμένων τε των χρωμένων ουθενός άξιον, ούτε χρήσιμον προς ουθέν των αναγκαίων εστί και νομίματος πλουτών πολλάκις απορήσει της αναγκαίας τροφής”. This text can be freely translated as follows: “If those who employ a currency system choose to change the agreements upon which it is created, the currency ceases to have its value and although one could have plenty of money one could no longer use it to procure the necessities of life”. This quote shows that the value of money has been a major concern since ancient times. The overriding responsibility of the European Central Bank is to achieve its primary objective and secure the purchasing power of our single currency in the euro area. By doing so, it contributes in a fundamental way to the long-term growth of real incomes and employment and, more generally, to the social and economic welfare of the citizens of Europe.

Thank you very much for your attention.