

Event Transcript

Italy's Effect on the Global Economy Mario Monti, Prime Minister of Italy

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Transcript is unedited.

C. Fred Bergsten: I greatly appreciate the applause, thank you. It is a unique honor and privilege and personal pleasure to welcome Prime Minister Monti back to the podium of our Peterson Institute for International Economics. I think it's fair to say that a simple syllogism sets the stage for today's meeting. The future of the world economy depends critically on the outcome of the euro crisis. The outcome of the euro crisis depends very heavily on what happens in Italy, by far the most important country at the epicenter of those developments. And the outcome in Italy will turn decisively on the success of the new Italian government led by Prime Minister Monti, both in overcoming its financial difficulties and in setting the prospects for sustainable economic growth over the longer run.

I don't want to put too much pressure on our speaker by putting it that way, but he and everybody else knows that he, his government, and his policies are truly critical to Italy, Europe, and the global economic outlook.

And I believe it's also fair to say that no one could be in a better position to respond constructively and successfully to those challenges than Prime Minister Mario Monti. As European Union Commissioner for competition policy, we all remember how he displayed enormous and repeated rounds of courage. He took on Jack Welch and GE, he took on Bill Gates and Microsoft, he took on the Landesbanken, he even took on our good friend who hasn't yet arrived, Sergio Marchionne, who co-chairs the Council for the United States and Italy to which Mario has spoken many times, with whom we partner here and are delighted to work so closely.

I think it's also fair to say that as EU Commissioner, particularly in his period for competition policy, he forcefully displayed his devotion to economic competition as a response and solution to underlying economic and particularly growth difficulties. And we all know that's what Italy as a nation and Europe as a region now needs more than anything else. And so again, Mario Monti is the ideal leader.

In addition to all his enormous professional accomplishments, Mario Monti has been a great friend of our Peterson Institute and think tanks

more broadly. He has been a member of our Board of Directors for six years; he was the founding chairman of Bruegel, our partner and close friend institute in Brussels and he's the only person—he may not know this—he's the only person ever to have delivered the two big annual lectures that we have in lecture series here at the Institute.

And when he gave the second of those in 2006, his title was, “Does Europe have an economic future?” His response was an unequivocal yes, but he cautioned, “Only if Europe did several important things to keep its forward momentum toward integration going.” And he stressed in particular the need for structural economic reform.

Now, Prime Minister Monti is in the most important position possible to make that happen. It's therefore a truly great honor, privilege, and personal joy to host the Prime Minister and to introduce him to this distinguished audience.

Super Mario!

Mario Monti:

Thank you very much, Fred. It's really very touching and emotionally heavy for me to be here with so many friends and so trapped by Fred's syllogisms about the crisis, Italy, Europe, *et cetera, et cetera*. I didn't quite realize how tall an order Fred would have been able to put in front of me. I really want to underline how we all involved in policy observing or in policy making have been benefitting from the Peterson Institute's work and from Fred's leadership in this and also in other, broader contexts. So I think there could be no better place for me to share with a highly-qualified audience a few reflections on this time, the economic future of Italy and Europe.

As Fred mentioned, yes, I delivered a few words in 2006 on the topic, “Does Europe have an economic future?” And after all, Europe did have an economic future, but I think that many of the questions surrounding Europe then are still there today and of course, I feel the responsibility in my temporary and luckily enough sharply time-limited role as Prime Minister of Italy to give a contribution to the solution of those problems.

Everybody has in mind of course the Eurozone crisis. I think everybody should be aware and I think everybody in this room is aware, but not everybody in this country or in Italy or in Europe is aware of the fact that this has not been a crisis of the euro. The euro has continued to display very, very remarkable stability, solidity. It has not incurred in any of the two situations in which a currency shows its weakness in terms of domestic purchasing power and in terms of external—well, in terms of exchange rates so I think it is really remarkable that although there has been and partly there still is a banking and financial and fiscal crisis in

many states of the Eurozone, the euro has not been affected. I think this tells a lot about the structural, institutional and policy resilience of this very, very junior currency in terms of age in the global arena.

Now, just in the last few hours, we understand that substantial progress has been achieved in Greece in order to overcome the worst moments of the crisis and I don't want to prejudge anything about what the Euro Group and the relevant bodies will decide on this, but let me just step back for a moment. The Greece case was of course the most severe and extreme and limit case test than one might have imagined for the Eurozone and although we can easily point to the fact that much of what was set out for Greece as a program, in terms of budgetary consolidation, in terms of structure reforms and so on, may have come too late, may have come in insufficient doses relative to the requirements. I think one day, even the Greek case will be seen to be a proof of the value of introducing throughout Europe the culture of stability that invented in Germany, in post-war Germany, through the social market economy model, has been through the euro, through the budgetary constraints surrounding the euro has been spreading throughout Europe.

Certainly, a country like Italy has benefitted enormously in the mid- and late '90s from the pressures to get into the euro that have brought very, very important structural reforms at that time already and the most recent economic and political experience in Italy of which for strange reasons, I happen to be one of the components today, would not have been there if it had not been for the continuing pressures exercised by the framework of EU policy making and if I were a German citizen, I would be proud even looking at Greece of the fact that the most successful of all heavy engineering products of Germany, the euro, through its diffusion throughout Europe, has brought the principles of budgetary discipline of the market economy and the wall that to even the most peripheral and culturally less prone—least prone part of Europe. So I think that transformations that in other times would have required, I don't know, a generation are now being put in place I hope in a non-reversible way, but this remains to be seen in just a couple of years, and that is because of the strength of the cultural reference to the values of stability that the euro has allowed us all to share.

Now, of course, the Economic and Monetary Union was a rather daring construction but a jigsaw where some key pieces were missing when I last was here to deliver a few reflections in 2006. As we know, it was both an economic and political project that was meant to complete the European single market as I think I said on that evening here. The euro is meant to be the cherry on the cake of a single market, but many of the problems were coming from the fact that the cherry had been put in that position,

but the cake was not yet completely there, given the still very imperfect stage of European real economic integration.

Now, the institutional framework of the Economic and Monetary Union is being reset to tackle the flaws in its design and operation that the crisis brought to the light. Most crucially, tools to resolve the crisis have been established within the European financial stability fund—sorry, with the European financial stability fund and the future permanent European stability mechanism.

The rulebook of the Stability and Growth Pact has been updated and enriched with sharper rules. Can I interject here the notion that one of the main problems brought about by the euro area crisis has been the resumption of old stereotypes about allegedly inherent and unchangeable characters of different people, sometimes constructed on the mere basis of the latitude of their countries? And of course, it was the two originating forces of the Stability and Growth Pact, Germany and France, which broke down its credibility in 2003 when they didn't quite like to submit themselves to the enforcement procedures.

And Italy, although not violating itself the Stability and Growth Pact at that time, provided a complicity in all this because it was Italy in the Chair of the ECOFIN Council, that allowed the two large member states to break the rules and after all, it took from 2004 to 2012 to rebuild again a credible pact. And of course, that was made even more difficult by the fiscal indiscipline in the mean time intervened particularly in some southern countries but traveling on the wide open road created by the non-acceptance of the rules by Germany and France in 2003.

So, we all have a responsibility to build a better European integration and many, if not all, also have to share in the responsibility of having not always operated in the right direction. So I think European integration can be built. All the better, the more we are all modest in assessing our performance relative to that of the other.

The principles of budgetary discipline are now—will shortly be enshrined in national constitutions and the—all member states have committed to be near to a balanced budget by 2015.

So far, the main focus has been, as it had to be, on austerity and fiscal consolidation, yet structure reforms are as important as fiscal discipline for the long-term future of Europe and fiscal discipline rules and the commitment to sound public finances can help European Member States overcome the blocking powers of lobbies and special interests.

These vetoes hampered reform in the past and led to national abuse of the imperfection in institutional framework of the Economic and Monetary Union. But fiscal adjustment is not sufficient, definitely, and the interesting current stage of the policy game in Europe is precisely on how to put to rest the concentration of minds and policy energies on fiscal discipline, putting them to rest not because fiscal discipline will not have to be observed, but because by now, it has been really set in a very, very sophisticated constitutional framework both at EU and at the national level and all the enforcement instruments are there and all the political will to comply with them is there. So this is a very interesting moment for all of us to concentrate more on the growth imperatives.

Of course, how can growth be generated in Europe in a context of continued budgetary discipline? I think most of the extra growth will have to come maybe by coordinated macroeconomic policies at the G8, G20 level, but as far as the EU is concerned, mainly, it will have to come from structural reforms or supply side measures within Europe.

This means that we have now to really work on the cake to make the cake more similar to the optimum currency area that we see in the textbooks. Otherwise, the euro will never—although being a solid currency—will never deliver its potential in terms of economic growth and wellbeing. But in order to make the cake a real cake, we need to have a single market. Although we come out—I mean, relative to when we were here together, many of you and I in 2006—since then, the single market has been in crisis, not in further development.

Why? Because the backlash against integration or the integration fatigue that has been observed in many EU countries has put more and more in question the objective, the single. We have seen concerns in France concerning an army of Polish plumbers that apparently were ready to come to France and we've seen in many countries increasing resistances towards cross-border takeover bids and we have seen in many, many countries a growing economic nationalistic sentiment and all that.

So the single market has been less and less a wished-for development and more and more a resistance development. But even the noun, the market, has been somewhat in crisis because many in Europe, following the financial crisis, have been putting in question, intellectually and politically, the notion whether the market economy was after all the best vehicle to generate growth and employment. So, not an easy time for a single market, let alone for a global European economic policy which wanted to bet on a stronger single market.

But now, I think we are really at the moment where we have to work in that direction if we want to make growth a reality in Europe and as I

hinted already six years ago in this room, the paradox is that there are many countries within the Eurozone therefore—which live the life of the Monetary Union which however do not really do very seriously their job as regards to economic union. Because in many continental countries, large continental economies which are key to the Eurozone, we find less compliance with the rules of the single market of competition, market openness, than we find on the [inaudible 0:22:32] countries like the UK, Denmark, Sweden, Poland, and these are all countries which do not belong to the Eurozone but which are more compliant and more indeed intellectually in line with market principles.

This can perhaps explain why my government in Italy is investing a lot in of course making use of the fact of having been readmitted to the meetings with the heads of governments of Germany and France and to play with them in order to provide impulsion to EU processes. But we invest, I would say, more than either of these two in the relationship with the UK, with Poland—that is, with countries which although not belonging to the Eurozone or not yet belonging to Eurozone, can put pressure on us for us all to become a bit more of an economically-integrated real entity and real single market.

And I think it's really a pity, not because we proposed the thing, but because I think it would have been helpful if Prime Minister Cameron, on the occasion of the European Council on the 9th of December where he finally decided not to stay on board the Fiscal Compact agreement—he did not go down the road that we had suggested for Britain: namely, do ask for a price in order to stay on board the treaty which is politically painful for you to ratify at home, but please ask for an acceptable price like a stronger commitment on the part of the Eurozone countries to accept—which would have been in the interest of the UK and the other non-euro countries—a big movement forward with specific deadlines concerning the single market for energy, for services, *et cetera*. But please don't ask for conditions that we could only reject because they would be regressive relative to the process of integration like exactly what he asked for, namely the unanimity rule on any future decisions on financial regulation which we could not accept and was not accepted. But this is just an observation on the link between the policy cooperation lines that can be established within the EU and the different degree of adherence to the key elements of this composite set of countries, the fiscal discipline growth, the single market, *et cetera*.

Let me come to a conclusion by saying that if a country wants to be coherent, if it pushes at EU level, in order to see a concrete policy with deadlines which we hope we will get to in order to stimulate growth through more single market (among other things), then that country has to be coherent domestically and not only will have to comply with budgetary

rules, but will also have to be more insisting on structural reforms domestically so that it can have a market which can cope with the challenges of being in a more and more real single market.

These are the two lines—budgetary consolidation and more structural reforms—that our government is committed to in Italy. I kept the objective that my predecessor, Prime Minister Berlusconi, had set in agreement with the ECB and the European Commission and that was done last summer in a moment of extreme financial emergency for Italy. Only this, I believe, can explain the fact that the Italian government had accepted to balance the budget by 2013 which means a couple of years before the other member states. And after a very quick reflection, we decided to stick with that commitment, although some macroeconomists would contend that that was the optimal course, but I think from a political point of view in Europe, we would have lost any authority and ability to influence developments if we had presented ourselves first with a demand for more leniency.

So we put together quickly a package adopted by decree law and then quickly converted into law by the Parliament to achieve this balanced budget by 2013 which will imply, by the way, a 5.5% of GDP primary surplus, so net of interest payments which will be the highest in the euro area. And we have introduced by decree law something unheard of in Italian but also in other member states (most of them history of structural reforms through decree law) a structural reform of the pension system going into a fully contribution-based system and with the increase of the retirement age to 67 for men and women by 2017.

This was done by decree law with only three hours of general strike, which means that—no, no, no. I say this not to denote the weakness of the labor unions. They are not weak, but I wanted to stress the maturity of the Italian public opinion including the labor unions which accepted a major—I mean, President Sarkozy could not believe that we had, without people in the streets for weeks, done that structural reform and then we proceeded in the month of January to a package again by decree law, in order—and this should be the politically perhaps most difficult, but we will see in the next few weeks.

I think we will bring home the conversion into law by the Parliament with minimal changes to the package to really introduce much more competition and opening up in areas ranging from the liberal professions to a topic that one gentleman at one of the stables has been following very closely with a high degree of responsible awareness mixed with concern about the unbundling between the gas generation and the gas distribution systems so all things going in the direction of more competition and openness which I believe could only be done through a very strange

government like the present one which as many of you will know does not enjoy a structured majority of a coalition of parties but enjoys or has so far enjoyed the concomitant support in Parliament of parties which hardly speak to each other coming as they do from a highly belligerent past.

But they are supporting this effort. But of course, they support this effort only if whatever we do—budgetary consolidation or structural reform—is bold enough and politically costly enough because number one, these are the things that they admit they could not have been putting in place. And secondly, if a party from the right has to support a reform squeezing out some rants from the liberal professions which are in their constituencies, they will accept this only if we do a pension reform, for example, in the area which is more a constituency of the left with equal boldness.

So, there is a virtuous mechanism of distributing pains in a homogenous way which makes—which ensures that we maximize the number of people who are unhappy, but at the same time, we seem to have—for the time being—convinced the public opinion at large that these were necessary things and for reasons which I cannot really understand, the general trust of the government policy seems to be supported by a very high percentage of the public opinion which opens up, in my view, a very optimistic consideration about the Italians: namely, it's not that they resist being governed. They had a pent-up demand for governance. It was the political system that perhaps was a bit hesitant normally to supply that governance, that decision-making that after all the people were ready and maybe willing to see in place.

A final point, I think there is a continuity—I forgot; I don't want to give anybody the impression that we forget the labor reforms. This is the third big pillar so budgetary consolidation, liberalizations and competition, and labor reform. There, we cannot even—even we cannot and do not intend to proceed by decree law so there are negotiations going on. They will be concluded by the end of March, and they will—they are being oriented in the direction of reducing—this is something the IMF, the EU, the OECD have always recommended to Italy, reducing the segmentation of the labor market, reducing the uneven treatment between the insiders and the outsiders who cannot get in, mainly the young.

And also changing the nature of some social protection mechanisms so as to reduce a bit the distance between Italy and some Nordic countries in having more flex security, namely a closer compatibility between a labor market made more flexible and a modernized system of social protection centered on the individual worker, but not on the individual job, as was the case for so many decades.

Now, this, ladies and gentlemen, cannot be—of course, it cannot be an unbiased report that I am submitting to you because I'm certainly very, very biased. Although I, as well as my ministers—no, I could—I will say that I am dilettante like my ministers but we have with us here the Foreign Minister. No, we should have had the Foreign Minister, but he had a meeting at this time with the Secretary of State. Certain of the ministers are by no means dilettante but at any rate, most of us are, but we are putting together this strange experiment and we cannot say of course how the final results will be, but we do feel that without the exaggerations with which Fred Bergsten politely started these introductory words, without these exaggerations, but we feel that there is a link between the degree in which Italy succeeds in shifting from being a problem to being an element of a solution and I think we are rather advanced in that, but above all, the degree to which this experiment will prove successful in Italy and the degree to which Italy will be able to exercise influence on the overall course of EU policy making towards a compact for growth in a fiscally-compacted Europe and I feel—we feel that there is a great similarity of feeling of policy perspective between the US and the EU in this respect.

And this is an additional huge reason of interest and commitment on our part in being in Washington today and I hope that although I've been exceedingly long, Fred, there would be some time for us to be able to benefit from your and the other guests' critical remarks and suggestions.

Thank you very much.

C. Fred Bergsten: Thank you.

Question and Answer Session

C. Fred Bergsten: Well, Mr. Prime Minister, thank you enormously for that very encouraging outlook and report. We're all strongly supporting you, encouraging the success of what you've said and we're very heartened to hear your report.

Let me ask you to elaborate, maybe in a couple of areas. You have quite rightly, of course, stressed the need to go beyond fiscal austerity, to marry it with growth strategies. Tell us a little more about your growth strategy, both for Italy and for Europe. What is a reasonable expectation for resumed economic growth in Italy? Once the fiscal consolidation takes place, your structural reforms begin to take effect, what could we look for as a growth target for Italy over the coming medium term? And can you give us any estimates of the extent to which the reforms you are now putting in place might generate that growth? Any quantitative estimates or even guesstimates, on what kind of payoff from your policies?

And then at the European level, in your fascinating interview that was in the Wall Street Journal yesterday, you talked as you did some today about the need for Europe as a whole to adopt structural reform, including Germany. Elaborate a little bit thereto, what specifics do you have in mind, what are the priorities and what could be the payoff, in terms of a resumption of European growth within the next two or three years?

Mario Monti:

Yes, the prospect for growth in Italy the—well, first of all, growth in Italy will be necessary, not only for the sake of growth and the reduction of unemployment in themselves, but also in order to make the improved budgetary situations sustainable. And I think it's very interesting that since about one year, even the rating agencies are putting much more emphasis on growth as a necessary condition for budgetary sustainability.

Of course, we are not putting in place a strategy for growth from the demand side, but—what do I mean? That certainly we are not compensating the deteriorating estimates for real economic growth in Italy and elsewhere in 2012, by additional demand stimuli. Clearly, we are not doing this.

But I believe that if the markets see the improvements in the policy outlook for Italy and in the sustainability of the budget, they will deliver a benefit to Italy in the form of lower interest rates.

We have been plagued by a very high interest rate on medium and long-term treasury bonds much above—I mean, the spread between the 10-year treasury bonds and the bund, the German bonds, reached 574 basis points on November the 9th, the moment in which the political scenario changed in Italy and since has come down to the 344 of this morning which deserves two remarks. One, the coming down of short-term interest rates has been much more remarkable, much bigger, and this leads many people to believe that there are some political uncertainties that are keeping up the longer-term interest rates, linked to what might happen after the new elections in Italy.

But there, I would like to be a bit reassuring and one element, which goes in this direction, many of you will have seen it, is the interview that Mr. Berlusconi gave to the Financial Times last week, supporting more openly than ever before the current government and committing to this support over in the medium term. Now, everything can change, but I think this provides Italy with a perspective of stability in that particular political sector, where most people were seeing the potential source of instability.

At any rate, interest rates are coming down, more the short term than the longer term. I believe that if this Greece potential explosive gets out of the

way, this will—this process of declining interest rates will accelerate and hence I think, we carve out through what we did on the budget, a bit of a support for growth through lower interest rates on treasuries, but also indirectly on bank loans to companies.

And then there is the more supply side. We saw a work done by the OECD on structural reforms, one of their fields of specialty, but they did a specific work on the sort of liberalization measures that Italy has been now introducing. They come to—they and other studies of the Bank of Italy come to the conclusion that this opening up of markets could altogether generate a 10, 11 percent increase in productivity, half of which could be there in the first three years alone, so also relatively in the short term.

Then of course, we have to hope that the global and European policy stance becomes more growth generating, hence our efforts, vis-à-vis the European level. And I come here to your second part about structure reforms beyond Italy, structure reforms at the EU level including Germany.

Well, I think that there is a lot to be done in terms of structure reforms country by country, which is the responsibility of the various governments, but also in part under the leverages of the European Commission. For example, the fact that the European Commission has now opened infringement procedures that is putting legal and political stimulus on countries to comply with the services directive, liberalizing the services area, and they issued most recently two infringement procedures symbolically enough.

One vis-à-vis Germany, the other one, vis-à-vis Greece, says that even in Germany, there is scope for greater domestic liberalization. And something I normally try to convey to our Anglo-Saxon friends, there is not much hope to persuade Germany to play the growth game through a more Keynesian frame of mind, but I think they are more likely to respond positively if one calls them to fully go in the direction of their invention, the social market economy of the '50s and the '60s, open up markets.

And I believe that if Germany fully went to the opening up of its domestic services sector, that will stimulate its own growth, as well as through increased exports of services from other EU Member States to Germany, the whole of European growth.

But lastly, there are some policies at the EU level, not domestic structure reforms of Member States, but policies at the EU level, which have, in my view, to change in order to reflect this growth orientation, now that we are no longer an undisciplined continent, but actually the most virtuous in the world in terms of budgets.

That means in particular, much more resources devoted, many more resources devoted to the EU budget and to cross border infrastructures, for example. And although I happen to be also a Finance Minister, I will not buy the argument put forward by my colleagues, the Finance Ministers saying, “Okay, the EU puts a lot of pressures on us to contain the national budgets.” Certainly, we are not ready to have in the future a greater EU budget, but I think this makes no sense, because it is a matter of economies of scale and the provision of public goods, some of which can only be provided at the level of EU.

So, I think it will be important, but will imply a difficult change in mentality and we are working towards that, important that I—the whole of EU policy stance becomes more growth-oriented. And this will, in the end, also generate some demand expansion across Europe without which purely supply-side reforms will not in themselves generate growth.

C. Fred Bergsten: Let me ask you again to elaborate on a couple of the comments you just made about the evolution of Europe. You are now Prime Minister of Italy, but for a long time, you’ve been one of the architects of Europe. You’ve been on many commissions, you’ve written many reports about the future of Europe, not to mention your 10 years implementing Europe as a Commissioner.

As Europe works its way through the current crisis, what do you see as the medium to long run outlook for the European Union as a whole and for the future prospects of the integration exercise? Many of us have observed that Europe has faced many crises over its five or six decades; some were existential. Out of all those, Europe did seem to come out stronger and move forward; will that happen this time?

Mario Monti: I think this is happening this time already. We are moving, perhaps without being aware, towards some degree of even political union. The crisis has brought about an unexpected acceptance by national governments of a much greater coordination at the EU level of national budgetary policies.

Since last year, the so-called European Semester is in place. This means that each of our governments has to submit to the European Commission and to the European Council of Ministers, in the first half of the year before it goes to the National Parliament, a draft budget.

This is incredible if you think of it. This was asked by the European Commission for years and years and always rejected by Member States. Isn’t this a vulnus to the sovereignty of parliaments? Well, it may be a vulnus, but now it is in place, so this is one aspect.

Then the acceptance of a much-enhanced economic purveyance on even the process of structure reforms in Member States, so there is an acceptance of more operational instruments of supervision by the EU.

So, the—in itself, slow structure of the twenty or of the seventeen members of the Euro area, has moved considerably. “Thanks,” one should say, to the Greek crisis. And if I look in five years’ time, I would imagine a Euro area that would have a composition more numerous than the current one.

I don’t see honestly countries going out of the Euro. I see some countries coming in the Euro in the next few years. I believe that the permanent crisis management system, the ESM, which we will put in place soon, will be there as an ordinary instrument for crisis management. The EU was not constructed to manage crisis and it was a big deficiency and this crisis forced us to update the machinery.

I believe that we will see a shift in the competencies, as shift in the functions, what Brussels does relative to the Member States, with some areas moving up. For example, there is a slow process, which in my view will accelerate concerning tax coordination, a very sensitive topic, but it is going ahead. And so, tax policy will be slightly more centralized, but on the other hand, some policies which have been ran in Brussels for decades as if it were in an incubator, are now ready to be delivered in a network, in a governance through network system. This is the case of competition policy in 2004, which was gradually outsourced to the National Competition authorities, although keeping it Brussels coordination.

So, I would imagine a Europe, which will be not necessarily more cumbersome, but focusing on its core business. The core business of Europe will evolve over time, but the ability to respond to crisis, luckily enough, is still there. The worst-case scenario, of course, would be to have crisis and no ability to respond to them. The best-case scenario would be to have an ability to modernize your structures. Even without crisis, we are not so virtuous yet.

C. Fred Bergsten: I have one more question then I want to open it up. You met with the Congressional Leadership this morning; you’re going directly from here to the Whitehouse to meet with President Obama. What can the United States, the rest of the world more broadly, do to help you? And is there any specific role for the International Monetary Fund in coming back into the picture, as it did at the outset of the crisis, to help support the resumption of stability?

Mario Monti: This is a moment where the German Chancellor has for two months, very constructively asked me, “What can we do more for you?” And maybe this will also be the question by President Obama; and in fact, it did come up also in the meetings this morning with the Congressional Leadership.

I think Italy is not in a state where it needs financial support, but it needs better governance and it wants to contribute to better governance. This has largely to be achieved within Europe. For example, I think we came to a deep common understanding with Germany, that anything which should improve the perceptions by the markets; that the Eurozone is well governed, in terms of readiness, to put up adequate firewalls, will actually imply a very small probability that such financial resources would have to be used, because they will be credible enough for the mere fact that they are there.

With the US, I think—this will be the topic of my conversations in—I don’t know. I hope I will not be late to the White House.

C. Fred Bergsten: We’ll get you there on time.

Mario Monti: How, given the fact that the US is struggling to have budgetary consolidation as we call it and is oriented towards growth and we are doing exactly the same in a different institutional context; how we can develop synergies in order to do this more easily.

As to the IMF—well, there is a prominent figure of the IMF in this room. I would say that the IMF is playing a very key and constructive role. I think the IMF is right when it says, concerning crisis management and financial firewalls, “We cannot do more vis-à-vis Europe unless the Europeans give proof of believing in themselves enough and doing themselves what they can do in terms of firewalls.” I think this is a correct attitude.

Where I perhaps would see a room for improvements also on the part of the IMF, would be in having a broader understanding of specific situations in which the strict adherence to a model might prevent a pragmatic solution of a problem.

Now I don’t have the latest details about the agreement reached by the Troika with Prime Minister Papademos and of the agreement between him and the three political parties. But it is my understanding that many of us in Europe, including the Member States, which traditionally are on the side of caution and of discipline, believe that this is the moment to consider that, if there is a minimum of compliance with the requirements set out, this is a moment to turn the page and to extinguish this potential Greek explosion.

C. Fred Bergsten: Okay. The floor is open. We've got two standing mics at the back; we have a couple of traveling mics here. Please identify yourself and then fire away. Okay, we got a question at the back and one over here.

John Dizard: John Dizard, with the *Financial Times*. The Greek program will apparently include a retroactive collective action clause, in other words a retroactive rewriting of bond contracts. Won't this impose a risk for bondholders and therefore, a higher price for issuers of local-law bonds, such as Italy or any other current—any other deficit country? Isn't there a risk for issuers, aside from Greece, who will now have to pay more, because of the Greece's rewriting of contract law? Of course, it was originally denied by Greece and by the ECB that this would happen. Now that it has, how credible is the assertion that PSI will be confined just to Greece? In other words, isn't there a cost to the rest of the European issuers for this rewriting of bond contracts?

Mario Monti: Two things. One, I think at the highest political level, it has been clearly said that this role given to the PSI, after the meeting between Germany and France has caused a lot of problems and will not become a permanent feature of policies.

Secondly, don't you believe—I'm returning the question to you if I may—don't you believe that the risk of countries rewriting contracts was already largely incorporated in the markets and therefore in interest rates already? I happen to think that the answer would have to be yes.

So, I don't expect that this would worsen the position of the Italian Treasury in the market, whereas I do think that once this page is turned, the benefit will be considerable for every issuer and for the markets overall themselves.

C. Fred Bergsten: Next question over here. Nancy?

Nancy: Nancy [inaudible 0:26:01]. When you responded to Fred's question on the future of European integration, you didn't talk about the banking sector issues. And we now have the banking supervisor assessing the results of the stress test and determining what they think is needed. But in terms of getting those outcomes, it's up to the individual states to try to figure out what has to be done. And I wonder, and looking at the future, what you see is needed in terms of greater harmonization and strength of the central banking structure?

Mario Monti: Yeah, very important point, and I think many politicians in Europe thought our friend Tommaso Padoa-Schioppa, was too visionary when he was invoking a real EU-level supervisory structure. Then events proved that he was a visionary, but highly realistic and in fact Europe has

gradually moved towards that direction with the de Larosière report and the subsequent policy decisions.

But I think you're absolutely right, I should have mentioned this because in the area—I mean, the banking sector is illustrative of two things, one, that when I was saying earlier that there has been a disaffection for integration or a rejection of integration. Well, the European banking system until three, four, five years ago had undergone a very remarkable process of cross border integration.

Then, following the crisis, the wish to stay closer to father and mother has prevailed and the states, the treasuries being the source of rescue money, has induced banks to retrench, to some extent. And so there has been more fragmentation in the European banking system and that is also—well, part—that is, because two elements of the European construction are not pronounced enough yet.

One is that there is still big room for state aid, which is state aid, not EU-wide aid. And secondly, there is this ambivalent ambiguous situation where banking supervision is half-baked between the real EU-level and the national level, so thank you for raising this. Europe will not make a decisive forward step towards being an integrated single market with the appropriate policy instruments at the EU-level until this is remedied.

- C. Fred Bergsten: As the Prime Minister said, we have to be sure that he gets to the White House on time and he also has to have a bite of lunch. So, we have time only for two quick questions. The two at the head of a queue, ask your questions one right after the other and the Prime Minister can choose how to respond to the two.
- Mario Platero: Mr. Prime Minister, you described Germany.
- C. Fred Bergsten: Please identify.
- Mario Platero: Mario Platero, *Il Sole 24 Ore*. Mr. Prime Minister, you described Germany as being a social market economy. You said that the central government in Europe should become bigger. Don't you fear that your message may be taken in the wrong way within the Republican candidates? And more seriously, how do you respond to the constant allegations we here in the debate here, that Europe is a socialist country and America is moving in that direction?
- C. Fred Bergsten: Rick, go ahead and ask the second question, then respond. Then that will be it.

Rick: [Foreign 0:30:35] and thank you very much Prime Minister. My question is, again regarding Germany, but somewhat different. Germany has grown quite rapidly, but [inaudible 0:30:43] large current account surplus. Italy has grown relatively slowly and has quite a large current account deficit, around 3.5 percent of GDP. Is this a sign of major, major competitiveness loss of Italy, vis-à-vis Germany and vis-à-vis the rest of the world? And how does your plan, beyond structure reforms, which take a long time to work, actually deal with that problem?

Mario Monti: Yep, can I take the second question—

C. Fred Bergsten: Please do.

Mario Monti: —the second question first. Yes, the answer is unambiguously yes. And Italian entrepreneurs and top managers in this room, will probably confirm that Italy has accumulated a sizeable worsening of competitiveness. And that explains, to a large extent, why Italy for the last twelve or fifteen years, has had an average rate of growth, about one-half that of the Euro area, not of the BRICs, of the Euro area.

Structure reforms play only in the long term, yes and no, because as coming out of the Bank of Italy and OECD estimates I gave earlier, some effects of structure reforms can come up rather quickly. And I think the direction of policy has really to look at total factor productivity, as you economists would call it, which means that a lot of work has been done in the field of the labor market, in order to facilitate increases in productivity there and the closer relationship between rewards and productivity. But also, a lot has to be done by remedying to elements of lack of competitiveness, which are outside the firm; like in other “infrastructures” like huge bureaucratic burdens.

True, each of these can play out its effect only in the relatively long-term. But I think that international investors, the markets, are watching very closely, what each country does or does not in these areas. And I perceive a view of Italy in the international business community, as the view of a country, which has very, very strong fundamentals in many respects, which compare very well with those of other countries, particularly in Europe. I will not list them here, but they are prevented from generating actual growth, because of these constraints. And I believe that once the markets will be convinced that things will change and have started changing. I think they—and I hope, of course, that they will accelerate this process by moving in; like on treasury bonds. I’m not here to promote them. My Deputy Finance Minister is now in New York, working also towards that.

But given the current levels of, still high—five and a half percent rates on medium to long-term treasury bonds in Italy—if really one is perceived that Greece is moving outside of the problem area, and that this policy process in Italy is going to continue and to achieve its results. Well, many people tell me, once we reach this conviction there is a remarkable room out there for capital gains on Italian treasury bonds. So, I think something similar, not at that speed, could happen as to achieving, rather early on, the benefits from pro-competitiveness policies.

While German growth, the question—is this a lunch speech on Germany?

C. Fred Bergsten: No, it's not.

Mario Monti: I spoke already too much in Germany—about Germany, sorry. But the first question by, Mr. Platero, brings us inevitably to Germany again, I'm sorry. Did I describe the—well, if Europe has the model of a social market economy and if I say that there will be a heavier government in Brussels for Europe, how will this resonate, especially with the Republicans, in Congress and in the US? Mr. Platero is an eminent journalist, so he's more inclined to sharpening views, than in following sophisticated “ifs and buts.” But the social market economy, contains the market in it for many of our countries in Europe as they were before the full impact of social—of European integration.

What Europe really brings is a much more pro-market orientation. Most of our domestic liberalizations in the network industries and elsewhere have been achieved, because of Europe. So Europe has been a powerful factor for liberalizing the EU economy. And so, speaking about the social market economy, if done in the appropriate context is not underlining a socializing effect of European integration on the contrary.

Equally, for the government of Europe, I just said, “Mario, that some functions will have to go up to Brussels, others can be devolved from Brussels to the national capitals or indeed the regions.”

So no, I do not expect a heavier Brussels government, but it is true that the borderline between socialism and pro-market attitudes is very thin and mobile. I always remember a day in 2001, the previous day I was Commissioner for Competition in Brussels. The previous day, I had blocked the GE-Honeywell merger and rejected a French state aid to a company. And so I was described as parliosocialist in the US press and as a dangerous neoliberal in the French press.

C. Fred Bergsten: Mr. Prime Minister, we could obviously go on all day. We wish you the best of luck. We are with you, we support you, we hope and pray for your success; and we're welcoming you to the United States. Thank you.

Mario Monti: Thank you very much. I appreciate it.

C. Fred Bergsten: Fantastic, and I will get you some lunch.

