3 Macroprudential Policy: 'Humility' and 'Hope'

First annual ECB/IMF conference

On 26 and 27 April, the symposium jointly organised by the ECB and the IMF took place. It was aimed at bolstering an analytical framework, the understanding and the diffusion of macroprudential policy (MAPO), at analysing its current state of play and its way forward. The words 'humility' and 'hope' echoed throughout the two days.

It was widely recognised that MAPO remains at an early stage despite the significant growth in the number of measures applied in the EU in 2015 as compared with 2014 -this was also stressed in the ESRB's *Review of Macroprudential Policy in the EU in 2015*. There was consensus that MAPO is **a useful tool against systemic risks in the whole financial system**, and that it has to be used wisely. Thus, policy design has to be built on an adequate internalisation of negative externalities and on bolstering competitive advantages.

Humility. The clarification of three essential building blocks is still pending:

i) Optimum European governance: Some participants reiterated that the President of the ECB should be the driver of financial stability in Europe, and that the ECB should also be given the power to relax national MAPO measures, to correct the current asymmetry that only allows it to make them harsher where necessary. Others emphasised that European supervision is a diversified *body* and all of its pieces have to be considered – the ECB, ESRB, European Commission (EC) and the Member States (MS). A third view was that the MS should have primary responsibility, followed by the European institutions. Based on these heterogeneous opinions, communication, coordination and cooperation among all the parties might be the first best in the short term; and at the same time it is necessary to keep working towards simpler, single, common European supervision of financial stability.

The ECB released its first bi-annual Macroprudential Bulletin in March, emphasising that it is taking its responsibilities seriously via the SSM and advocates for leading European financial stability and fostering transparency.

ii) Whether MAPO and monetary policy (MP) should be used jointly or separately under normal conditions: MAPO and MP seem to be more complementary than substitutes. They might generally reinforce each other, because financial and economic cycles are strongly interconnected despite their different frequencies. However, during the conference, it was noticed that MAPO and MP should focus on their respective targets being sought separately under normal conditions, that both policies should row in the same direction only during stress episodes, and that MAPO should look at price stability at a secondary level because it might be helpful for MP. Would it not be preferable for MAPO and MP to mutually consider, as a second condition, the main goal of the other whenever this is possible?[4]

iii) The lack of a complete toolkit: the ECB has raised possible changes in the CRD IV pack to transfer some relevant national MAPO tools – such the LTV, the DTI and the DSTI - from the MS to the European authorities.

Hope: some progress has been achieved in calibrating instruments and matching them with objectives[5], and in measuring and releasing the state of the financial cycle. However, there was agreement that it is too early to judge the effectiveness of the tools implemented, mainly due to a lack of data for a complete financial cycle.

In conclusion, given the fact that "hope is not a policy strategy" and that building trust is a must, prudence, strength and temperance should also be considered, for the sake of a stable and profitable financial system at the service of real economic growth and, most importantly, of people.

4: On the one hand, Timbergen's rule states that a certain number of targets requires an equal number of instruments. On the other, game theory demonstrates that in repeated games cooperative solutions make a stable equilibrium possible.
5: *Effective Macroprudential Policy: Cross-Sector Substitution from Price and Quantity Measures* by J. Cizel, J. Frost, A. Houben, and P. Wierts. Among other things, they conclude that quantity-based measures are more effective in reducing bank credit than price-based measures.

DISCLAIMER

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