
The EU's Most Influential Economic Policy-maker: Mario Draghi at the European Central Bank

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Abstract

This article assesses the legacy of Mario Draghi as president of the European Central Bank (ECB) from 2011 to 2019, with particular reference to the Greek's sovereign debt crisis. Most macro-economic indicators improved over the course of Draghi's tenure at the ECB, including inflation, budget deficits, yield spreads among euro-area borrowers and unemployment. Draghi played a decisive role in turning the tide on the crisis of confidence that afflicted the euro area and threatened the survival of Europe's single currency in the wake of Greece's sovereign debt crisis. Yet the ECB's unconventional policies prompted sustained controversy and contributed to a low level of trust in the central bank among people in the euro-area member states. The focus of controversy has been on possible asset-price bubbles and 'hidden' transfers between euro-area member states. When and how to normalize its policies is a major challenge for the ECB, as it is for other major central banks that adapted similar policies in response to the global financial crisis.

Mario Draghi became the third president of the European Central Bank (ECB) on 1 November 2011 under difficult circumstances. The International Monetary Fund (IMF) concluded 10 days earlier that Greece's public debt was not sustainable except with 'much stronger' private sector involvement than previously envisaged.¹ On 26 October 2011, the euro-area summit urged all parties to work in earnest towards a bond exchange with significant debt relief for Greece. In May 2010, Greece received its first three-year rescue package of €110 billion; the European Financial Stability

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¹ 'Greece: Debt Sustainability Analysis', 21 October 2011, available at <https://publicintelligence.net/troika-greece-debt-sustainability-analysis-october-21-2011/>.

Facility was set up and the ECB established its ‘secondary market purchase programme’ to reduce sovereign bond yields. However, in 2011, the outlook for Greece worsened. Greece’s borrowing costs increased again rapidly. In July 2011, the IMF concluded that Greece’s debt was not ‘sustainable with a high probability’. A July 2011 proposal for debt rescheduling came to naught.²

Draghi brought wide-ranging, high-level public and private sector experience to the ECB: a doctoral degree in economics at the Massachusetts Institute of Technology, supervised by Nobel prize winners Franco Modigliani and Robert Solow;³ professor of economics at the University of Florence; Italy’s executive director at the World Bank from 1984 to 1990; director general of the Italian Treasury from 1991 to 2001; vice-chairman of Goldman Sachs International from 2002 to 2005; governor of the Banca d’Italia, Italy’s most respected public institution, from 2005 to 2011; and chairman of the Financial Stability Forum from 2009 to 2011. His senior position at Goldman Sachs International in London dogged him at his confirmation hearings in the European Parliament, particularly considering Goldman Sachs’ assistance to Greece to camouflage the extent of its public deficit.⁴ His membership in the Group of 30, a high-level group of public officials, academics and bankers was also criticized.⁵

The Greek debt crisis was an open wound that lingered for more than two years and threatened to engulf the entire Euro zone.⁶ Like his predecessor, Jean-Claude Trichet, Draghi vigorously debated the appropriate policy response to the debt crisis and, more generally, the ECB’s monetary policy stance with his own Governing Council and euro-area governments. On 26 July 2012, merely eight months into his presidency, Draghi acted more decisively than national governments: ‘Within our mandate, the ECB is ready to do *whatever it takes* to preserve the euro. And believe me, it will be enough.’⁷ With these 24 words, Draghi courageously and decisively turned the tide on the crisis

² See the succinct account in Zettelmeyer, Trebesch and Gulati, ‘The Greek Debt Restructuring: An Autopsy’, 28 *Economic Policy* (2013) 518.

³ Dizikes, ‘The Productive Career of Robert Solow’, *MIT Technology Review* (2019), available at www.technologyreview.com/s/614860/the-productive-career-of-robert-solow/.

⁴ ‘Mario Draghi Recommended as Candidate for Next ECB President, European Parliament’, press release (15 June 2011), available at www.europarl.europa.eu/news/en/press-room/20110614IPR21328/mario-draghi-recommended-as-candidate-for-next-ecb-president; S. Foley, ‘What Price the New Democracy? Goldman Sachs Conquers Europe’, *The Independent* (18 November 2011), available at www.independent.co.uk/news/business/analysis-and-features/what-price-the-new-democracy-goldman-sachs-conquers-europe-6264091.html.

⁵ The Consultative Group on International Economic and Monetary Affairs. Other serving and former governors of central banks are also members (for example, Mark Carney of the Bank of England and Haruhiko Kuroda of the Bank of Japan). The European Union ombudsman recommended in July 2018 that Mario Draghi suspend his membership. Recommendation of the European Ombudsman on the Involvement of the President of the European Central Bank and Members of Its Decision-making Bodies in the ‘Group of Thirty’, Doc. 1697/2016/ANA, 5 July 2018; C. Jones, ‘EU Ombudsman Says ECB in Denial over Bankers’ Group’, *Financial Times* (5 July 2018), available at www.ft.com/content/dc64b6e2-8060-11e8-bc55-50daf11b720d.

⁶ P. Blustein, *Laid Low: Inside the Crisis That Overwhelmed Europe* (2016); M.K. Brunnermeier, H. James and J.-P. Landau, *The Euro and the Battle of Ideas* (2016).

⁷ M. Draghi, ‘Verbatim of the Remarks Made by Mario Draghi’, Global Investment Conference, London, 26 July 2012, available at www.ecb.europa.eu/press/key/date/2012/html/sp120726.en.html.

of confidence that afflicted the euro area and threatened the survival of Europe's single currency. The ECB underscored its determination to the world at large that it would act as the lender of last resort and the guardian of financial stability for the entire euro area.

The assessment of Draghi's legacy at the ECB depends partly on one's conception of the appropriate role of the ECB considering its treaty mandate. Asset purchase programmes became a new tool in modern monetary policy, but they have been controversial, in part because they blur the divide between monetary and fiscal policy. Major central banks, including the US Federal Reserve, the Bank of China, the Bank of England and the Bank of Japan adopted such programmes before the ECB.⁸ The Court of Justice of the European Union upheld the lawfulness of some of the ECB's asset purchase programmes in the *Pringle* and outright monetary transactions (OMT) judgments.⁹

To Draghi's fans, including many financial market participants and economists, he played a decisive role in averting the collapse of the eurozone and became one of the most distinguished central bankers of his generation. Nobel prize-winning economist Paul Krugman considers that Draghi 'very clearly saved the euro from collapse in 2012–13, which arguably makes him the greatest central banker of modern times'.¹⁰ The ECB's policies under his leadership are the reason why the eurozone still exists in 2020.¹¹ In contrast, for his many critics, the ECB's unconventional monetary policy – specifically its asset purchase programmes – exceeded the ECB's mandate and lost sight of what ought to have been its overarching priority: price stability.¹² Others expressed concern that the costs of these programmes outweighed the benefits.¹³ And some alleged that the ECB designed and implemented monetary policy tools to specifically support crisis-hit countries.

Price stability was enshrined in the EU treaties to ensure that the euro would be as strong and stable a currency as the German mark, which is overseen by the German Bundesbank.¹⁴ But the definition from 2003 onwards of 'close to, but below, 2 percent over the medium term' already departed from the understanding of inflation hawks.¹⁵ Jürgen Stark's resignation from the ECB's Executive Board in September

⁸ European Central Bank (ECB), 'Asset Purchase Programmes', available at www.ecb.europa.eu/mopo/implement/omt/html/index.en.html.

⁹ Case C-370/12, *Thomas Pringle v. Government of Ireland and* (EU:C:2012:756); Case C-62/14, *Peter Gauweiler and Others v. Deutscher Bundestag* (EU:C:2015:400).

¹⁰ P. Krugman, 'After Draghi (Wonkish)', *New York Times* (24 May 2019), available at www.nytimes.com/2019/05/24/opinion/after-draghi-wonkish.html.

¹¹ J. Randow and A. Speciale, *Mario Draghi L'Artefice: La Vera Storia dell'Uomo Che Ha Salvato l'Euro* (2017).

¹² H.-W. Sinn, *The Euro Trap: On Bursting Bubbles, Budgets, and Beliefs* (2014); A. Mody, 'Draghi's Dangerous Farewell', *Project Syndicate* (9 September 2019), available at www.project-syndicate.org/commentary/mario-draghi-ecb-monetary-stimulus-risks-by-ashoka-mody-2019-09; M.C. Kerber, *Die Draghi-Krise: Wie die Europäische Union plant und Deutschland bezahlt* (2018).

¹³ Mody, *supra* note 12.

¹⁴ J. Harold, *Making the European Monetary Union: The Role of the Committee of Central Bank Governors and the Origins of the European Central Bank* (2012).

¹⁵ ECB, 'The Definition of Price Stability', available at www.ecb.europa.eu/mopo/strategy/pricestab/html/index.en.html. The Harmonised Index of Consumer Prices (HIPC) does not include owner-occupied housing in its measure of inflation. In 2003, the ECB tweaked its definition of price by adding 'close to'. P. Hartmann and F. Smets, 'The First Twenty Years of the European Central Bank: Monetary Policy', ECB Working Paper no. 2219 (2018).

2011 underscored the deep discontent in the Bundesbank and mainstream German economic thinking about the ECB's ostensibly dovish policy stance (which was in synch with the policies of other major central banks).

Table 1 shows that most macro-economic indicators improved over the course of Draghi's tenure at the ECB. Crucially, inflation, if anything, undershot its target from 2015 to 2019. Of course, the ECB was far from the only actor whose actions affected these macro-economic variables. Yet its decisive actions at the height of the debt crisis were the single most important reason why the euro area has enjoyed a robust recovery since 2012. Some criticize the ECB during Draghi's tenure for under-shooting on inflation.¹⁶ At 1.3 per cent, year-on-year inflation is arguably well below the target of close to, but below, 2 per cent. To some, this is a serious shortcoming given that the ECB's primary objective, enshrined in the treaties, is to maintain price stability. Others consider that the ECB, under President Trichet in 2003, adopted too high an inflation target and that the ECB's expansionary monetary policy since 2013 holds in store spikes in inflation for the future.¹⁷ Arguably, President Draghi steered a pragmatic middle course that leaves many seemingly unhappy. The ECB did not achieve its inflation target, but it did avoid Japan's deflation trap for now.¹⁸

On the plus side, annual GDP growth in the euro area over the last five years has been higher than it was in 2011 and 2012. Unemployment has fallen sharply from a peak of above 11 per cent to 7.5 per cent across the euro area (equivalent to the creation of 11 million jobs) and from a peak of above 25 per cent to under 17 per cent in Greece. Draghi himself regards the significant improvement in labour markets as his most important achievement.¹⁹ Sizeable government deficits in 2011 – a legacy of the global financial crisis and the huge fiscal costs associated with it – shrunk to a fifth from 2011 to 2019. The stock of euro-area government debt is slowly declining, albeit from an uncomfortably high level of over 90 per cent on average. Borrowing costs of euro-area governments are again clustered together, as reflected in a yield difference of 0.37 between triple A rates for euro-area borrowers and all other euro-area borrowers at the end of Draghi's tenure. This reflects the widespread sentiment in financial markets that Europe's common currency is here to stay and that no euro-area member state will leave the euro area in the foreseeable future. Support from the public for the common currency increased from a low point of 67 per cent to 75 per cent at the end of Draghi's tenure.

The distributional implications of the ECB's crisis response are not yet clear. On the one hand, real household disposable income in the euro area declined from 2008

¹⁶ V. Romei and M. Arnold, 'Draghi's ECB Tenure: Saving the Euro, Faltering on Inflation', *Financial Times* (29 October 2019), available at www.ft.com/content/a62b221c-eb64-11e9-a240-3b065ef5fc55.

¹⁷ E.g. H.-W. Sinn, 'Mario Draghi Lays Out Plan for a Dangerous Round of Stimulus', *The Guardian* (31 July 2019), available at www.theguardian.com/business/2019/jul/31/mario-draghi-lays-out-plan-for-a-dangerous-round-of-stimulus.

¹⁸ E.g. T. Ito and E.S. Mishkin, 'Two Decades of Japanese Monetary Policy and the Deflation Problem', NBER Working Paper no. 10878 (2004).

¹⁹ F. O'Brien and J. Randow, 'Three Words, 11 Million Jobs: Draghi's Legacy for Euro Area', *Bloomberg* (22 October 2019), available at www.bloomberg.com/news/articles/2019-10-22/three-words-11-million-jobs-draghi-s-euro-area-economic-legacy.

Table 1: Key indicators during Mario Draghi's ECB presidency

	Start of Draghi's tenure at the ECB (1 November 2011)	OMT announcement (2 August 2012)	End of Draghi's tenure (31 October 2019)
ECB's deposit facility rate	0.0%	0.00%	-0.50%
ECB's main refinancing rate	0.75%	0.75%	0.00%
Euro-area annual GDP growth rate	0.6% (-10.2% for Greece)	-1.0% (-7.9% for Greece)	1.2% (Q2)
Euro area annual rate of inflation	3.8%	2.8%	1.3%
Unemployment (% of labour force)	10.6% (20.5% for Greece)	11.6% (25.9% for Greece)	7.5% (16.6% for Greece)
Government deficit/surplus (% of gross domestic product [GDP])	-4.5%	-3.8%	-0.7% (Q2)
Euro-area government debt (% of GDP)	90.7%	92.6%	85.8%
Size of ECB balance sheet	€2.33 trillion	€3.07 trillion	€4.69 trillion
Difference in yield between triple A-rated euro-area borrowers and all euro- area borrowers (5 year)	1.69	2.99	0.37
Euro-US dollar exchange rate	1.36	1.26	1.11
Support for the euro	67%	67%	75%
Trust in ECB	36% trust / 46% no trust	37% trust / 45% no trust	42% trust / 41% no trust

Source: Author's own compilation from ECB, IMF, Eurostat, Eurobarometer.

to 2014 but increased from 2015 to 2019.²⁰ The Gini coefficient for the euro area remained largely unchanged at around 30.5 during Draghi's tenure.²¹ Nevertheless, the analysis of the distributional impact of monetary policy on income and wealth remains in its infancy, and the few existing studies reach different conclusions.²² Even

²⁰ ECB, Statistical Data Warehouse, 'Report on Household Disposable Income and Components', available at <https://sdw.ecb.europa.eu/reports.do?node=1000004869>.

²¹ Eurostat, 'Gini Coefficient of Equivalised Disposable Income: EU-SILC Survey', available at http://appsso.eurostat.ec.europa.eu/nui/show.do?wai=true&dataset=ilc_di12.

²² M. Lenza and J. Slacalek, 'How Does Monetary Policy Affect Income and Wealth Inequality? Evidence from Quantitative Easing in the Euro Area', ECB Working Paper no. 2190 (2018); P. Bunn, A. Pugh and C. Yeates, 'The Distributional Impact of Monetary Policy Easing between 2008 and 2014', Bank of England Staff Working Paper no. 720 (2018); P.R. Lane, 'Households and the Transmission of Monetary Policy', Central Bank of Ireland/ECB Conference on Household Finance and Consumption, Dublin, 16 December 2019, available at www.bis.org/review/r191217b.pdf.

if the jury is still out, the perception that monetary policy benefited the top 5 per cent of the wealth distribution with assets to invest has been hard to dispel and has dogged the ECB (as well as other central banks) since the global financial crisis that started in 2007.

On the negative side, much of this success is probably attributable to extremely low interest rates for a prolonged period (on the serious side effects of which more is discussed below) and an arguably undervalued euro (for example, the important euro-US dollar exchange rate went from 1.36 in November 2011 to 1.11 in November 2019). At the end of Draghi's tenure, the ECB's deposit facility rate was -0.5 per cent, and its main refinancing rate was 0 per cent. The ECB was the first major central bank to cut rates deep into negative territory.²³ As a result, the ECB had even less room for manoeuvre than other major central banks to ease monetary policy in response to the next crisis. There is little monetary firepower in terms of interest rates left. Moreover, the size of the ECB's balance sheet doubled during Draghi's tenure, with the ECB owning a quarter of all outstanding government bonds issued by euro-area countries.

Trust in the ECB among citizens is stuck at just over 40 per cent, and the percentage of people that distrust the ECB increased compared to the first decade of the ECB's existence. This is not good enough and represents a major disconnect with the success of the ECB's crisis policies, as reflected in major macro-economic variables.²⁴ That said, limited trust or loss of trust in the central bank is not confined to the euro area. The US Federal Reserve System experienced a loss of trust after the global financial crisis. One of the declared priorities of Christine Lagarde is to increase trust in the ECB.²⁵ As Benoît Cœuré, an Executive Board member for much of Draghi's tenure, put it, the ECB must 'bring monetary policy closer to the people to dismantle the veil of effectiveness and to foster acceptance of policies and instruments that were often used as scapegoat for shortcomings and deficiencies elsewhere in [the Euro area's] public policy apparatus'.²⁶

In macro-economic terms and in terms of the eurozone's continued existence and integrity, Draghi's legacy shines bright. When firefighting, the twin priority is to prevent the fire affecting neighbouring buildings and to extinguish the fire. Rebuilding and laying sound foundations for the future may have to wait for some time. The ECB that Draghi left in November 2019 is a different institution from the one he inherited eight years before. It became a modern central bank with an array of monetary policy tools that might come in handy for future crises. Draghi defended and protected the ECB's independence at the time of extreme stress – and at least in that respect is

²³ The first central bank to take the main interest rate below zero was Sweden's Riksbank in early 2015. R. Mile and M. Arnold, 'Why Sweden Ditched Its Negative Rate Experiment', *Financial Times* (19 February 2020), available at www.ft.com/content/478fe908-5168-11ea-8841-482eed0038b1.

²⁴ Benoît Cœuré, 'Monetary Policy: Lifting the Veil of Effectiveness', ECB Colloquium on Monetary Policy: The Challenges Ahead, Frankfurt am Main, 18 December 2019, available at www.ecb.europa.eu/press/key/date/2019/html/ecb.sp191218~12a0385d3b.en.html.

²⁵ Interview with Christine Lagarde, *Challenge Magazine*, 8 January 2020, available at www.ecb.europa.eu/press/inter/date/2020/html/ecb.in200108~f3ba434000.en.html.

²⁶ Cœuré, *supra* note 24.

comparable to the legendary chair of the US Federal Reserve, Paul Volcker.²⁷ The institution that Draghi led for eight years is now at the very heart of euro-area economic policy-making.

Nevertheless, the ECB's ultra-low interest rates for the last decade have had important side effects, particularly possible asset-price bubbles²⁸ and the misallocation of capital. Like in other major jurisdictions, there is widespread agreement on the need for the central bank to normalize monetary policy but disagreement on the appropriate pace and timing of such normalization. Some compare the ECB's prolonged, major stimulus to 'steroids' or 'drugs', the withdrawal of which is increasingly costly and difficult the longer it persists. In September 2019, Draghi's parting shot was to restart quantitative easing with no time limit, despite opposition from several national central bank governors.²⁹ He also cut its deposit facility rate from -0.4 per cent to -0.5 per cent. Draghi passes on a difficult legacy to Christine Lagarde, the IMF's former managing director and his successor. Specifically, there is growing concern about the ECB's inability to respond to the next downturn³⁰ and the continued fragility of the euro area, due to the absence of automatic stabilizers and the lack of a centralized fiscal capacity.

For the last several years of his tenure, a debate has raged about the dark side of Draghi's legacy, particularly possible asset-price bubbles. After the ECB restarted its asset purchase programme and lowered its deposit rate to -0.50 per cent on 12 September,³¹ the German tabloid newspaper *Bild* referred to the outgoing ECB president as 'Count Draghila' and depicted him with vampire teeth. It referred to how the ECB's asset purchase programme and low interest rates 'suck the accounts [of German savers] dry'.³² Such narratives can have a powerful hold on the public's imagination.³³

²⁷ P. Volcker and C. Harper, *Keeping At It: The Quest for Sound Money and Good Government* (2018); Goolsbee, 'The Volcker Way: Lessons from the Last Great Hero of Modern Finance', 92 *Foreign Affairs* (2013) 166; R. Lowenstein, 'How Paul Volcker Banished Inflation and Protected the Fed's Independence', *Washington Post* (15 December 2019), available at www.nytimes.com/2019/12/09/business/paul-a-volcker-dead.html; B. Apelbaum, R.D. Hershey Jr. and P.A. Volcker, 'Fed Chairman Who Waged War on Inflation, Is Dead at 92', *New York Times* (9 December 2019), available at www.nytimes.com/2019/12/09/business/paul-a-volcker-dead.html; L. Barber, S. Fleming and D. Lascelles, 'Paul Volcker, Central Banker, 1927-2019', *Financial Times* (9 December 2019), available at www.ft.com/content/9f39065c-1a8c-11ea-9186-7348c2f183af.

²⁸ B. Brown, *Euro Crash: How Asset Price Inflation Destroys the Wealth of Nations* (2014).

²⁹ T. Fairless, 'As Draghi Gets Ready to Exit, His Legacy Remains Contested', *Wall Street Journal* (13 September 2019), available at www.wsj.com/articles/as-draghi-gets-ready-to-exit-his-legacy-remains-contested-11568404206.

³⁰ M. Feldstein, 'Europe's Economic Dilemma', *Project Syndicate* (30 October 2017), available at www.nber.org/feldstein/projectsyndicateoct302017.html.

³¹ ECB, 'Monetary Policy Decisions', press release (12 September 2019), available at www.ecb.europa.eu/press/pr/date/2019/html/ecb.mp190912~08de50b4d2.en.html.

³² 'Geld Wahnsinn: So saugt GRAF DRAGHILA unsere Konten leer', *Bild* (13 September 2019), available at www.bild.de/bild-plus/geld/wirtschaft/politik-inland/ezb-leitzins-schlecht-fuer-sparer-frau-merkel-stoppen-sie-endlich-den-minus-zins-64669942.

³³ I. Schnabel, 'Narratives about the ECB's Monetary Policy – Reality or Fiction?', Speech at Juristische Studiengesellschaft Karlsruhe, 11 February 2020, available at www.ecb.europa.eu/press/key/date/2020/html/ecb.sp200211_1~b439a2f4a0.en.html.

Such charges that the ECB's policies predominantly benefited crisis-hit countries or 'frugal' creditor countries are simplistic and have caused considerable harm for cohesiveness and solidarity across euro-area member states. A more nuanced assessment requires constructing counterfactuals that take account of all of the major variables. For example, one cannot conclude that the ECB's policies have hurt savers across euro-area economies without considering, among others, the risk of the euro area breaking up and the stability implications for deposit-taking institutions. The position of savers could have been much worse if there had been a disorderly disintegration in the euro area. Moreover, many savers are also employees and, thus, benefit from lower unemployment, and companies in the northern member states reaped benefits from the euro's competitive exchange rate.

The debate about the benefits and costs of the ECB's crisis response across and within euro-area member states is set to continue. With the establishment of the European Monetary Union, the economic destiny of the euro-area member states have become intertwined. It is a matter of common concern for the euro area as a whole if individuals and businesses in one or several member states can only borrow at rates considerably above those in other euro-area member states; if a member state free rides on the common pool of creditworthiness of the euro area or if national authorities undermine the independence of a national central bank governor.

It was perhaps the inevitable consequence of the euro-area sovereign debt crisis and the aftermath of the global financial crisis that the ECB has come under sustained scrutiny and attack, both by countries most directly affected, such as Cyprus and Greece, and by countries that became deeply concerned about intra-euro-area transfers, such as Germany or the Netherlands, among others.³⁴ As president of the ECB, Draghi created the conditions for the euro's survival at a time when there were serious questions about its sustainability. For the continued success of the European Monetary Union, it is critical that the euro and the ECB enjoy broad-based support and trust across all of its states and peoples.

³⁴ Cf. the debate on Target2, the Euro area's payment settlement system. E.g. H.-W. Sinn, *The Euro trap* (2014), ch. 6; C. Watzinger, *Rechtliche Probleme der Ausgestaltung von Zahlungsverkehrssystemen in der Europäischen Wirtschafts- und Währungsunion: Eine Analyse von TARGET2* (2016); P. de Grauwe and Y. Ji, 'What Germany Should Fear Most Is Its Own Fear', *Voxeu* (18 September 2012), available at <https://voxeu.org/article/how-germany-can-avoid-wealth-losses-if-eurozone-breaks-limit-conversion-german-residents>.