CONCLUDING REMARKS

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I would like to thank all the participants for the presentations and for the discussions that we have had. I said yesterday that I was looking forward to learning from all of you, and I can report to you that I have indeed learned a lot and I hope that each of you has learned as well.

I am a soccer fan, I like soccer. And, at the end of conferences like this, I always feel the way I feel at the end of the first week of the soccer World Cup: I know I have watched many games, but I don't quite remember which teams I have seen and which plays I liked. It's all mixed up. Something similar happens at the end of conferences like this: there is information overload. But, as well as in the world of soccer you can watch the replay, in a conference like this, you can always go back and read the Power Point presentations, the notes you have taken, and the proceedings.

So, I encourage you to do that in the next few days, if you have time, and try to draw from those the main takeaways, the main conclusions you got from the four or five main dimensions of spillovers from negative interest rates in the euro area that have been discussed over the past couple of days. I have a few tentative takeaways that I would like to share with you, but like at the end of that first week of soccer games, they are not very clear, they are not conclusions, they are not a summary or interpretations, but just my preliminary takeaways to give you some more things to think about.

The first one has to do with what you call here, appropriately, "euroization," prevalent in the Western Balkans, and developments related to the interplay between that process and financial stability.

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The first point is a very general point: what to do with euroization in those economies that have a partial euroization process going on. There are two extreme attitudes: one is total indifference and the other is obsession.

None of the two extremes is correct to approach partial euroization. So, central bankers and policymakers need to strike a balance between denial, neglect, or total indifference on the one hand and obsession with how to undo it on the other hand. Now it turns out that striking a balance between financial and monetary objectives is not in the DNA and should not be in the DNA of central bankers. Central bankers are encouraged to be obsessed about maintaining inflation low and stable and about preserving financial stability. I encourage central bankers to remain obsessed about that, but, in the spectrum between obsession and indifference about this issue, I will encourage central bankers to be further away from obsession in the issue of how to deal with partial euroization. This is my first takeaway.

The second takeaway is related to the first one. It has to do with the time horizon over which partial euroization should be considered a concern.

I think that clarity about the horizon over which macroeconomic or financial variables respond to shocks and the horizon over which policies to mitigate the effects of the shocks are relevant is one of the most common casualties of policy discussions.

The same happens in conferences like this. We tend to focus on the sign of a given phenomenon: if it has a positive effect or a negative effect or a neutral effect. There are many reasons it is like that. Take the issue of partial euroization. We have heard many times over the past two days that partial euroization seems to have negative effects and seems to negatively affect the effectiveness of the monetary policy. That's one effect. We have heard less that partial euroization also increases the risk to financial stability.

Over what horizons are these two problems relevant? Are these short-term issues, should they be short-term concerns, both of them,

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or are they medium-term concerns, are they long-term concerns? It's different depending on the problem you focus on.

The problems that euroization causes for the conduct of monetary policy cannot be mitigated over a short term. It is more of a medium-term issue. So, we have to deal or cope with the issue that there is a partial euroization and we should remain focused on achieving the low and stable level of inflation despite the partial euroization. At the same time, one should try to adopt measures that are long-term to ease the consequences of partial euroization or contain it.

We just heard one of the colleagues mentioning that it is a marathon, and I would agree with that. I would just add that there is not just the marathon of the next Olympics, but there are the marathons of the next three Olympics. It is a long-term horizon over which addressing partial euroization should be an objective. It's a matter-of-years issue, it's not a matter-of-quarters issue.

How about the effects of euroization on financial stability? That's completely a different horizon. That is a short-term problem. That is a near-term issue. Protecting and preparing the economy for negative shocks in an economy where the balance sheets are partially euroized, should be the main concern of all central bankers and authorities, even though the euroization or the partial euroization is not going away.

So, this risk or this vulnerability brought by partial euroization is the main reason I said at the beginning that the concern of the central bankers should be further away from obsession on partial euroization but not all the way to the denial and neglect. You cannot ignore that the balance sheets of an economy partially euroized are weak and are subject to shocks of many types. They will be aggravated by the fact that you have all these mismatches lying on those balance sheets of banks, of the government, and of households. When there is a downturn or a shock, that can take many shapes and forms and has happened in many countries; the outcome is invariably negative, and that is not the time to start preparing to mitigate the effects. You must be prepared beforehand.

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The third takeaway is also related to the discussion of the past two days. We have heard that there are no differences between low interest rates and negative interest rates. The traditional policy rate effects continue unfolding when interest rates turn negative. Everything is fine and smooth. Perhaps, indeed, this is the case for monetary policy, which was the focus of the presentations. One aspect that was not discussed, because it was not the subject of this conference, is that at the same time that negative interest rates have exerted some effects for monetary policy in the euro area and in Switzerland and have had spillovers on monetary policy for all the countries including the Western Balkans, they have also increased systemic risk both in the center, in the euro area, and in the periphery. So, the systemic risk in a low interest rate environment has increased. That's true and there is enough evidence to show that this is the case.

This increased systemic risk is aggravated by two factors that are specific to emerging markets and to the Western Balkans: one is the ownership of the banks and the other is the partial euroization or the mismatch of the balance sheets. I talked about partial euroization so I will not get into that, but let me talk about ownership of the banks. Banking systems in emerging markets, like your region, are very different from the banking systems in advanced economies, not just because of the size or the number of banks, but also because of the ownership structure of the banks. In most advanced economies, all banks are private businesses, private banks, small, medium, large, mostly privately owned. You go to emerging markets and you have three types of ownerships: you have private domestically owned, foreign private banks, and government-owned banks. In addition to that, you have fewer banks. So, the presumption that whatever works in terms of financial stability and resolution and activity in the euro area or in the US applies directly and without a matter of thought to emerging market is a wrong presumption.

The same goes for using and having a false sense of security for traditional indicators such as a small leverage of households, natural hedges, lower NPLs. All these are nice in a crisis; however, in crises, as we have seen, it does matter also what type of relationship exists between the branches of the foreign banks and the parents of the foreign banks. Most countries have found too late that what they

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thought was going to happen didn't happen, especially regarding the expected support that foreign banks would provide to their local subsidiaries. This means that you must not assume, but prepare. Check with your foreign banks what is the exact presumption or agreement, what would happen if the event materializes in your country or the rest of the world. It doesn't have to be your country; it can be a neighbor country, it can be in the region.

Complacency about the risk to financial stability is the biggest risk for a central bank. When it comes to identified tail risk or extreme event risk, there is no middle ground here between a central bank not being indifferent to systemic risk and being obsessed. It must be obsessed to anticipate to the largest possible extent tail risks, and it must prepare a strong resolution framework for extreme events.

I have seen this in other parts of the world in different attempts. I've seen countries come and say: we fully adopted the dollar and this will protect us completely against financial crises, and I saw those countries undoing full dollarization because they had to. In an extreme event, that can happen; the presumption that the reserves were covering all possible events may not hold. When liquidity assistance needs to be provided to banks beyond the level of reserves held, in a foreign currency you cannot issue, you have to issue something else, and if that doesn't contain the damage of the negative shock and the foreign-owned parent banks don't give liquidity to the local banks, then, you have to do something with their banks.

So, you truly must be prepared and, in some cases, I have seen it more than once, financial stability risks materialized because the authorities were adopting not very prudent policies, and in other cases, it was just a bad combination of external shocks. So, the bottom line of all this is to bring the issue of financial stability as an additional dimension to the negative interest rate environment and apply it to your own countries.

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