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INFO SAVING CGS IN FRG AND WEST BERLIN

MIPT AND MY TELS NOS 426 AND 427 : EUROPEAN MONETARY COOPERATION

SUMMARY
1. BUNDESBANK PRESIDENT POHL ELABORATED HIS VIEWS ON EUROPEAN MONETARY COOPERATION IN A MAJOR NEWSPAPER ARTICLE PUBLISHED ON 28 MAY. ARTICLE HIGHLIGHTS THE MANY DIFFICULTIES INOVLVED IN CREATING A EUROPEAN CENTRAL BANK.

DETAIL
2. IN A LONG ARTICLE IN FRANKFURTER ALLGEMEINE ZEITUNG, PUBLISHED ON 28 MAY, THE BUNDESBANK PRESIDENT AMPLIFIED HIS VIEWS ON MONETARY COOPERATION OUTLINED AT HIS PRESS CONFERENCE ON 5 MAY (MY TELS NOS 426 AND 427).

3. POHL OBSERVED THAT THE EC WAS ENTERING A NEW PHASE WITH THE APPROACH OF 1992. LIBERALISATION OF CAPITAL MOVEMENTS AND FULL CONVERTIBILITY OF CURRENCIES WERE ESSENTIAL COMPONENTS OF THE SINGLE MARKET AND ALSO THE BASIS OF EUROPEAN MONETARY UNION. AS THE 1970 WERNER REPORT HAD MADE CLEAR, FIXED EXCHANGE RATES WERE ANOTHER PRECONDITION OF MONETARY UNION. IT WOULD BE A SMALL STEP FROM MONETARY UNION TO THE CREATION OF A COMMON CURRENCY. BUT ALL THIS WAS STILL A LONG WAY OFF. THE DIFFICULT POLITICAL DECISIONS INVOLVED IN MOVING TOWARDS FULL EMU COULD NOT BE SIDESTEPPED BY CREATING A PARALLEL CURRENCY, AS THE HISTORY OF THE ECU HAD SHOWN. A PARALLEL CURRENCY COULD ONLY REPLACE NATIONAL CURRENCIES WHEN IT COULD COMPETE WITH THE STRONGEST EC CURRENCY.

4. A EUROPEAN CENTRAL BANK WAS NOT ESSENTIAL TO MONETARY UNION. EUROPEAN CENTRAL BANKS COULD COOPERATE SUCCESSFULLY IF A SUBSTANTIAL DEGREE OF ECONOMIUC CONVERGENCE COULD BE ACHIEVED. BUT A MINIMAL INSTITUTIONAL FRAMEWORK WOULD BE A USEFUL UNDERPINNING. ANY STEP TOWARDS INSTITUTIONALISING MONETARY COOPERATION WITH THE AIM OF CREATING A EUROPEAN CENTRAL BANK POSED A NUMBER OF FUNDAMENTAL

QUESTIONS WHICH HAD TO BE ADDRESSED RIGHT AT THE BEGINNING. FOR EXAMPLE:

A) WHAT SHOULD BE THE OBJECTIVES OF A EUROPEAN CENTRAL BANK? IN POHL'S VIEW ITS PRIMARY OBJECTIVE, AS IN THE CASE OF THE BUNDESBANK, SHOULD BE TO PROTECT THE CURRENCY BY ENSURING PRICE STABILITY. WITH THEIR MEMORIES OF TWO DISASTROUS INFLATIONS, MOST GERMANS COULD ACCEPT THE CONCEPT OF A EUROPEAN CENTRAL BANK ONLY IF THE PRE-EMINENCE OF THIS OBJECTIVE WAS GUARANTEED. THE BANK COULD NOT BE DIVERTED FROM ITS PRIMARY TASK BY OTHER OBJECTIVES RELATED TO EXCHANGE RATE STABILITY, REGIONAL POLICY, EMPLOYMENT CREATION ETC., WHICH MIGHT CONFLICT WITH THIS FUNDAMENTAL OBJECTIVE.

B) HOW COULD ITS INDEPENDENCE BE GUARANTEED? THE TASK OF PROTECTING THE CURRENCY WOULD ONLY BE POSSIBLE IF A EUROPEAN CENTRAL BANK ENJOYED COMPLETE INDEPENDENCE IN DECISION-TAKING NOT ONLY FROM NATIONAL GOVERNMENTS BUT ALSO FROM EC INSTITUTIONS. IN SOME MEMBER STATES THIS WOULD REQUIRE FAR-REACHING CHANGES IN THE CONSTITUTION OF THEIR CENTRAL BANKS. CHANGES WOULD ALSO BE REQUIRED IN THE FRG WITH ITS QUASI TWO-TIER SYSTEM OF REGIONAL CENTRAL BANKS IN EACH OF THE TEN LAENDER AND WEST BERLIN AND A CENTRAL DIRECTORATE IN FRANKFURT.

C) HOW SHOULD IT BE ORGANISED? IN POHL'S VIEW, A EUROPEAN CENTRAL BANK SHOULD BE ORGANISED ON FEDERAL LINES, WITH CENTRALISATION ONLY WHERE ABSOLUTELY NECESSARY, LEAVING AS MANY FUNCTIONS AS POSSIBLE TO NATIONAL COMPETENCE.

D) HOW SHOULD ITS ROLE IN FINANCING PUBLIC BE CIRCUMSCRIBED? A EUROPEAN CENTRAL BANK SHOULD NOT GET INVOLVED IN FINANCING PUBLIC DEFICITS BY INCREASING THE MONEY SUPPLY. WHILE SUCH A ROLE WAS EXPRESSLY FORBIDDEN BY LAW IN THE FRG, THIS PRINCIPLE WAS NOT NECESSARILY TAKEN FOR GRANTED IN OTHER COUNTRIES.

E) TO WHAT EXTENT SHOULD A EUROPEAN CENTRAL BANK BE RESPONSIBLE FOR EXTERNAL EXCHANGE RATE POLICY? EXCHANGE RATE STABILITY COULD NOT BE THE PRIMARY OBJECTIVE OF MONETARY POLICY IF THIS WAS LIKELY TO LEAD TO INFLATION. BUT THERE WOULD BE SOME SCOPE FOR MONETARY COOPERATION WITH COUNTRIES OUTSIDE THE EC. A EUROPEAN CENTRAL BANK WOULD THEREFORE HAVE TO CONTROL AND ADMINISTER PART OF THE NATIONAL CURRENCY RESERVES. THIS REQUIREMENT HAD BEEN FORESEEN WHEN THE EMS WAS CREATED BUT AT THAT TIME MOST MEMBER STATES WERE RELUCTANT TO TRANSFER PART OF THEIR CURRENCY RESERVES TO A SUPRA-NATIONAL INSTITUTION.

F) WHERE SHOULD A EUROPEAN CENTRAL BANK BE SITED? FRANKFURT, PARIS, BRUSSELS AND LONDON WERE ALL POSSIBLE CONSIDERATIONS.

5. IT SEEMED DOUBTFUL WHETHER MEMBER STATES WERE READY TO TAKE SUCH FAR-REACHING DECISIONS AFFECTING NATIONAL SOVEREIGNTY WHEN FOUR MEMBERS OF THE EC, THE UK, SPAIN, PORTUGAL AND GREECE, WERE NOT YET MEMBERS OF THE ERM AND ONE, ITALY, HAD SPECIAL ARRANGEMENTS.

6. NEVERTHELESS, CONSIDERABLE PROGRESS TOWARDS MONETARY INTEGRATION HAD BEEN MADE SINCE THE FOUNDATION OF THE EMS. THE COMMITTEE OF CENTRAL BANK GOVERNORS HAD PLAYED AN IMPORTANT ROLE IN THIS PROCESS AND MIGHT BE GIVEN ENHANCED POWERS, FOR EXAMPLE, THE RIGHT TO TAKE DECISIONS REGARDING CHANGES IN EMS ALIGNMENTS WHICH COULD BE DONE IN A TIMELY AND DISCREET MANNER. BUT SO FAR THIS IDEA HAD BEEN REJECTED BY FINANCE MINISTERS. THE EUROPEAN FUND FOR MONETARY COOPERATION, ON THE OTHER HAND, WAS NOT A SUITABLE BODY TO FORM THE NUCLEUS OF A EUROPEAN CENTRAL BANK SINCE IT WAS DEPENDENT ON THE EC COUNCIL OF MINISTERS.

7. THE STRENGTH OF THE GERMAN ECONOMY HAD ENABLED THE D-MARK TO PLAY A STABILISING ROLE IN THE EMS. THE BUNDESBANK WOULD HAVE TO BEAR THE MAIN BURDEN OF INCREASED INTRA-MARGINAL INTERVENTION AS A RESULT OF RECENT AGREEMENTS (NYBORG ETC). DESPITE DEMANDS BY SOME MEMBER STATES FOR GREATER ''SYMMETRY'', THE EMS WOULD ONLY BE WEAKENED RATHER THAN STRENGTHENED IF THE BUNDESBANK WAS OBLIGED TO TAKE ON EVEN GREATER COMMITMENTS TO INTERVENE IN SUPPORT OF OTHER EMS CURRENCIES, FOR EXAMPLE, BY HOLDING THEIR CURRENCIES IN ITS RESERVES. THE FRG WOULD TAKE STEPS TO REDUCE ITS BALANCE OF PAYMENTS SURPLUS AS A CONTRIBUTION TO EQUILIBRIUM IN THE EMS BUT THIS WOULD BE DONE BY STRENGTHENING DOMESTIC DEMAND NOT BY MONETARY MEANS.

8. EUROPEAN MONETARY UNION WAS A DESIRABLE POLITICAL AND ECONOMIC OBJECTIVE. FULL LIBERALISATION OF CAPITAL MOVEMENTS, WHICH SHOULD BE ACHIEVED BEFORE THE END OF THE GERMAN PRESIDENCY, WOULD BE A MILESTONE IN THAT DIRECTION. SO WOULD PARTICIPATION BY ALL EC MEMBER STATES IN THE ERM WHETHER FURTHER INSTITUTIONAL STEPS TOWARDS MONETARY UNION WOULD BE POSSIBLE WAS IN THE HANDS OF NATIONAL GOVERNMENTS AND PARLIAMENTS. REALISM WAS MORE IMPORTANT IN THIS PROCESS THAN WISHFUL THINKING.

MALLABY