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FRAME ECONOMIC
FRAME EXTERNAL

ECOFIN COUNCIL: 12 MARCH: GERMAN ECONOMIC AND MONETARY UNION (GEMU)

SUMMARY

1. FRG PROGRESS REPORT OVER LUNCH ON MONETARY UNION. NO CLEAR TIMETABLE ESTABLISHED, BUT INDICATIONS THAT FRG WAS NOT CURRENTLY PLANNING INTEREST RATE RISES TO COUNTER INFLATIONARY PRESSURES. DELORS NOTED THE PRACTICAL PROBLEMS OF UNIFICATION FOR COMMUNITY LAW AND PROMISED A PAPER ON THIS FOR THE INFORMAL ECOFIN AT THE END OF MARCH.

DETAIL

2. WAIGEL (FRG) GAVE A LENGTHY ACCOUNT OF THE SITUATION IN THE GDR AND A PROGRESS REPORT ON GEMU. IT WAS EXCITING TO ATTEND ELECTION MEETINGS IN THE EAST ATTENDED BY EIGHTY TO A HUNDRED THOUSAND PEOPLE. BUT EAST GERMANS WERE STILL DAY DREAMING ABOUT THE FUTURE AND THE FRG GOVERNMENT SAW IT AS ITS JOB TO MAKE THEM FACE REALITY. MUCH CHANGE WOULD BE REQUIRED. THERE WERE BOUND TO BE SOCIAL PROBLEMS. THE GDR'S EXTERNAL DEBT WAS INCREASING BUT IT WAS NOT AS BAD AS SOME HAD MADE OUT. DOMESTIC DEBT WAS MORE SERIOUS. THERE WAS AN URGENT NEED FOR NEW INSTITUTIONS AND A TAX SYSTEM. PRODUCTIVITY WAS VERY LOW. MONETARY UNION WOULD BRING PRICE RISES AND UNEMPLOYMENT BUT THERE WAS GREAT POTENTIAL FOR MOPPING UP SURPLUS LABOUR. THE SERVICE INDUSTRY IN THE GDR WAS ALMOST NON-EXISTENT. THERE WAS NO INSURANCE INDUSTRY.

3. WAIGEL SAID LITTLE ON THE TIMETABLE FOR MONETARY UNION. SOME IDEAS HAD BEEN PUT TO THE GDR GOVERNMENT BUT IT WAS NOT CLEAR WHEN THEY WERE GOING TO RESPOND. ON THE DEUTSCHMARK/OSTMARK CONVERSION RATE, THE FRG WAS STILL UNDECIDED. ONCE THEY HAD CLEAR INFORMATION ON THE AMOUNT OF PRIVATE SAVINGS IN THE GDR THEY WOULD BE ABLE TO SET A TIMETABLE. IN THE MEANTIME, SPECULATION ON THE EXCHANGE RATE RATIO WAS COUNTERPRODUCTIVE (''SOME PEOPLE SHOULD SHUT UP''). BUT PRUDENCE AND CAUTION WOULD CONTINUE TO BE THE WATCHWORDS FOR THE FRG. THE GROWTH RATE SHOULD NOT EXCEED THE NORMAL INCREASE IN GDP.

THE BUNDESBANK MUST REMAIN INDEPENDENT. THE GDR GOVERNMENT HAD BEEN TOLD THAT THERE WAS NO ROOM FOR COMPROMISE ON MONETARY POLICY. THE MONEY SUPPLY MUST BE CONTROLLED. INTEREST RATES WOULD STABILISE AND COME DOWN WHEN PEOPLE REALISED THAT MONETARY UNION WOULD NOT INCREASE THE VOLUME OF MONEY IN CIRCULATION. THE FRG WOULD HAVE TO FIND GREATER SOCIAL SECURITY PROVISIONS, BUT IT WAS NOT INCUMBENT UPON THEM TO PAY FOR NEW INFRASTRUCTURE IN THE GDR. IN ALL THIS WE SHOULD BEAR IN MIND THAT THE POPULATION OF THE GDR WAS NO BIGGER THAN NORTH RHEINLAND/WESTPHALIA AND ITS ECONOMY WAS ONLY THE SIZE OF HESSEN.

4. WAIGEL STRESSED THE BENEFITS OF GEMU FOR OTHER COMMUNITY MEMBERS. THERE COULD BE INCREASED EXPORT OPPORTUNITIES. THE FRG TRADE SURPLUS WOULD BE REDUCED.

5. SARCINELLI (CHAIRMAN OF THE MONETARY COMMITTEE) WAS REASSURED THAT WAIGEL BELIEVED INTEREST RATES WOULD COME DOWN IN THE MEDIUM TERM. CHRISTOPHERSEN (COMMISSION) AGREED WITH WAIGEL'S ANALYSIS. THERE WOULD BE ADJUSTMENT PROBLEMS FOR THREE YEARS. IF INFLATIONARY PRESSURES LED TO AN INTEREST RATE RISE THAT WOULD CAUSE PROBLEMS FOR OTHERS. CARLI (ITALY) SAW BIG SHORT TERM PROBLEMS. THERE WAS A GREAT DEAL OF UNUSED PURCHASING POWER IN THE GDR. HE DOUBTED WHETHER MONETARY UNION WAS POSSIBLE WITHOUT FREEZING THIS. HE WAS PESSIMISTIC ON IMMIGRATION. IF WAGES REMAINED LOWER IN THE GDR MIGRATORY PRESSURES WOULD PERSIST. IF THERE WERE NO WAGE DIFFERENCES UNEMPLOYMENT WOULD RISE PRODUCING ITS OWN MIGRATORY PRESSURES. IF THE TRANSITION TO UNIFICATION HAPPENED QUICKLY INFLATIONARY PRESSURES WOULD BE UNAVOIDABLE. INTEREST RATES WERE BOUND TO RISE, AND THERE WOULD BE DANGERS FOR EMS STABILITY.

6. THE CHANCELLOR OF THE EXCHEQUER ASKED HOW THE FRG WOULD TACKLE INFLATION RESULTING FROM MONETARY UNION. WHAT WOULD THE COSTS OF GMU BE? IT WAS IMPORTANT THAT AFTER ITS ELECTIONS THE GDR ESTABLISHED A PRIVATE SECTOR ORIENTED ECONOMY WITH A REGULATORY FRAMEWORK BASED ON SINGLE MARKET LEGISLATION AND AVOIDED SUBSIDIES AND BARRIERS TO OUTSIDE FIRMS. BEREGOVOY (FRANCE), KOK (NETHERLANDS) AND KONTOGEORGIS (GREECE) AGREED THAT THERE WOULD BE INFLATIONARY PRESSURES IN THE SHORT TERM AND EXPRESSED FEARS ABOUT INTEREST RATES. KOK SUGGESTED AN INFORMAL DISCUSSION AT THE INFORMAL ECOFIN OF THE IMPLICATIONS OF GMU. REYNOLDS (PRESIDENCY) AGREED TO THIS.

7. DELORS (COMMISSION) RAISED THE IMPLICATIONS OF UNIFICATION FOR COMMUNITY LAW. MANY DIFFICULT QUESTIONS WOULD ARISE AS WITH AN ACCESSION E.G. ON THE WEIGHTING OF VOTES, BUDGET CONTRIBUTIONS,

NUMBER OF MEMBERS OF THE EUROPEAN PARLIAMENT, STATE AIDS AND THE IMPLEMENTATION OF INTERNAL MARKET MEASURES. EC COUNTRIES WOULD NOT ACCEPT UNFAIR COMPETITION. THERE WERE GREAT SENSITIVITIES AMONG MEMBER STATES ON THE RATIO OF THEIR BUDGET CONTRIBUTIONS TO RECEIPTS. THE COMMISSION WOULD PRODUCE A DISCUSSION PAPER LISTING THE PRACTICAL QUESTIONS THAT NEEDED TO BE ANSWERED. THIS MIGHT BE AVAILABLE FOR THE INFORMAL ECOFIN AT THE END OF MARCH.

8. IN RESPONSE TO OTHERS CONCERNS, WAIGEL SAID THAT IT WAS NOT HIS IMPRESSION THAT THE BUNDESBANK WOULD RAISE INTEREST RATES: ''NO IMMEDIATE PLANS ARE AFOOT''. HE DENIED THAT THERE WERE DANGERS FOR THE EMS. HE WOULD NOT BE DRAWN FURTHER ON THE COSTS OF AND TIMETABLE FOR MONETARY UNION. THE LATTER DEPENDED ON THE GDR. THERE WOULD NOT NECESSARILY BE A GREAT BOOST TO CONSUMPTION. HE HOPED EAST GERMANS WOULD INVEST IN SECURITIES AND NEW HOMES. ON IMMIGRATION, EAST GERMANS WOULD NOT RECEIVE ANY BENEFITS AFTER 18TH MARCH.

9. REYNOLDS ASKED IF HE SHOULD ANNOUNCE TO THE PRESS WAIGEL'S REASSURING REMARKS ON INTEREST RATES. WAIGEL THOUGHT THAT THIS WOULD BE UNWISE.

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