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MY TELNO 431 : GERMAN ECONOMIC AND MONETARY UNION

SUMMARY

1. DEBATE ABOUT THE EXCHANGE RATE FOR GEMU CONTINUES. NO DECISION YET.

DETAIL

2. THE PUBLIC DEBATE SPARKED OFF BY THE BUNDESBANK'S ANNOUNCEMENT IN FAVOUR OF EXCHANGING EAST MARKS FOR DEUTSCHMARKS AT 2:1 CONTINUES TO GET HEAVY COVERAGE IN THE WEST GERMAN PRESS.

3. THE FINANCIAL COMMUNITY (BUNDESBANK, MINISTRY OF FINANCE, MINISTRY OF ECONOMICS AND THE PROFESSIONAL ECONOMIC COMMENTATORS) REMAIN UNREPENTANTLY CONVINCED THAT A 1:1 EXCHANGE RATE WOULD BE A DISASTER FOR THE GDR. THEY BASE THIS BOTH ON THE UNEXPECTEDLY LARGE COMPANY DEBT IN THE GDR, WHICH WOULD HAVE TO BE SERVICED AT DM INTEREST RATES, AND ON THE CONTENTION THAT PRODUCTIVITY IN THE GDR IS LESS THAN HAD PREVIOUSLY BEEN ASSUMED AND WOULD NOT JUSTIFY EVEN PRESENT WAGE LEVELS CONVERTED AT PAR. THEY POINT OUT THAT PRICES AND WAGES CAN ADJUST THEMSELVES ACCORDING TO THE MARKET, INDEPENDENTLY OF THE EXCHANGE RATE. WAIGEL, TALKING TO COMMUNITY AMBASSADORS, INSISTED THAT IT WAS BETTER TO START FROM A LOW SALARY WHICH COULD RISE QUICKLY THAN WITH AN UNCOMPETITIVE SALARY LEVEL WHICH WOULD PROVOKE GREATER UNEMPLOYMENT. HE HAD PUBLICLY DENIED A SUGGESTION THAT HIS MINISTRY WERE PLANNING TO SUBSIDISE INCOMES TO THE TUNE OF DM 200 PER PERSON PER MONTH.

4. THE OPPOSING CAMP, COMPRISED OF THE FDP, LEFT WING CDU, AND THE TRADES UNIONS, ARGUE THAT A 1:1 EXCHANGE RATE IS ESSENTIAL TO MAKE GOOD OF THE COMMITMENT WHICH KOHL ALLEGEDLY GAVE DURING THE GDR ELECTION CAMPAIGN. (KOHL SAID THAT SMALL SAVINGS WOULD BE EXCHANGED 1:1 BUT DID NOT CORRECT THE WIDESPREAD IMPRESSION THAT THE EXCHANGE WOULD BE AT PAR ACROSS THE BOARD). THEY ARGUE THAT A 2:1 EXCHANGE RATE WOULD LEAVE WAGES AND PENSIONS BELOW SUBSISTENCE LEVEL. THEY ALSO CLAIM THAT THE BUNDESBANK'S PROPOSAL HAS BEEN REJECTED BY ALL SHADES OF POLITICAL OPINION IN THE GDR. THE SPD ARE PLEASED THAT THE

FEDERAL GOVERNMENT HAVE GOT THEMSELVES INTO A POLITICAL MESS AND ARE CLAIMING THAT THEY ALWAYS FAVOURED A MORE MEASURED APPROACH TO GEMU, IN WHICH THE CURRENCY EXCHANGE WOULD COME AFTER ECONOMIC REFORM.

5. FOLLOWING THE FIRST DISCUSSION OF THE BUNDESBANK RECOMMENDATION IN CABINET ON 4 APRIL, THE FEDERAL GOVERNMENT HAVE SAID THAT NO DECISION HAS BEEN TAKEN FOR THE MOMENT AND THAT FINAL OUTCOME MUST DEPEND ON NEGOTIATIONS WITH THE GDR GOVERNMENT WHEN IT IS FORMED. THE DILEMMA IS REAL: THE FEDERAL GOVERNMENT CANNOT OVER-RULE THE ADVICE OF THE FINANCIAL EXPERTS WITHOUT BRINGING UPON THEMSELVES THE CHARGE THAT THEY ARE FUELLING INFLATION AND KNOWINGLY CREATING THE WRONG CONDITIONS FOR ECONOMIC PROSPERITY IN THE GDR. THE BUNDESBANK IS BEGINNING TO PUT ITS FOOT DOWN PUBLICLY. SCHLESINGER HAS WARNED THAT AT 1:1 THE DANGER OF A WAGE/PRICE INFLATIONARY SPIRAL WOULD CAUSE THE BANK TO APPLY THE MONETARY BRAKES. ON THE OTHER HAND, IF THE FEDERAL GOVERNMENT IMPOSE AN EXCHANGE RATE OF 2:1 UPON THE GDR AGAINST THE EXPECTATIONS OF THE POPULATION, IT WILL STORE UP MASSIVE RESENTMENT AGAINST THE CDU, AND COULD HAVE EFFECTS IN THE GDR COMMUNAL ELECTIONS IN MAY, QUITE APART FROM IMPLICATIONS FOR ALL-GERMAN ELECTIONS IN DUE COURSE. RENEWED MIGRATION WOULD BE PROBABLE.

6. THERE IS SOME TALK OF THE 2:1 RATE ONLY BEING 'AN AVERAGE'. THIS SUGGESTS THAT THE FEDERAL GOVERNMENT MAY BE DEVISING A WAY THROUGH IN WHICH WAGES AND PENSIONS ARE TREATED DIFFERENTLY FROM CASH, SAVINGS AND DEBT, OR IN WHICH THE EXCHANGE RATE IS ACCOMPANIED BY SUBSIDIES OF VARIOUS KINDS, WAIGEL'S DENIALS NOTWITHSTANDING. THEY MAY ALSO RAISE THE CEILING FOR THE 1:1 EXCHANGE OF SMALL SAVINGS FROM THE DM2,000 PROPOSED BY THE BUNDESBANK TO SOME HIGHER FIGURE ACCEPTABLE TO THE GDR GOVERNMENT. LAMBSDORFF HAS SPOKEN OF MOST SMALL SAVERS HOLDING LESS THAN 5,000 MARKS, WHICH IS POSSIBLY AN INDICATION OF THE LEVEL WHICH THE FDP WILL BE LOOKING FOR.

7. IT IS NOT CLEAR YET WHETHER THESE DISAGREEMENTS WILL RESULT IN POSTPONEMENT OF THE 1 JULY TARGET DATE FOR COMPLETING PREPARATIONS FOR INTRODUCING GEMU (WAIGEL, AGAIN WITH COMMUNITY AMBASSADORS, POINTEDLY REFUSED TO CONFIRM IT). THE LONGER THE FEDERAL GOVERNMENT TAKES OVER ITS DECISIONS, THE WORSE ITS DIFFICULTIES ON THIS ISSUE ARE LIKELY TO GET.

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