COMMITTEE FOR THE STUDY OF ECONOMIC AND MONETARY UNION

15th December 1988

Meeting on 13th December 1988
(BIS, Room E)

Mr. E. Hoffmeyer (First tape 857 - 899)

There for the first time the word of subsidiarity appears on p. 5, the second to last indent, the last word. Of course, I understand your argument that you are using the principle of least resistance and that the requirements for the monetary system are rather strong, rather high. You put very strong demands on that, whereas on the fiscal side you introduce this principle of subsidiarity which means that you let the Heads of State get along with the impression that this can be managed in one way or another, whereas in the monetary field you have very strict rules. I think that it should be explained in a little more detail. Secondly, I think that when you then come to the conclusions, i.e. on p. 10 and the conclusions regarding fiscal policy on p. 14, we have to specify exactly what the requirements in the monetary field and in the fiscal field are. In the monetary field there are three requirements: firstly, according to what is described here, we have to have one currency, that means you have to abolish national currencies; secondly, you have to have one central bank, this means that you have to change all the national laws on central banks; and thirdly, you have to have decisions by majority. These are very strong requests on the various countries. When you look at what you really imply under the second field, i.e. fiscal policy, it is also very far-reaching because you have five points that I have found in the text. Firstly, you have to have a system for rules and budgetary policy, i.e. you have to have lines on the amount of deficit, we have to have this system, but more than that you have, secondly, to harmonise the welfare system and that is a very far-reaching thing, because that means, for instance, that unemployment, relief, etc. should be harmonised between countries. Thirdly, you have to harmonise the tax system - that is also here in the report. Fourthly, you have to harmonise the wage policy - that is also said here. Fifthly, you have to have a system of transfers. I think that even though you don't propose a formal system under this second point, you have to be very clear in the conclusions, you have to formulate these conclusions in five points, because this is very far-reaching and I don't think that when you mention it in various places in the text, when you summarise it to put it before the Heads of State how far-reaching these demands are. It is for clarification, because politicians often only read summaries! You have to be very clear about what the demands are.

Prof. N. Thygesen (1117 - 1138)

Mr. President, contrary to two people who have already spoken, I am happy with the balance of the report. Indeed, my main concern with it is that it makes the demands on other policies too stringent, rather more stringent than I think they are. I think there are three reasons why there has to be a certain imbalance between the monetary and economic parts of our report. Firstly, a principle of subsidiarity itself. In the monetary area, given some of the decisions that have already been taken, a degree of financial integration that we can foresee, a high degree of centralisation of decision-making is required to make for efficient policies. There are some arguments in favour of that centralisation, which do not apply to a similar degree to the fiscal area where both welfare considerations and allocative concerns dictate a much higher degree of national sovereign decision-making. So there is certainly a clear difference in degree between the different kinds of policies. The second reason is a simple one that this is a Committee, Governor Doyle referred to that, largely of central bankers and it would be strange if it did not emphasise primarily the area in which it has expertise. The third reason is, and that was touched upon by our President, that economic union is not in itself a very well defined concept, unless you begin to discuss it in the context of monetary union, then some things begin to emerge - the accompanying policies, requirements on other policies. For those three reasons I think there has to be a certain imbalance in the report and that discussion of the monetary union has to come before the economic union. I join Prof. Lamfalussy on that point.

M. J. de Larosière (1287 - 1300)

Mr. Chairman, to go along with Gov. Doyle, it seems to me that at the end of p. 5 we might add the following: "For the economic and monetary union form two integral parts of a single whole". I suppose Mr. Doyle will accept that. You could add: "it is for reasons of expositional clarity that in the following sections the distinction is drawn between them and that the first section is devoted to monetary union". But I would even go as far as adding - but the intertwining of these two concepts is so narrow that we we will have to be very precise in the rest of the report on the way to interlock parallel progress on those two matters, because if we do not do it the monetary union alone would break down. ...

Mr. M.F. Doyle (1301 - 1302)

Mr. Chairman, I had underlined the word "only" in the last sentence and put a question mark against it because that was what was bothering me.

M. J. de Larosière (1305 - 1318) (Interpretation)

Here Mr. Chairman I have a question on p. 6. We read at the beginning of the page: "A monetary union describes a single currency area, i.e. an area in which one money serves as a means of payment, unit of account and store of value ...". I wonder whether it would not also be true to say that a monetary union may allow for the coexistence of several national currencies whose relative parity values would be fixed and interconnected. It seems to me in other words that here, when thinking about the ultimate stage of monetary union, one over-emphasises this idea of the single currency, whereas it seems to me that even if one has several currencies closely interlinked one would have almost all the ? components of such a union. I have a little difficulty with this one-money concept.

M. A. Lamfalussy (1324 - 1336) (Interpretation)

Yes, I would like to emphasise this too. What is very interesting in this part is that it clearly shows that monetary union is not a finite whole, which once you have reached it no further progress is possible. In the first para. one ought to give this idea. In the ultimate stage of monetary union, of course, you are going to have a single money, but one should also indicate that one first has to go through a preliminary door, and this is represented by interlocking of the currencies and then further progress can be made and part of this section does describe the need for further progression, it is just a matter of presentation. No, it is not only a matter of presentation, but it means that you can deal with this concept of single money separately and that is very important. One might perhaps add the word "ultimately" - ultimately one money.

Dr. W.F. Duisenberg (1350 - 1371)

I have really the same point as M. de Larosière and therefore I think that this para. is a little bit too one-sided. Monetary union means I think two things: irrevocably locked exchange rates and one monetary policy. Those are the two elements. Irrevocably locked exchange rates can mean the transition to one currency, but it is not necessary, so it is a technical appearance and I think that has to be made clear, because the draft as it is now represents the introduction of one currency as an essential element and I don't think it is essential. Deriving from that it is a plea to already introduce a common currency, so to say to gain experience and to get used to it, and therefore if you say from the outset that it is not essential then you can also not place the emphasis on the necessity of introducing one currency. It may be thought by some advisable to do so, but it is not technically necessary. I think it is much more realistic to place more emphasis on increased policy co-ordination, intensified policy co-ordination, firstly, maybe by consensus and ultimately by decisions actually being taken, perhaps by majority decisions. But that is much more important, it seems to me, than what I regard as the gimmick to move to one currency in an early stage.

M. J. de Larosière (1394 - 1405) (Interpretation)

I rather agree with M. Boyer. We have to put the three Werner points to the top and then indicate that common policy will follow, because you cannot achieve these things without a common policy. The wording at the end of p. 6: "The essential macro-economic measures laying the foundations of a single currency ..." is not very good because it is very much more than laying the foundations - it already is monetary union. If you agree we could start by giving these three points of the Werner definition and then have this more flexible form of wording as to the possibility of ultimately reaching the single money. There will be other things that will have to be corrected, e.g. in p. 6: "Secondly, it requires the introduction of the policy which will eventually replace national currencies." This will have to be rephrased more conditionally in order to reflect what has emerged in this discussion here.

M. A. Lamfalussy (1405 - 1409) (Interpretation)

A single money is indispensable only if the interlocking of the exchange rates is not credible and one can say that this will not be entirely credible politically if there is no single money. But that comes later.

The Chairman (Second tape 000 - 31) (Interpretation)

From this morning's discussion I conclude that what we have at the top of p. 7 might be used as a wide definition of monetary union, that we shall attach more conditionality to this idea of single money. I would like us to say a word about the other two important points - apart from any other points you may have - one monetary policy and one exchange rate policy, the two major points in this chapter.

Mr. M. Boyer (280 - 327) (Interpretation)

Firstly, an editorial remark: "the result that the Community as a whole will be much less open". Here one runs the risk of giving the impression of the Community moving in such a direction as to establish fortress Europe and closing in on itself. I would suggest that we eliminate these words. Let us say simply that the Community will be less sensitive to outside financial shocks - it is just a matter of wording. A change in relations with the outside world is not a fact that one is more closed within oneself. Then the other remark about the advantages and drawbacks.

One ought to put this at the beginning, but after having given the definition- give the definition first, consequences for monetary policy and then advantages and drawbacks. As far as those are concerned, I think one might simply go back to literature, there is quite a lot that has been written about the pros and cons - in the report of Mr. Gros and Mr. Thygesen a great deal is said about the advantages and drawbacks. There is a decrease in uncertainties, a decrease in the cost of transactions, probably lower interest rates in each of our countries than if there were exchange risks. Then, and it is here that we get back to the single market, the competitive devaluations are eliminated, as a pre-condition in order to accept the rules of the game governing the single market. If you are going to go in for competitive devaluations then the single act won't work and then there is always more and more of a feeling of rejection against the inflationary model of devaluation. It is something that one agrees can be rejected. Those are the advantages. As for the drawbacks there is a problem of symmetry - I don't know whether we want to refer to it or not, perhaps, not in order not to complicate matters. This is a serious problem. The system is not in balance just now, but I am not going to belabour this point. The main drawback is the one that you find here. You do away with exchange rates which are an instrument for bringing back equilibrium. This would come after the definition and the advantages and drawbacks.

M. A. Lamfalussy (492 - 510) (Interpretation)

Perhaps I can try and explain what is meant here, or we could ask the rapporteurs. I read it as follows: monetary union, then there may be differences emerging between the regions for all kinds of reasons - structural, demographic reasons, etc. When you have balance-of-payments statistics which are kept regularly, you have two different currencies, you have the possibility of fluctuation, then these basic differences have a visible impact on statistics and on exchange rates and are therefore very fast indicators of an incipient disequilibrium. If on the other hand, you have a situation with a single money, where the balances of payments are calculated, or rather guessed at, a year or two after the event, as an indicator of disequilibrium you only have unemployment or the gradual grinding to a halt of economic activity in a region and it is a much slower indicator.

M. J. de Larosière (535 - 559) (Interpretation)

We can say that what disappears is the immediate constraint imposed by the exchange markets. But we also have to go into this matter of statistics in some depth. Contrary to Mr. Boyer, I doubt very much that you can record all transactions when they cross a border, because one is trying after all to cut through red tape and to do away with so much recording, and if you are going to do it again for statistical reasons, where is the advantage? Then, of course, you can reach a ridiculous level that has been reached in Belgium, where the Flemish and the Walloons are still arguing about their relative position as to the balance of payments. Nobody really knows - not even the Governor. The margin of uncertainty is so great as between Belgium and Luxembourg - no even worse between the Flemish and the Walloons. What about the United States? The argument about the two deficits may also one day concern one of the countries of the Community. To what extent would have that have an impact on the external position of the Community, etc. It will have an impact on the economic policy of the Community and we will have to talk about the trade deficit, etc. one cannot ignore all of these things. I don't think that it will be possible to do away with a discussion on balance of payments.

Mr. E. Hoffmeyer (610 - 619)

May I repeat on the summary question: could one follow the same presentation as on p. 7 where you have the Werner Report in three indents, saying: what is the summary, the summary is either locked exchange rates or one currency - that is one point. The second point is that we have to have one central bank, this means that we have to change the central bank acts of the various countries. The third point is that you have to have this decision-making procedure, probably by a majority. These three conclusions, I think should stand out explicitly.

The Chairman (647 - 692) (Interpretation)

Can we move on to economic union, the subject of all our concerns? What is the structure? Firstly, mention of the single market, dismounting of barriers, setting-up of a minimum of harmonisation and implementation of a European policy in respect of competition; secondly, one can no longer use exchange rate adjustments in order to offset disequilibria and then one moves onto what will have to be discussed in depth this afternoon - other economic measures. It is that which will have to be discussed. Firstly, co-ordination between fiscal policies. In theory the problem is well-known - what constraints, what consistency between budgetary guidelines and monetary guidelines, the system for financial transfers - we haven't gone very far there yet. I said earlier on what the package approved by the Community amounted to, but is that enough? It is not only a matter of financial transfers, but it is also a matter of how the resources are going to be used. Finally, the authors of the report thought, without perhaps being clear enough, that a European fiscal framework was necessary. Personally I translate this as follows: the major structures of compulsory withholding taxes of various kinds will have to be very similar in our various countries. If you look at tax levied on private income, corporate tax on wages and salaries, it will be very difficult to have an economic union if the differences are too great between our various countries, as at present. Hence, the Community authorities tried to come up with - not a uniform system - but a framework and the Community budget would then play the role of an instrument which would encourage or control. This will hopefully produce some answers to what was said at the beginning, namely that the economic union had to be described in as much detail as the monetary union. Mr. Thygesen said that we have invested a lot of work already in monetary union, there are vast volumes that deal with this, but we have very little about economic union, just a reminder of certain historical experiences - custom union, Zollverein - but those were very different in nature from what is being attempted here and aimed at very different objectives from those which have been defined in connection with the Single Act. This is something entirely new and different from the historical precedence.

Mr. M. Boyer (755 - 819) (Interpretation)

I think the problem of economic union cannot be tackled by examining all the aspects of the economic policy of a country or a group of countries, because we would lose our way. The most practical way of tackling this is to say, what are the instruments which should be used at the Community level and what are the instruments that can be used by the individual countries themselves? Countries with a discipline of more fixed exchange rates, I think that what can be done by the individual countries will be to handle very classical, conventional instruments of supply policy, their markets will have to become more flexible, they ought to be able to organise their expenses and their tax systems, taking into account the movement of labour and other resources in order to give incentives for saving, etc. Do you add the possibility that each country may still have a free hand in developing its territory, its land? That is very important, well yes it is not so important for us to recall the classical factors of development in each country, but there continue to be certain things that will fall to the countries and what we have to do in the report is to indicate what can be done at the Community level, since one will have given up the exchange rates. What will one be able to do at the Community level, in order to eliminate or reduce the differences between member countries? Monetary policy is eliminated, what is left is fiscal policy or the constraints will come from monetary aspects. I think that a central bank system will find it very difficult to give up the capability of saying the maximum deficit a country can accept is so much and for financing the deficit we will take this or that form. One will have to fix some limits to the deficit and to its funding, this being said there may be efforts at harmonisation. There the British position, which says let us do this not by agreeing on an initial compromise but let us let things move and let us see how these things will develop. Except for the harmonisation of tax levied on capital profits, the exchange rate discipline will apply considerable constraint on certain fiscal elements. A deficit must be fixed, its funding and what is left to the Community? Regional policy and the implementation of the 1992 package to the elimination of the movement of persons and capital, one accepts that this movement will take place and one wishes to facilitate it and what is left after that? Only regional policy. The whole of the economic policy that can be talked about at the end will be the Community's regional policy - we haven't discussed this because we need reports, documentation. Governor Doyle has given us a first report, ... additional report. The subject is very difficult. Funds will be limited in view of the fact that there is growing reticence to pay tax in various countries. There will be even less enthusiasm if the tax collected will go to a neighbouring country and one will have to find certain ideas as to how best to use limited funds in order to encourage growth. I don't think there is very much more to be said. There is monetary policy, you do without it. There is fiscal policy full of constraints, the only thing that is left is regional policy and there one will have to give a few ideas but they aren't so numerous.

M. J. de Larosière (1012 - 1034) (Interpretation)

A few ideas come to mind after this very interesting discussion. First idea: quite apart from structural problems, the economic and monetary union must not be subject to abuse or misuse, I should not imagine that this or that country may derive any undue advantages by abusing the others, for instance, applying no fiscal controls at all in order to get its citizens to benefit from better organised policies pursued elsewhere. It seems to me that the greatest protection against this happening will be guidelines in respect of fiscal policy. Then you have a second set of problems, these are the structural problems. One has to explain that if one removes the exchange rate instrument, those countries which structural difficulties, where productivity is less, if they are deprived of the exchange rate instrument this will mean additional problems for them. One has to explain why this is so, it is not very easy to explain this. Then one will have to explain that an appropriate long-term structural policy might help, perhaps, allowing a longer period of transition.

The Chairman (1034 - 1044) (Interpretation)

That is good, that makes for clarification. It is very much in line with what others have said. As President Pöhl said, in respect of Part III we shall have to be less technical and clearer and emphasise the basic ideas - the principle of subsidiarity, the fact that monetary union must certainly not benefit the least stringent, you need rules, and thirdly, there are countries with structural weaknesses and the single market enhances the risk of disequilibrium and you must combat this by means of appropriate policies. These are, perhaps, the three basic ideas.

The Chairman (1093 - 1115) (Interpretation)

We haven't. For the time being a subject to an indepth discussion as to the regional policies, by that we refer to everything that can be done at the Community level over and above efforts undertaken by the various countries in order to improve the infrastructure. If we don't discuss this now we will have to discuss this in January or February. As a key idea we retain in order to simplify the text here, after all you have said that this skeleton is too technical and the strong points, the basic ideas must appear more clearly. For this chapter I would suggest the following major ideas. Firstly, some countries will not be able to use the exchange rate instruments to correct disequilibria, therefore a certain discipline must be imposed on them in order to prevent them from relaxing their policies and then one must given them the means to improve their economic performance. This would be the basic thrust and then we will add information, once we will have had time to think about regional policy instruments. Nevertheless, the secretaries have posed another problem, for instance, the possibility of having a European Fiscal Framework. President Pöhl is still with us and I would like to make the most of this and move on to institutional aspects and should we have a Treaty or not, i.e. p. 14 onwards.

Herrn K.O. Pöhl (1368 - 1416)

In order to avoid misunderstandings, I want to explain a little more. Firstly, I fully agree with what has been said. I think any European central bank system has to be included in a framework, as has been said here in this skeleton, and I have no objections to using that as an introduction, that one has to see the European monetary institution as part of the European decision-making process, there is no doubt about that. As far as the Bundesbank law is concerned, Robin, it says that the Bundesbank has to support the economic policy of the Government as long as this does not conflict with its prior responsibility to safeguard the currency. The formulation is very vague. What I think we should avoid is to begin a discussion of all the details of a European central bank system. I think that has to be left to official inter-governmental negotiations, because that has to be a legal, binding Treaty and we can make recommendations, suggestions, and I am fully prepared if you want to go into more detail, point by point, I am open to that. But at this stage, and taking into account the political situation and several statements made by Prime Ministers, etc., I think it would be more realistic to say, if you want to have an economic and monetary union you have to be aware that that needs a certain legal and institutional framework. For economic union you have made this proposal for an economic policy centre, and I have not referred to that; as far as monetary union is concerned, you need the framework for a European central bank system. We cannot draft all the details of such a statute, but if you want to ask a group of experts to negotiate a statute for a European central bank system, and this is our recommendation to you, it should be done on the following lines. It should include the following features. That is my suggestion, if you think it is more advisable for all the reasons you mentioned to go more into detail, I am fully prepared to discuss that, but then we have to discuss it point by point and we will easily, very soon, reach a point where we recognise that we have very different conceptions on how such an institution should be organised, to whom it should report. For instance, if you say it should report to the Council of Ministers, I would never propose that, I would never subscribe to such a recommendation because it is not consistent with our basic philosophy in this area. I would have less problems if you could agree to say this institution should report to a committee of the European Parliament, for instance, something like the Federal Reserve System where the Chairman of the Fed has to report to Congress. In Germany I don't have to report either to the Government or to the Parliament, in other countries it is different. So that is a very very difficult question. Another question is, for instance, where should the seat of that institution be - should it be in London, Paris, Frankfurt, Luxembourg or where? We don't have to answer that question, we can't answer it, we don't have to answer it fortunately. It is a political decision. If we tell the Heads of State and governments, look, if you want the monetary union you will reach a point, and maybe you will reach it earlier than most people expected, where the exchange rates are rather inflexible maybe even locked, even irrevocably locked, and when you have that you need a central bank system and if you want a central bank system you have to answer this kind of question. I don't think we have to say more.

Mr. W. Duisenberg (1423 -1450)

I feel very attracted by this list of guiding principles as I see it, which should govern an eventual central bank or Federal central banking law. I work under a law which was proposed by a government and approved by parliament and not by the then also existing central bank, but of course the then existing central bank had some advisory role to play in it - that is maybe also our role. Ultimately, I have no illusion that the outcome, if there is an outcome, will be the outcome of negotiations between governments and approved in the present structure by national parliaments in Europe. That is one thing. On a few of the items here I would also need more time to study it. If I may make three comments. The fourth line, "a commitment to regulate the amount of money in circulation and of credit", that is the major goal for the central bank, as said here. In my bank law it says a commitment to stabilise the value of money and the value of money is both internal - price stability - and external - the exchange rate. Instruments to do that are regulating the amount of money that comes under the heading "instruments to achieve that goal". But the first goal, and this is also in the skeleton report, is price stability or more generally speaking the value of money: internally price stability, externally the exchange rate. Then there are various instruments to use. One instrument is not mentioned here and one could think of including that, that is the legal ownership and the task to manage the foreign currency reserves, or the foreign exchange reserves, of the Community - that is one thing one might want to add to leave no ambiguity there. My second point, which I would also want to add in this list of guiding principles, is that this federation of central banks or central bank should be charged with banking supervision at the Community level - that is one thing I would like to add. The last line - the seat of the institution - I would be inclined to say "comma Amsterdam"!!!!

Mr. E. Hoffmeyer (1451 - 1457)

I could agree on this, because I think it is much better than the skeleton report which I think is much too detailed. I think one should express very clearly that there are political decisions that have to be taken under these issues and then one could presume or mention that it would be natural for the Committee of Governors to be asked to fill out the basic political decisions that might be taken by the Heads of State.

Herrn K.O. Pöhl (1469 - 1484)

May I respond to that for a minute because that is such an important point. What I am saying, Jacques, is only that I myself will not recommend to the Council such a proposition. If there would be a political decision, I have to follow it, that is the only thing. I am not saying that you cannot envisage a European central bank system which has to report to the Council of Ministers; you can envisage a European central bank system which would be guided by the Council of Ministers - I wouldn't like it, but it can be envisaged. But this is not our decision, we cannot take that decision, we can make recommendations and I would not recommend it. I would say it should be independent. Frankly speaking I thought this list would be more acceptable to the group than the other one, because the other one looks very much like the Bundesbank law with this Council (... That is why I immediately said I preferred your version ...). What you said, Wim, on price stability, they said on p. 15 the "mandate of the system must be to maintain the stability of money as the prime objective of the Community's monetary policy". I like that language but it sounds very tutonic so I thought that I would make it a little more acceptable to the rest of the group. (... I would need non-inflationary growth, here ...) Maybe we should make it a little more stability oriented.

Mr. W. Duisenberg (1484 - 1488)

I have to publish, according to my law, an Annual Report to the shareholders - there is only one - but the shareholder does not have the right to approve or disapprove of it. He can only take note of it and that is some form of accountability.

M. A. Lamfalussy (1489 - 1501)

I think also that accountability somehow has to appear at the same time as independence in the monetary policy decision. Secondly, I think I wholeheartedly agree with Wim Duisenberg that the external function has to be put in somewhere, I am not quite sure how that will be handled because of course there you do not have the same kind of clearness of tradition of independence, but clearly you cannot bypass the whole question of the exchange rate role in the reserve holding exchange rate determination vis-à-vis the rest of the world. I think that has to appear and also again the prudential function, although that may or may not be watered down so that you could leave place for some sort of two-tier system, that also exists in some places. I think a central bank cannot be excluded from some sort of prudential responsibly.

The Chairman (1679 - 1708) (Interpretation)

Let us suppose that economic union, we boil this down to the points raised by Miguel Boyer, a centre for economic policy decisions would fix the fiscal constraints, would implement joint policies based on the Community budget and would define the policy mix, which already poses a problem of collusion with the monetary authority. But let us assume that this is what is done here. The question that then arises is is an ECOFIN Council of Ministers which meets 8 times a year in a position to accomplish this task in view of the way in which it operates? If this is not so, it will either hand over this responsibility to the European Commission or it will set up an appropriate body under its authority, under its aegis. Whatever the system used it will be accountable to the European Parliament. The European Parliament can bring to nothing the consistency between monetary and economic policies by rejecting the budget, for instance. It has joint decision powers as far as the budget is concerned and this is the problem. I think that the Council of Ministers of Finance, in view of the way in which it works, cannot play this role otherwise one would have to go beyond our mandate and tackle a more fundamental question. If more decisions are made at Community level, should there not be a Council of Ministers every 2 weeks at Brussels to make the decisions? If this is not so decided then one must give more power to the Commission so that, under the control of the Council of Ministers, it could play this role. It is very difficult to put this in writing, but that is the problem. Suddenly one finds that one goes beyond the mandate that was given us and starts thinking about the future of the Community institutions in the long term. Do we really wish to open that Pandora's box? With the risk of having the kind of discussion at a European summit that I am used to, where some Head of State starts talking about the beautiful future of the institutions and others get very annoyed. That is how the question is before us. One can of course think about this for a little longer.

Mr. M. Boyer (1708 - 1739) (Interpretation)

Mr. Chairman, I think that one ought perhaps look a little more closely at the type of decision that has to be made: every year the limits of fiscal deficits that each country could go to, how these deficits would be funded, and then the problem of fund transfer and the heading of regional policy. The limits to be imposed on fiscal deficits will derive from monetary policy considerations and it may very well be that recommendations emerge from the central bank system. To preserve exchange rates, etc., to control the growth of the money supply, central banks will in practice define that the limits should not be exceeded in terms of budget deficits. So I don't think that you need a body to meet once a year to talk about deficits and limits. This will be a by-product of the Community monetary policy, no, it is far more complicated than that. If one talks only about financial transfers, a country which is below the average in terms of GDP per capita, this country will receive transfers not only by virtue of the regional policy but other policies and also the common agricultural policy and the percentage may be 3, 4 or even 5% of GDP. Therefore there is a constitutional problem, because the European Parliament is party to the approval or not of the Community budget and even if it all boils down to the very simple things that you have mentioned, nevertheless, the convergence procedure must be strengthened because it is not working well. The convergence procedure is as though you celebrated High Mass while having lost your faith already. But there is the problem of fiscal deficit, compatible with monetary policy. Then there is the problem of the Community budget some of which will be used for regional transfers. An increase in the Community budget and the growing complexity of the Community budget will probably require a more elaborate system for the setting-up of this budget.

The Chairman (1826 - 1829) (Interpretation)

Let me put a question to you, do you want us to try to put in writing what I said earlier on, so that we would not have such a vague text but something which would be more outspoken? The centre for economic policy decisions would become a centre for the co-ordination of economic policies.

Mr. E. Hoffmeyer (1830 - 1840)

One should be very precise about what should be achieved and I think one could start with that. I mentioned five points on p. 14 and you can have other things, there should be for one thing a system of rules on budgetary policy, some kind of harmonisation of the welfare system, some kind of harmonisation of the tax system, some kind of harmonisation of cost policy and there should be a transfer system. If you start with that and say this has to be accomplished otherwise the monetary union cannot be achieved. The way in which you accomplish that is saying what the Heads of State may decide, institutional framework is not easy to prescribe. This I think is a fair position because it is hornet's nest, as you describe it, and it may then be better to leave it, but make it a condition that these things are accomplished - that I think is a major point.

Mr. J. de Larosière (1894 - 1915) (Interpretation)

I think we have to explain clearly in the report why it is essential to have in one way or another a centre where economic policy decisions are made at Community level. This has to be explained and if we do not explain this and a European central bank is set up then it is the central bank which will have to make decisions between nominal growth rates and real growth rates and will have to intervene through monetary policy. In this way its role will be too great and it will not be accepted politically, whatever the accountability that will be specified, because it will be an entity which is at a certain distance from the national parliaments and political authorities and this will be much more difficult than in the case of a national central bank. Therefore you need a centre where the overall macro-economic policies of the Community are worked out. There must be a centre which will ask itself what is the rate of growth we want to achieve, what is the kind of monetary stability that we want to have and what is the fiscal policy which, in view of what we know about the thrust of monetary policy, would ensure that we achieve these objectives? We have to tell the heads of state that we need some centre, some entity which does this - it could be the Council of Ministers if the Council of Ministers were a truly executive instance, but it may be an emanation of the Council of Ministers. But I would not immediately propose the setting-up of a centre. You have to proceed in a socratic manner, you must indicate that this responsibility must be shouldered by some entity. Normally it would be the Council of Ministers, can the Council of Ministers do this or not and move forward gradually or not?

M. J. de Larosière (2052 - End) (Interpretation)

My scenario is to be found under none of these headings, it is not on your page, Gov. Hoffmeyer, because what I was thinking of was this. The principle of an amendment of the Treaty is accepted, then one begins to negotiate and draft the new Treaty right from the start. The first step within that Treaty, one would need a scenario No. 6 to describe it, would be my embryo. So scenario 6 - embryo. First step: in a Treaty, negotiations for which would begin immediately. This being said my first step, be it linked to an amendment of the Treaty or not, for me one would need a new Treaty, but one could perhaps do this without amending the Treaty, well you would have to consult the legal experts. After all my scenario provides for the partial pooling of reserves and interventions, but one would have to see whether this is possible without amending the Treaty. Yes, I am quite certain but I am not certain that this is possible without amending national legislation. Since you have put the question to me I am going to tell you how it would work. An intervention fund would be set up whose purpose would be to intervene in third currencies. This would involve the pooling of 5 or 10% of the member countries reserves, the Fund would administer these pooled reserves and would intervene in the currency market under the conditions that govern concentrations. Concertation in other words, we are not trying upset the monetary policy of member countries in any way, we might even say that should there be conflict at the beginning between various central banks about an intervention, the fund would not intervene, it would move only once consensus had been reached. There would be a monetary analysis department in this Fund and this department should analyse money internally and externally and this would, one hopes, make it easier to arrive at a Community stance in respect of a rate of growth, growth of the money supply for the Community as whole. I think one could go further, in respect of preparing economic co-ordination, if one had this analysis department and if one limits oneself to exchanging information between central banks, each central bank, of course, being governed by its own objectives in regard of monetary policy. Then I describe what the structure of this think-tank on monetary analysis might be. There might be an executive committee on which one would have the Governors of central banks and then a management committee, which would be appointed by the Governors, selected by the Governors, which would be very small and which would look after the management of the two departments in this fund. It is very modest, as you can see. I thought that this would be a first step and would be part and parcel of the Treaty even if it does not acquire the dignity of entailing an amendment to the Treaty. I thought that it wouldn't be a bad thing to make a start in this way, make a start immediately negotiating the Treaty, drafting the Treaty, ratifying it as quickly as possible and the first step that would be taken would be described in some detail in the Treaty. The next steps of course being described in vaguer terms. I have produced a very short piece of paper to replace p. 31.

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To be quite clear, you have said in passing, participating central banks, to be quite frank, this would mean that certain seats would remain unfilled.

M. J. de Larosière

Yes, I already said that once. Yes, this would be open to everyone, be logical, for those who participate in the narrow band system of the EMS and who have accepted to pool part of their reserves.

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This monetary fund would have some of the competences delegated by central banks and would also have some of the instruments of central banks which would be reintegrated into the policy of central banks.

M. J. de Larosière

As I was saying in my note, this is not a dynamic movement which would push us to the very extremity of European construction, after all one hasn't pooled all the reserves of member countries within the IMF and I maintain that this can continue to be a modest embryo and will not necessarily grow and develop towards a single central bank. This is a reply to the irreversible nature of this change, it is not tantamount to putting your finger into a piece of machinery which will just drag you along. Even if we are not politicians we cannot ignore the political aspects. A great hope has been created, the Heads of State at Hannover have, after all in some way approved a monetary effort.... (End of Tape)

(Third tape: 000 - 25)

... If we draft the scenarios such as Scenarios 1 and 2, then I think it would be better to keep a low profile, especially as you are also the personal representatives of your heads of government and not only central bank governors, so you have to show the flat to some extent and I would like to start immediately, I suggested Scenario 5, drafting a Treaty which would be the first tangible proof of the fact that something is happening. I think that politically one must give something to heads of state of this menu, otherwise they are going to run the risk of remaining hungry.