

Dr. Wolfgang Rieke, c/o  
DEUTSCHE BUNDESBANK

FRANKFURT AM MAIN. 16. März 1989

Herrn  
Dr. G. Baer  
Assistant Manager  
Bank for International  
Settlements  
Centralbahnplatz 2

CH-4000 Basel

Lieber Herr Baer,

hiermit übersende ich Ihnen die Änderungsvorschläge zu dem  
WWU-Bericht in der Fassung CSEMU/12/89 vom 2. März 1989, die  
Präsident Pöhl Herrn Präsident Delors übermittelt hat.

Mit freundlichen Grüßen

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W. Rieke

KARL OTTO PÖHL  
PRÄSIDENT DER DEUTSCHEN BUNDESBANK

6 FRANKFURT AM MAIN  
WILHELM-EPSTEIN-STRASSE 14  
TELEFON 1581

March 16, 1989

Monsieur Jacques Delors  
President  
Commission of the  
European Communities  
200, rue de la Loi

B-1049 Brussels  
Belgium

Dear Mr. Chairman,

Following our meeting in Basle I enclose a number of proposals containing amendments to the draft report (CSEMU/12/88) which we discussed last Tuesday. I would strongly urge that these considerations be reflected in the new version of the report to be delivered by the end of this month.

These proposals are being sent directly to the Secretariat in Basle, too.

Sincerely yours,

*gez. K.O.P.*

Attachment

Karl Otto Pöhl

Frankfurt am Main, March 16, 1989

Draft Report on Economic and Monetary Union in the  
European Community (CSEMU/12/88, 2nd March 1989)

**Comments and proposals for changes**

Foreword, sub-para 2, first line:

Replace: "decision" by "request".

Foreword, sub-para 2, last line:

After "... members of the Committee" add "and do not commit the institutions they represent."

Foreword, sub-para 3, third but last line:

Replace: "will" by "could".

General remarks on the entire report:

Council Regulation No. 3180/78, as published in the Official Journal of the EC, L 379 of 30. December 1978, stipulates that "... the Fund's operations shall be expressed in a unit of account known as the ECU which is defined as the sum of ... amounts of the currencies of the Member States...". Consequently this unit should read 'ECU' instead 'ecu', thus reflecting the abbreviation of 'European Currency Unit'. Furthermore the ECU should be called 'unit' rather than 'currency', this latter expression being normally reserved for money which is legal tender.

Para 1, sub-para 2, first line:

Delete "institutional".

Para 2, sub-para 2:

Delete this sub-para.

Para 4, sub-para 1, sixth line:

Rephrase as follows: "... has greatly helped some participating countries ..." and add new sentence: "The exchange rate constraint may have made this more difficult for some other countries, e.g. low inflation countries like Germany."

Para 4, sub-para 1, last sentence:

Redraft as follows: "... economic factors have protected intra-European trade against excessive exchange-rate volatility."

Para 4, sub-para 2, sixth line:

Add after "managed": "..., especially by the increasingly close cooperation between central banks. The system has also benefited from the role assumed by the DMark as an "anchor" for participants' monetary and intervention policies."

Para 4:

Add new sub-para 3: "At the same time, the EMS has also suffered from a number of weaknesses, among them the lack of convergence of fiscal policies as reflected in large and persistent budget deficits in certain countries. This has remained a source of tensions and has put disproportionate burdens on monetary policy. Moreover, even after ten years of EMS one major EC-country, the United Kingdom remains outside the exchange rate mechanism, while Italy adheres to a wider (± 6 percent) fluctuation margin instead of the normal (± 2 percent) margin. The transition to the second stage of the EMS, as foreseen by the Resolution of the European Council adopted in 1978, has proved impossible."

Para 5, sub-para 1, last phrase:

Redraft as follows: "... the ecu has for a number of reasons played only a limited role in the operating mechanisms of the EMS. One reason is that compulsory intervention and the build-up of intervention balances to be settled in ECU has remained rather limited as central banks had increasing recourse to intra-marginal intervention involving the use of partner currencies, especially the DMark."

Para 5, sub-para 2, seventh line:

Rephrase first half sentence as follows: "Community institutions (e.g. EIB) have played an important role in promoting the use of the ECU as a denominator for their debt instruments, as have public authorities of certain Community members, but to an important extent the growing use of the ecu must also be attributed ..."

Para 5, sub-para 2:

Delete last sentence, since a recent opinion poll in Germany revealed no special interest in private use of the ECU.

Sections 3 and 4:

Preferably delete these sections, as they deal disproportionately with matters that are well known to Heads of State and Government.

Para 7, third line:

Delete "institutional".

Para 8, sub-para 2, thirteenth line:

Delete: "...was adopted within six months and which ...".

Para 11, sub-para 1, last line:

Add: "However, these benefits will accrue only if the single market remains open to competition within a global free trading system and avoids the creation of new barriers vis-à-vis third countries."

Para 11, sub-para 2:

Redraft from fourteenth line on as follows: "... thus necessitates much greater and durable convergence of economic policies and their results. To this end coordination of policies between separate national authorities needs to be intensified further and thus be made more effective. Freedom of capital movements and integrated financial markets would quickly translate incompatible national policies into exchange rate pressures, while at the same time putting increasing burdens on monetary policies and their coordination between central banks. The need for more intensive and effective policy coordination extends to all areas of national economic management which affect aggregate demand, prices and costs of productions, including monetary policy."

Para 12, fourth line:

Delete "in essence".

Para 12, third sentence:

Replace by: "While voluntary co-operation should be relied on as much as possible to arrive at increasingly convergent national policies, thus taking account of diverse constitutional situations in member countries, there is also likely to be a need for more binding procedures."

Para 13, sub-para 1, ninth line:

Redraft as follows: "... exercised at the Community and the national levels, in such manner as to guarantee a consistent economic management."

Para 15, third sentence:

Rephrase as follows: "Thus the impact of the internal market programme on growth in the Community could be further raised, if the removal of market barriers ....." (Delete reference to the Cecchini Report as estimates are highly tentative).

Para 16, sub-para 2, eighth line:

Redraft as follows: "... affecting domestic demand, prices and the cost of production as well as the structure of the economies if major regional disparities..."



Para 16, sub-para 2, eleventh line:

Redraft after "and monetary union." as follows: "The effects of this change could only be alleviated in an economic and monetary union if appropriate use is made of Community policies and of policy coordination. As external shocks would normally not affect the entire economy of a single member country, but rather manifest themselves in specific sectors throughout the Community, the appropriate remedial action would be in the form of structural policies instead of exchange rate changes. Sizable imbalances among Community countries could, however, emerge if individual countries embarked on incompatible policy courses, which would no longer be manifest in balance of payments problems but in regional employment and growth differentials. Reliance on ad hoc voluntary cooperation may not suffice to prevent such developments and a new set of rules, procedures and institutional arrangements that are characteristic of economic and monetary union is called for."

Para 17, last line:

Replace "examined" by "referred to".

Para 21, sub-para 3, tenth line:

Rephrase as follows: "However, given the impact that they might have on the overall domestic and external economic situation of the Community and their implications for the conduct of a common monetary policy, such decisions would have to be placed within an agreed macro-economic framework and be subject to binding rules which would avoid major differences between individual member countries in public sector borrowing requirements and put binding constraints on the financing of budget deficits."

Para 22, second line:

After "clear understanding" add "and acceptance."

Para 24, fourth line:

Delete "in principle".

Para 24, from third sentence:

Rephrase rest of para as follows: "A single currency would clearly demonstrate the irreversibility of the move to monetary union, considerably facilitate the monetary management of the Community and have much greater weight relative to other major currencies such as the US-Dollar, Yen etc. than any individual community currency. It is probably too early for a decision that the present ecu should develop into the future currency of the Community. The present basket ecu assumes the existence of its component currencies. Their disappearance would by definition also mean that the existing ecu would have to be replaced by a new abstract ecu at the time of transition to the common currency. In any case the transition would have to be made without discontinuity from the existing basket ecu if it were so decided. Adequate time would be required for economic agents to become acquainted with the new ecu and its characteristics."

Para 25, sub-para 1, twelfth line:

Replace "expansion" by "supply"

Para 25, sub-para 1, last sentence:

Rephrase as follows: "Firstly, agreement on a procedure for determining the Community's aggregate monetary policy; and secondly, instruments would have to be developed for the implementation of the common monetary policy at national levels."

Para 25, sub-para 2, second sentence:

Rephrase as follows: "Although a progressively intensified coordination of national monetary policies would in many respects have prepared the move to a single monetary policy, the implication of such a move would be far-reaching. Together with the permanent fixing of exchange rates it would deprive individual countries of the principal instrument available to correct economic imbalances and act independently in pursuit of national objectives, especially price stability. This loss would be most intensely felt by those countries that had retained some room for manoeuvre to pursue stability objectives under the less binding EMS rules."

Para 25:

Begin new sub-para in line 14 from below: "Even prior to the decision..."

Para 26, second sentence:

Rephrase as follows: "This would create a monetary union in which all national currencies became increasingly close substitutes for each other and might eventually be replaced by a sole community currency."

Para 26, last sentence:

Rephrase end of para as follows: "... of monetary integration, effective measures to enforce policies in non-monetary areas."

Para 28:

Delete this para as unnecessary to section.

Comment: The text also assumes partial harmonisation of national tax treatment, but nowhere in the text is there firm support for the idea that tax authority should be (partly, largely, in good part?) vested with the Community (i.e. a future European Parliament), as part of the needed degree of uniformity of fiscal policy, and in response to the need for built-in redistribution mechanisms to deal with the effects of regional imbalances (in place of otherwise unavoidable large-scale demands for fiscal transfers).

Para 29, sub-para 1:

Delete this subpara.

Para 29, sub-para 3, first line:

Replace "realignment" by "adjustment".

Para 29, sub-para 4, last sentence:

Redraft as follows: "Nonetheless, such imbalances if left uncorrected would manifest themselves as regional imbalances in the form of pressures on output and employment."

Para 29, sub-para 5

Delete first sentence and redraft second sentence and connect with preceding sub-para: "Measures designed to strengthen the mobility of factors of production would be one way to deal with such imbalances."

Para 31, last sentence:

Rephrase as follows: "The use of government subsidies to assist particular industries should be strictly circumscribed because they distort competition and cause inefficient use and allocation of scarce economic resources."

Para 32, sub-para 4:

Add new first sentence: "At the same time excessive reliance on financial assistance through regional and structural policies could cause tensions that need to be avoided. The principal objective ..."

Para 33, sub-para 1, second line:

Replace "in order to have" by "for".

Para 33, last sub-para:

Redraft as follows: "In the budgetary field binding rules are required that would, firstly, impose effective upper limits on budget deficits of individual member countries of the Community; secondly, exclude access to direct central bank credit and limit recourse to external borrowing, including borrowing in non-Community currencies. With a view to effective control and coordination of market borrowing by public entities at all levels, a 'public finance coordinating authority' consisting of representatives of all such entities should be established. One of its objectives would be to facilitate the conduct of a coherent mix of fiscal and monetary policies."

Para 34, sixth indent:

Rephrase as follows: "- effective and binding rules which would ensure a coherent macro-fiscal policy stance in the Community, exclude access to direct central bank credit and limit recourse to borrowing in third currencies."

Para 36, sub-para 1, last but one sentence:

Redraft as follows: "At the final stage the ESCB - acting through its Council - would be responsible for formulating and implementing monetary policy as well as managing the Community's exchange rate policy vis-à-vis third currencies."

Para 36, sub-para 2, first indent, first sentence:

Redraft as follows: "... at the Community level and its implementation at the national level, ..."

Para 36, sub-para 2, first indent, last sentence:

Rephrase as follows: "the System would have to regulate the amount of money in circulation and the volume of credit supplied by banks and other financial institutions with a view to safeguarding overall price stability;"

Para 36, sub-para 2, second indent:

Rephrase as follows: " - the System would participate in the co-ordination of banking supervision policies of the national supervisory authorities."

Para 37, sub-para 1, last sentence:

Redraft as follows: "The new Treaty would have to specify this adaptation and determine the areas where additional decision-making authority would have to be transferred from the national to the Community level."

Para 37, General criteria, end of first indent:

Redraft as follows: "... a similar allocation of responsibilities could be envisaged in the economic field by reserving the right to determine the broad lines of economic policy to the Council of Ministers, while the day-to-day execution of these policies would be in the hands of the Commission."

Para 37, General criteria, end of second indent:

Add a new indent:

"-in case of non-compliance by a member state the Commission would have the responsibility for taking effective action to assure compliance; the nature of such action would have to be explored."

Para 37, sub-para "Macro-economic policy":

Rephrase as follows: "The broad objective of economic policy coordination would be to promote growth, employment and external balance in an environment of price stability. For this purpose co-ordination would involve defining a medium-term framework for budgetary policy within the economic and monetary union; managing common policies with a view to structural and regional development; determining, in close consultation with the ESCB Council, the Community's exchange rate policy; and participation in policy coordination at the international level.

New procedures required for this purpose would have to strike a balance between reliance of binding rules where necessary to ensure effective implementation and discretionary co-ordination adapted to particular situations.

In particular it would seem necessary to develop procedures and binding rules for budgetary policy, involving

- the definition of the overall stance of fiscal policy over the medium-term, including the size and financing of aggregate budgetary positions in the Community;
- strict limitations on public borrowing, e.g. related to public investment requirements;
- exclusion of access to central bank credit and other monetary financing;
- strict limitation of borrowing in non-Community countries."



Para 38:

Rephrase as follows: "The new Treaty laying down the objectives, features, requirements, procedures and organs of the economic and monetary union would add to the existing community institutions (European Council, Council of Ministers, European Parliament, Commission and Court of Justice) a new institution of comparable status, the European System of Central Banks. With due respect for the independent status of the ESCB, as defined elsewhere in this Report, appropriate consultation procedures will have to be set up to allow for effective co-ordination between budgetary and monetary policy. To this end, attendance by the President of the Council and the President of the Commission of meetings of the ESCB Council, without power to vote or to block decisions taken in accordance with the rules layed down by the ESCB Council, should be provided for. Equally, attendance by the Chairman of the ESCB Council meetings of the Council of Ministers should be provided for, especially on matters relating to budgetary and other policies of relevance to the conduct of monetary policy. Consideration would have to be given to the role of the European Parliament especially in relation to the authority evolving on the Commission in budgetary matters, where the latter should be accountable to the European Parliament. The same should apply in regard to action, or non-action, taken by the Commission in response to non-compliance of a member country with binding rules or decisions especially in the budgetary field."

Para 44, sub-para 1, sixth line:

Delete "...their economic behaviour..."

Para 44, sub-para 1, last line:

Insert after "the course of action": "and its timing".

Para 46:

Redraft last sentence: "In essence, parallelism would have to be maintained in the medium-term, but also before proceeding from one stage to the next."

Para 47, last three sentences:

Redraft as follows: "There should be a clear indication of the timing of the first stage. It could begin with the entry into force of the Directive for the full liberalisation of capital movements on 1st July 1990, [subject to full participation of all original EMS members in the exchange rate mechanism]. The second stage could begin with the entry into force of a new Treaty. The Treaty would be negotiated in accordance with a time schedule to be decided upon in the light of progress made in the first stage towards completion of the internal market and the creation of a zone of internal and external stability comprising all Community members."

Para 48, sub-para 2, third line:

Replace "formulated" by "decided".

Para 48, sub-para 3, last sentence:

Delete "... and common decision-making".

Para 48:

Add at end of last sub-para: "However, already in the first stage, a significant strengthening of coordination procedures in the economic field must be established with recommendations formulated collectively and reports evaluating progress in major economic areas."

Para 50, sub-para 2, two last sentences:

Redraft to become new para 51: "As a consequence, one approach would be to provide for new concrete steps towards economic and monetary union that would initially be confined to measures designed to strengthen co-operation, mutual surveillance, analysis of current developments and prospects, and non-binding coordination of policies until such time when preparation and ratification of a new Treaty is considered appropriate. In the monetary field, the Committee of Central Bank Governors should be called upon to proceed accordingly; in the economic field, the existing Community institutions would be instructed likewise. A new Directive by the Council would define the objectives to be pursued and the detailed steps to be taken without institutional change.

Para 51:

Replace "One" by "Another".

Para 52, second phrase:

Rephrase as follows: "Such a Treaty would indicate the procedures by which ..."

Para 53:

Delete from "The Committee ..." to end of sub-para. Connect second sub-para with first sentence of section.

Remarks on this para:

1. References to artificial support of the ecu should be eliminated.
2. Discussion of the role of the official ecu should reflect the fact that the volume of ecu transactions among central banks depends on the volume of intervention and settlement operations.
3. Use of the ecu in the context of a common monetary policy is subject to serious reservations of a conceptual and practical nature, which suggest that reference to such a role should be deleted.

Para 54:

Redraft as follows: "Firstly, the Committee was of the opinion that a monetary union does not necessarily require a single currency. However, political and psychological reasons suggest that a single currency would be a desirable feature of a monetary union. A declaration that the ecu properly defined should assume the role of the future single currency of the Community could be made at the outset in order to assure private agents that there would be no discontinuity between the present ecu and the single currency of the union and that ecu obligations would be payable at face value in ecu if the transition to the single currency had been made at the time of the maturity of the contract. But it was also felt that such a declaration might better be left for a time considerably closer to the birth of the common currency."

Para 56:

See remarks on para 53.

Para 57:

See remarks on para 53.

Para 58:

In fourth and fifth line delete "institutional".

Para 59:

Redraft: "The first stage would encompass a clear and convincing political endorsement of the final objective of economic and monetary union. It would, moreover, provide for

- closer coordination of monetary policy by central banks, taking due account of the effects of the complete liberalisation of capital movements by mid-1990, through the adoption of appropriate procedures by the Committee of Central Bank Governors;
- closer cooperation in the area of exchange market intervention, taking account of their implications for the effectiveness of monetary policy in individual countries;
- strengthened coordination of economic policies conducted at national and community levels, taking account of the requirements of growing economic integration, and based on a revision of the procedure layed down in the 1974 Decision om convergence."

Para 59, last sub-para:

Delete this sub-para and replace by section dealing with follow-up procedure at end of Report.

Para 60, first line:

Rephrase as follows: "... when the new Treaty..."

Para 62:

Redraft as follows: "... for the Single European Act at a time to be decided in the light of progress made in the integration process in stage one." Delete second sentence.

Para 64, third sub-para:

Rephrase as follows: "Secondly, all Community currencies should be included in the EMS exchange rate mechanism."

Para 64, fourth sub-para (beginning with "Thirdly"):

Delete this indent, as elimination of certain national safeguards of the exclusive role of the domestic currency for specific purposes (e.g. legal tender) would constitute an institutional change not covered by stage one.

Para 64, sub-para 5, first sentence:

Delete second half of sentence, beginning with "... and making it ...".

Para 64, sub-para 5, first indent:

Redraft as follows:

"- formulate opinions on the overall orientation of monetary and exchange rate policy ... and credit targets."

Delete last sentence beginning: "In the event of ..."

Para 64, sub-para 6, second sentence:

Delete from: "In order to reinforce ..." to end of para.

Para 66, sub-para 1, fourth indent:

Rephrase as follows:

"- these members consider it essential that intervention should be coordinated wherever necessary to ensure its effectiveness, not the techniques of common intervention; such co-ordination can provide the necessary training ground while avoiding the unnecessary complications caused by instituting an additional intervention window."

Para 66, sub-para 2:

Delete this sub-para beginning with: "However, the Committee members ..."

Para 68, sub-para 1:

Rephrase as follows: "In the economic field the Council, the Commission and the European Parliament would be empowered to reinforce their action ..."

Para 68, sub-para 4, second indent:

Add after "... their financing;": "the Commission should have the responsibility to bring before the Council any non-compliance by member states and should propose action as necessary."

Para 69, sub-para 3:

Delete from: "In addition, ..." to end of para."

Para 69, sub-para 3:

Delete to end of para."

Para 71, fourth sub-para:

Rephrase as follows: "In particular, the Council of Ministers and the Commission, under the control of the European Parliament, would have the authority ..."

Add new section "8. Follow-up procedure on Treaty change".

Para 73

Based on this Report the following follow-up procedure is suggested: The Council and the Committee of Central Bank Governors are invited to take the necessary action to implement the first stage [coinciding with the entry into force of the Decision on the full liberalisation of capital movements on 1st July 1990] [and subject to the full participation of all original members of the EMS in the exchange rate mechanism without recourse to special regimes].

Para 74

Upon entry into force of the first stage the competent Community bodies are invited to work out concrete proposals based on this Report, for a second and final stage of EMU. These would serve as a basis for negotiations on a new Treaty in an inter-governmental conference to be called by the European Council.

Para 75

The decision on the entry into force of a new Treaty would be taken in the light of progress made in the first stage towards the completion of the internal market program and the creation of a zone of internal and external monetary stability comprising all member countries of the Community.