Memorandum from the Commission to the Council on the problems raised by the present monetary situation (10 september 1971)

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1. The measures taken on 15 August by the United States Government have created an international crisis which will be felt far beyond the bounds of economic, commercial and monetary policy.

The task which must now be fulfilled consists in particular of rebuilding an international and monetary system on the foundation of the institutions which have managed it hitherto (IMF and GATT) and taking into account the needs of the developing countries, which are likely to be the main victims of the present disruptions.

The Commission considers that we shall be far more successful in attaining this objective if the Community, in close collaboration with the countries seeking membership, pursues with resolution and coherence the establishment of economic and monetary union, which is necessary not only for its own development but also for a better balance in internationally economic relations.

Convinced that the Community can play an essential role in the major international meetings which will be seeking solutions to the monetary problems to be solved, the Commission feels it must submit to the Council its views on the existing situation.

2. The Commission has noted with interest the exchanges of views which were held within the Monetary Committee and the Committee of Governors of Central Banks on reform of the international monetary system. It thinks that they can provide a useful contribution in drawing up a joint position within the Group of Ten and the IMF.

In this connection it would like to make the following remarks:

(a) A satisfactory balance will be restored to international payments relations only if there is a realignment of the parity relationships between the currencies of the industrialized countries.

This realignment should involve the currencies of all the countries concerned, including the dollar; it should be carried out in conditions which ensure that the burden of readjustment is shared out in the light of the relative economic positions of these countries.

In this context, the commercial measures taken by the United States - on which the commission reserves the right to submit to the Council proposals for a Community position - introduce an element of uncertainty in the assessment of the relative competitive capacities of the economies. The abolition of these measures would be a useful contribution to solving the problem of realigning parities.

The new equilibrium in international payments will be maintained only if, in future, all countries or organized groupings of countries without exception respect the obligations and requirements of the process of adjusting the balance of payments and implement the appropriate domestic policies.

(b) The reforms to be carried out in the international monetary system must respect the principle of fixed parities, as this is necessary for the security of financial operations and the growth of trade, both of which are matters of particular interest to the Community in its position of the world's foremost trading unit.

However, the smooth functioning of a system of fixed parities requires that measures be taken to deal with international movements of capital. There are some major deficiencies in the Bretton Woods Agreements on this point. These deficiencies could be made up by action along two lines: a slight widening of fluctuation margins to offset the effect of capital movements brought about by differences in interest rates, and an effective regulation of the flows of short-term capital, as these are a source of instability.

(c) International liquidities will still be made up of gold and, increasingly, of reserve instruments created and managed at international level; this implies adjustment and extension of the system of special drawing rights. A gradual rundown of the reserve role played by national currencies must therefore be organized.

This opportunity should be seized so that the authority of the IMF can be enhanced and its possibilities of action reinforced wherever it exercises powers and so that steps may be taken to ensure that the Community can act as a Community in this institution.

3. The existing monetary difficulties are unquestionably a source of danger for the Community. The common agricultural policy is affected by them: even if trade has not been interrupted at present, the single market no longer exists. Progress towards economic and monetary union is at a standstill. There is a danger that the process which, for the last 15 years, has ensured the expansion of the common market may no longer appear to be irreversible. These dangers could only grow worse if the present situation continued for too long.

This is why the Commission has since 9 May 1971 been endeavouring in the Council and in the Conference of Ministers of Finance to bring the positions of the Member States closer together. It is also why it on 19 August last endorsed the formula suggested by the Monetary Committee for harmonizing exchange arrangements within the Community.

The Commission does not, of course-as the fixing of new parity relationships between the currencies of the Member States cannot at present be envisaged-underestimate the difficulties which are raised by the choice of an interim system that could limit the drawbacks which the Community faces because of the present situation.

It feels, however, that the Member States could come to an agreement on a formula which would be based on the principles which it put forward at the Council meeting on 19 August 1971:

(a) Establishment of fixed and realistic exchange rates to be agreed on between the member countries, without prejudice to the official parities;

(b) Introduction of a certain flexibility in exchange rates for operations with non-member countries, in particular by a slight widening of fluctuation margins, the size of which would still remain to be determined; the effective rates for the Community currencies should not deviate from the agreed rates by more than 1.5 %, a, margin which would be gradually reduced in accordance with the Council resolution of 22 March 1971 on economic and monetary union;

(c) Application by all Member States of effective measures to establish a concerted policy against excessive capital inflows and to limit their effects on internal liquidity;

(d) Concerted intervention by central banks on the exchange markets, to be carried out increasingly in Community currencies till such time as the Community possesses an autonomously fixed unit of account, the functions of which would be gradually enlarged;

(e) Institution of a mechanism that will bring about financial solidarity leading to the European fund monetary cooperation provided for in the Council resolution of 22 March 1971.

4. The Commission hopes that the Council will accept the points set out in Section 2 of this memorandum as the basis of the joint position to be adopted by the Member States in the Group of Ten and the IMF.

With regard to Section 3, the Commission requests the Council to confirm the instruction given on 19 August 1971 to the Monetary Committee and the Committee of Governors of Central Banks, under which they are to seek methods for stabilizing exchange relations between the Member States and to report back as early as possible.