Note from the President of the EC Commission on the prospect of monetary union (La Roche-en-Ardenne, 16–18 September 1977)

Caption: At a reflection meeting of the Commission of the European Communities held from 16 to 18 September 1977, the President of the EC Commission presents a note on the prospect of monetary union in Europe.

Source: Meeting of the Commission at La Roche-en-Ardenne. The prospect of monetary union. Commission President. [online]. Brussels: Commission of the European Communities, 16–18 September 1977 [accessed 29 May 2012]. Available on: http://ec.europa.eu/economy_finance/emu_history/documentation/chapter9/19770916en19prospectmonetunion.pdf.

Copyright: (c) European Union, 1995-2014

URL: http://www.cvce.eu/obj/note_from_the_president_of_the_ec_commission_on_the_prospect_of_monetary_union_la_roche_en_ardenne_16_18_september_1977-en-28a25e64-8865-4ef7-9e3f-d77b69d28431.html

Last updated: 20/10/2014

COMMISSION
OF THE
[EUROP]EAN COMMUNITIES

[Offi]ce of the President

UEM

MEETING OF THE COMMISSION AT LA ROCHE-EN-ARDENNE

16-18 SEPTEMBER 1977

THE PROSPECT OF MONETARY UNION

(note distributed by the President)

The President indicated in the early discussions about the meeting of the Commission at La Roche-en-Ardenne that he might circulate a paper on monetary union. Attached is a draft prepared by the President's Cabinet which complements M. Ortoli's paper "Eléments de Réflexion sur l'Union Economique et Monétaire" (SEC(77)3125).

While M. Ortoli's paper surveys a broad range of possible developments in Community policy with special reference to the next five years, the present paper looks more at the merits of the case for monetary union as it now appears in the light of recent economic developments.

[Post]al address: Rue de la Loi 200 B 1049 Brussels - Telephone 735 00 40/735 80 40 - Telegraphic address: "COMEUR Brussels" - Telex 21877 COMEU B"

THE PROSPECT OF MONETARY UNION

Contents

1. What monetary union consists of

2. Failure of the Werner Plan

3. The case for monetary union - in principle

   (i) the small country case

   (ii) the large country case

4. The case for monetary union - applied to the Community

   (i) inflation

   (ii) exchange rate, balance of payments and international financial policy

   (iii) employment

   (iv) living standards

5. Summary and conclusion

Annex: attitudes to monetary union

THE PROSPECT OF MONETARY UNION

1. What monetary union consists of: a common currency, and a single apparatus of control over note issue and money creation by banks, including in practise the main instruments of monetary policy affecting interests rates, credit expansion and exchange rate and international financial policy*.

It may be asked whether less centralist concepts of monetary union are possible. Is the U.S. federal reserve system not a federative monetary system? Do not some monetary unions have more than one money (B/Lux, England and Scotland for that matter?). The answers here are basically no; monetary policy cannot be shared. In the final analysis some single authority has to decide how money supply should grow, and whether the exchange rate is to be supported. The U.S. reserve district authorities have little more power than the regional offices of the Bank of France in monetary policy (the U.S. reserve districts are mainly important for bank supervision). The Luxembourg note issue is constrained to a fixed proportion of Belgium's, which is little different to the Scottish bank note's status. This is only cosmetic monetary independence. (Ireland maintains a fixed exchange rate with the U.K. with the aid of massive official reserves and a very conservative central bank policy as regards taking Irish Government debt; but the U.K./Irl is not a monetary union).

It may also be asked whether other kinds of gradualistic or partial approaches to monetary union are possible, the 'snake' being a shell-shocked example. The thesis here argued is again basically no (excepting the small country special case - see more below) and certainly not in the sense that budgetary power may be split between two, three or even four tiers of general government in widely different degrees, and adjusted in percentage share year by year (e.g. Germany in fact frequently adjusts the split of VAT revenues between Bund and Länder to reflect the changing pattern of spending by each). One may pass years contemplating the prospects of monetary union, and preparing psychologically by going through economic policy coordinating procedures (as now), but a decision is basically required whether or not to jump in at

../..

*For basic texts see Max Corden (1) and (2).

the deep end. The proposition of monetary union is comparable in importance to forming a common defense authority. In constitutional terms either entail going over the threshold of confederation; it is significant that both defense and monetary unions almost always go together (for small states the free-rider phenomenum in defense is analogous to the small satellite state in a monetary union). Monetary union would entail a transfer of power bigger than the whole of the Community's existing competences put together. Some monetary economists have recently been promoting ingenious schemes for a European parallel currency as a gradualistic approach to European monetary union, and some people in the Commission argue that the new unit of account ought to grow into this function. But this a phoney proposition so far as the crucial issues of monetary union are concerned *. If the parallel currency became a significant part of the money of some countries it would still have to be controlled by a monetary authority. But the intermediate stage where, say, half a country's money supply and price and wage contracts were in Euro money and half in the old national currency would be quite chaotic. This would be not far removed from allowing the Euro-dollar market open access to the internal money markets of Member States, but where the European monetary authority was seeking to control banks' Euro money activities alongside national banks controlling national money transactions. The new unit of account may usefully be given a fair number of functions (budget, borrowing etc.) but it cannot pretend to a large-scale monetary role without raising the crunch issues posed by monetary union (who is to be the monetary authority?).

2. Failure of the Werner Plan

Monetary union is at the moment a widely discredited concept in Europe. This is because the Community set itself a programme to be completed by 1980, which shortly after its adoption in 1972 was in ruins. Why? For three reasons. **

(i) The programme led with exchange rate action. The 4% IMF margins were narrowed to 2 1/2% as a precursor to a final locking of exchange rates and, eventually, installation of a new money. To be kind to its authors, the Werner Plan failed because the first stage coincided with

---

* See Max Corden who calls this proposal a 'brilliant non-starter' (2), p.16

** See Marjolin Report (3)

the break-up of the fixed exchange rate system, a too unsettled monetary environment.

(ii) But the authors also underestimated the fiscal redistributive and regional policy role that would seem to be a major and necessary condition for the viability of monetary union for the Community as a whole *. The Italian member of the Werner Plan group argued that without this Italy stood to be impoverished. He was not listened to. Germany argued that inflation discipline was the preventive medicine. The Benelux countries were influenced by their small country bias which makes monetary union more easily an attractive position (see further below).

(iii) Member States took no major step of an institutional kind towards transferring economic policy powers to the Community. It may be doubted whether they were really prepared to do so. Rather they thought or pretended that the non-mandatory coordination of economic policies would lead Member States along a path of natural convergence of economic performance and interest. They would move by osmosis towards monetary union, and only at a late stage would governments have to face up the crunch decisions on institutional powers and on what the economic policy should actually be.

The remnants of this largely discredited doctrine still inspires (or haunts) the Community in all its various coordination and convergence procedures. But Member States are not sufficiently prepared or able to adjust their political preferences and change their economic behaviour now in order to move towards a common normative Community standard in the interests of a distant and vague Community objective. We see this at the moment, with Germany having been long hesitating over reflation with its inflation rate comfortably down to 3 1/2% to 4%, while France and the U.K. are more tempted to start reflating before having mastered their inflation problems.

The lesson therefore is that voluntary convergence in the early stages of a gradualistic approach to economic and monetary union is on the whole not working, despite the strong efforts by France and the Benelux countries to keep up with Germany.

../..

* See MacDougall Group Report (4).

It is significant that another gradualistic scheme, the Duisenberg proposal from bringing'snake'and'non-snake' currencies together into a more orderly exchange rate system was not taken seriously by the larger Member States. This is recognition that proposals for further monetary integration which do not entail changing the institutional system in fundamental ways have little hope of standing up to the forces at work in today's international monetary environment. The bull has to be taken by the horns. The big step changes - creating a common monetary authority, vastly expanding the regional and redistributive fiscal powers of the Community - will have to be imminent or actually taken before the unconstrained behaviour of national goverments, their businesses and trade unions, is to be seriously changed in the ways that would become necessary in a monetary union.

3. The case for monetary union - in principle

(i) The small country case.

Why do small countries tend to gravitate into the monetary orbit of large neighbouring countries? This may seem to be a secondary question, since the main European problem is one of sticking together several medium-sized countries rather than bringing in the small countries; but it serves illustrative purposes for the main argument. There are two separate reasons. The first reason is that when a small country has massive, competitive trade relations with a large state, its business interests cannot afford to get out of line with the cost and price performance of the neighbour, either in terms of day to day reality, or in terms of medium to long run expectations. This is a situation in which the effectiveness of exchange rate changes to redress an uncompetitive situation is much impaired. The vicious circle of importing inflation through exchange rate depreciation becomes very high-powered, and in addition there will probably be tendencies towards wage parity bargaining across frontiers. These are the circumstances behind the theory of the 'optimal currency area'. The economic advantages of monetary independence are small and are outweighed by the gains from additional industrial productivity, trade and commerce that accrue in the monetary - plus - customs union beyond those obtained by a customs union alone. The small

country therefore stands to benefit by giving up its largely ineffective degree of monetary policy independence to a dominant neighbour. The second reason is that the small country may benefit from a lower inflation rate by accepting the disciplines of associating with a large stable neighbour. This compensates for the incapacity of a small and very open economy to have an effective stabilisation policy of its own. The 'snake' countries are influenced by both these reasons in their association with Germany, although Germany's stability is somewhat too stringent for the rest to follow entirely; thus the 'snake' is a long way off being a monetary union, and the small countries tend to devalue quite often by small amounts against the DM. In the UK/IRL case, the first reason (importance of trade relations) still keeps the Irish pound with sterling but the second reason (inflation performance of the dominant economy) has been an unfavourable factor in recent years, which is why Irish economists and politicians have been considering breaking with sterling (but with the sterling's present strength this idea is in abeyance).

(ii) The large country case

For larger countries the benefits of joining a monetary union are certainly less straightforward than for the small country case - although not necessarily insufficient or negative. The large countries' trade interdependence is less, the imported inflation problem is less acute, wage parity bargaining across countries may work less strongly (although it may still arise - e.g. in U.K. car workers' present pay negotiations), and the impact of exchange rate changes on competitivity, employment and the balance of payments is greater. Their ability to conduct effective independent monetary and demand management policies should be greater, but may nonetheless, at least for medium-sized European countries nowadays, be pretty weak and in need of drastic improvement.

These are all differences of degree, rather than of absolute character, in making monetary union less obviously attractive to large countries, compared to a small one alongside a large one. A small inner core of highly integrated states may well be an easily viable currency area but sub-optimal. The 'optimal currency area' is formed as other states, with sufficient common interests for the

../..

process of extending membership to yield further benefits still are added for the club. However, different kinds of benefits may also now be brought into account to make the monetary union sufficiently attractive on balance for the marginal states, the hesitant or sceptical candidates.

These advantages may be:

- of a fiscal nature, with budget transfers improving the living standards of poorer states and their economic capacity (through regional grants, subsidies for infrastructure, etc.)
- of a political nature, with monetary union acting as a vital part of the hard core to a political union with a minimum degree of centralised authority.

To summarise, the prospect of monetary union must be judged on the basis of four main factors weighing in the balance:

Specialisation?

(1) the chances of improving living standards by achieving a more efficient industrial structure and more intensive trade and commerce than in a customs union alone;

(2) the chances of improving the effectiveness of macroeconomic policy - i.e. handling inflation, employment and the balance of payments more successfully (which also stands to affect living standards but indirectly).

(3) fiscal redistribution, some paying others gaining;

(4) political integration, some seeing this as more valuable than others.

4. The case for monetary union - applied to the Community

All this being strong stuff in principle, one has to try to say more concretely how the main preoccupations of our Member States would be affected as a result of forming a monetary union.

In part this is like answering the question: 'How could Europe benefit from a common defense force?'. Unified policy would be more powerful, the weapons (instruments of policy) would be more efficient, but it would also crucially depend on the authority's political motivation, and the circumstances

../..

to which it found itself compelled to react. So the following account of the consequences of monetary union are in part intrinsic to monetary union as a necessary consequence, and in part the possible outcome of a selected policy.

(i) Inflation

One thing would necessarily follow. First and foremost a common rate of price increase would be established. Would it be a high rate or a low rate? The monetarist debate has now sufficiently progressed that one could envisage the European monetary authority declaring a target of Euro money supply increase of say 8 to 9%, and controlling note issue and bank money creation accordingly. This would be a golden opportunity to make a clear break in the inflationary psychology and habits of the U.K., Italy, France, etc. The prospect of European stabilisation policy being led by a fairly hard-line central bank is quite a plausible and attractive one. But this has to be seen with the employment prospects, on which more below.

Who would decide on the rate of Euro money supply? The Board of Governors of the European monetary authority - who would be controlled by the Council of Finance Ministers or not? - a clear political issue. Some might advocate an independence of the kind enjoyed by the U.S. Federal Reserve Board or the Bundesbank, which is contrary to the Anglo-French tradition. Modern monetary theory is sufficiently influential that many people would be more sympathetic than a few years ago to giving independent powers to the monetary authority. On the other hand the budgetary powers would, while significant, be much less than in the U.S. (see on fiscal power below). The monetary authority would have the main European level economic policy instruments in its hand, and this would militate against giving it too much independence.

What would be the situation for wage bargaining? Inflationary countries would have to make a break in their habits no more drastic than in the tougher phases of some recent incomes policy experiences. But the difference would be that there could be no relapse after a year or so into 20 to 30% pay rounds; that would mean facing bankruptcy in the private and public sectors, since national governments could not resort to monetary financing of inflation. If they overdid their sales of debt to support too many lame ducks, finance excessive pay rises, etc., they would be in a New York-type situation.

Would there be Euro-incomes policy, Brussels wage controls? No, since our assumption is a minimum centralisation, but one could imagine coordinated price control moves by national authorities, and the Tripartite Conference becoming an important consultative body here (for German style 'Concerted Action').

Would there be a harmonisation of wage rates across countries? The unions would probably push in that direction. This would be one of the crucial questions. A premature alignment of wage rates would be catastrophic for employment in less efficient countries. Eventually there should be a significant convergence of income levels, and there might be some early move because of the cushioning effect of fiscal transfers (see below). But basically the pressure for wage parity would make dramatically urgent the need to narrow productivity differentials and mount a really powerful Community regional policy or else face unemployment in less efficient countries on a scale to provoke secession from the monetary union (see more below on employment and living standards).

(iii) Exchange rate, balance of payments and international financial polic

If wage bargaining could be successfully adapted, the abolition of exchange rate changes in Europe could be very helpful in making inflation more manageable. Violent interactions between exchange rates changes and inflation would be virtually eliminated - i.e. reduced to the modest scale experienced by the U.S. This is because the Community exchange rate would be a far more bulky and stable element in th international monetary system. A strike here, or national election there, would not change the rate with the dollar much.

A related advantage is that the Euro-currency would rival the dollar as a world currency. This would relieve the Community of many short-run balance of payments preoccupations. It could live through patches of unfavourable trading results (like the U.S. now) with a few points slide in the exchange rate and relative equanimity. International capital would be more stable having fewer exchange risks to play on, and Europe would stand to gain in seigniorage through being the issuer of a world currency. To have a world currency is a great advantage if you have the financial and economic strength behind it, and this Europe could aspire to have.

National balance of payments problems would wholly disappear as an immediate constraint on economic management of member states (as well as the Community's overall balance of payments being an attenuated constraint, as just described). The disappearance of national balance of payments problems may be seen as a major attraction to all member states with tendencies towards worrying deficits (all the Nine except Germany and Benelux). But this begs the major question as to what payments inbalances would in fact be financed by the central budget. There is no meaning to making balance of payment problems go away unless it is for some states or regions to have deficits and surpluses of a pattern and amplitude different to those imposed by normal international financial disciplines. Regional payments imbalances in modern monetary unions are in fact very large indeed - this being financed by fiscal redistribution (on which more below). International payments inbalances are considered to be serious at the level of 1 to 2% of GNP; in poor regions of monetary unions deficits are often financed by budgetary means at the level of up to 10% of GNP, or even more (15 to 30%) in extreme cases (N. Ireland, Brittany, Calabria * . This financing is important to living standards. However, it does not necessarily resolve regional economic development problems. Indeed monetary union can be said to convert balance of payments problems which are corrected by exchange rate changes, into regional problems which are attenuated by fiscal transfers.

(iii) Employment

There is the level and regional distribution of employment to consider.

As to the aggregate level of employment, it would be determined by three main factors:

(a) the political choice of the European monetary authority, which could be more or less pro-employment or pro-stability in the way that any government has to make this kind of choice; this amounts to taking a chance on whether the policy choice of the monetary authority

* Report of the MacDougall Group, (4), p.32-33.

will accord with one's own preference or not (majority voting procedures would have to prevail, since decisions would have to be taken efficiently on a day to day basis); the Community would also have fairly substantial budgetary powers, for discretionary use.

(b) the political choices of member states which would retain large autonomous budgetary powers affecting employment (a key question would be how autonomous these powers could remain without running into intolerable problems of contradictory policies by the Community and member states);

(c) the technical improvement in the effectiveness of monetary policy run at a centralised European level rather than at the member states level. This is the joker in the pack, as will be seen in a moment.

The question of technical improvement in economic policy is extremely important. What we need to look at here is the appropriate level of government for macroeconomic policy. There are theoretical and practical issues pointing to the different levels of government (speaking roughly in terms of population size of the jurisdiction) that are best for different kinds of public policy *. For example few people would doubt that local governments should do garbage disposal. Our main concern here is whether the location of macroeconomic policy power at the level of the member state today works reasonably well or not; if not, are there any fundamental defects in the present system that could be improved on by passing a large piece of economic policy power to a European monetary union?

It should be clear that macroeconomic policy is performing very badly in Europe today - in terms of inflation, employment and exchange rates; sufficiently badly to constitute a major threat even to political and social values as well as being economic failure. Does this have anything important to do with the level of government at which policy is being made? Prima facie evidence here, to say the least, is seen in the fact that all European Governments place a large part of the blame for their present

../..

*See Wallace E. Oates (5) and (6).

discomfort on the incapacity of their government to determine the international economic climate, which in turn is a critical constraint on their hopes for employment, or price stability, or the balance of payments.
Why is the United States moving out of recession reasonably well, while Europe is wallowing in immobility and dissarray?

The United States is moving ahead again because Mr. Burns has inflation more or less under control, Mr. Carter will use his budgetary powers to sustain the recovery, and neither have to worry much about the deteriorating balance of payments.

In Europe German investors are not investing because they do not see the demand coming from the rest of Europe; and they are only being realistic because everybody knows that any major reexpansion in France, or Italy, or the U.K. will immediately trigger off financial speculation, a big drop in the exchange rate, and a consequential rise in inflation prospects etc.

Europe is thus paralysed. Is it because of domestic socio-political disorders coinciding in three big countries, or because of a fundamental defect in the organization of economic policy in an integrating Europe? No doubt both, with powerful interactions.

The sceptical European and optimistic nation-state man may argue that we are witnessing a passing spasm of socio-political disorders. Why should we change the constitution of Europe (which monetary union entails) in response to just a somewhat deeper than usual cyclical recession due to the oil crisis? This is a respectable question, and it is a matter of judgement. But a serious argument can be made that, in order to get Europe back onto a sound employment and growth path, we need to:

- establish a low common rate of inflation in Europe,
- remove the paralysing combination of financial instability interacting on inflation that the majority of member states is suffering from.

The prospect of monetary union may be seen as a key to doing just this. Of all the new 'structural problems' in Europe that are so loosely talked about there is perhaps none more important or concrete than the decline in effectiveness of national economic policies. This decline has resulted from the gradual internationalisation of business and finance, the collapse

../..

of the fixed exchange rate system combined now with the financial consequences of the oil crisis.

As to the regional distribution employment this would depend on how the wage bargaining situation and fiscal-regional policies developed in the future, compared to the present situation in which exchange rate policy is the main (but how efficient?) instrument for distributing employment between countries. There are, thus, three variables to assess here; future wage bargaining responsibility, future regional policy magnanimity and present exchange rate effectiveness. This can be thought of schematically:

Outcome ...	determining factor		
for regional distribution of employment in monetary union	future wage bargaining responsibility (a)	future regional policy magnanimity (b)	present exchange rate effectiveness (c)
very positive	good	large	bad
very negative	bad	little	good
outcome uncertain	bad	large	bad

Notes

(a) meaning: trade unions do not push too quickly for wage parity across member states

(b) meaning: high inter-regional redistributive power of budget and/or administrative regional policy powers

(c) meaning: exchange rate changes are not fully or quickly offset by further differential inflation.

(iv) Living standards

The usual argument is that living standards should rise because a higher degree of trade intensity should become possible. The stable monetary relations between states should reduce the risk of working towards a much higher degree of mutual market penetration - it has been estimated that the regions of countries like the U.K. and France are two to three time more 'open' (trade-intensive) as economies (regional exports and imports in relation to regional product) than national economies of comparable size

../..

like Benelux and Denmark in the international setting.

A second and new argument - as argued above - that is living standards should rise because macroeconomic policy achieves a more favourable employment - inflation relationship. This means being able to push the economy to a higher growth performance before encountering excessive inflation, or balance of payments constraints of the national or extra-Community variety.

But there is, as for employment, the question whether the inter-regional distribution of the increase in living standards would be distributed in a politically acceptable way - indeed whether all regions or states would be better off compared to a situation where some states might acquire more than all the increase in economic welfare. Economic history shows that this distribution question cannot be left to 'invisible hands'.

The inter-regional equity problem must be managed by redistribution through the Community budget.
Fiscal redistribution is seen within our member states largely as a matter of political preference. In a confederal setting fiscal redistribution may be seen in functional economic terms: it can provide the assurance that the gains from customs and monetary union are distributed so as to make all states better off. In practise such transfers can be either in the form of unconditional income grants between state governments (via the federal budget as in Canada or Australia, or, in part, directly between state governments as in Germany) or conditional grants tied to specific purposes, like improving the economic capacity of weaker states (regional investment incentives, training schemes, employment premia, infrastructure projects, etc.). The former act more on living standards than employment; the latter are more employment and productivity oriented.

It is frequently the case that peripheral states have to be 'bought into' monetary union with fiscal transfers, since these are the states that stand to benefit least in the first round distribution of benefits from customs and monetary unions; they may even be made worse off in the absence of these transfers.

It is a general rule that monetary union among large industrialised states has to be buttressed by powerful fiscal mechanisms. This is necessary because imperfections in the economic system do not produce a smooth rate of employment across all regions and states: this concerns monopoly power of business in the states or regions that get the upper hand, the difficulty

../..

of getting trade unions to adjust to their efficiency wage rate in the weaker states, and the tendency towards concentration of economic activity at the geographic centre. We do not here go into the technicalities of fiscal redistribution. This has been done extensively in the MacDougall Group Report. But one of the interesting conclusions was that monetary union could probably be supported by fiscal transfers of magnitudes which, while important, could be small by conventional federal budget standards: i.e. a few percentage points of GNP of the order of 2 to 4% in addition to the present 1%, as opposed to the 20 to 25% of GNP found in classic federations.

Fiscal redistribution may also serve as compensation for the loss of some political independence. In the case of Quebec fiscal redistribution from Ottawa seems to be unduly generous by economic standards. But the richest member states may value political union more highly than the weaker states - and they have more money (the weaker states may even give political unity a negative value).

Summary and conclusion

Monetary union is a radical and uncompromising proposition. We either have a single money or we don't, and if we do it implies an enormous centralisation of economic policy power, comparable in importance to setting up a common defense force. To talk about it seriously implies a total change in the name of the Community game. The concept is at present completely discredited in the Community context. This is for two reasons.
In the last attempt it became evident that member states were not prepared to accept the basic transfer-of-power implications when the early stages of their gradualistic approach were reversed by exchange rate developments. Also countries with regional and employment problems saw no clear doctrine as to how monetary union would handle these problems in the absence of the ability to make exchange rate changes, and so formed unsympathetic political attitudes.

As with the prospect of a European defense force, one cannot fully answer the question as to what the consequences of monetary union would be - it partly depends on how this massive instrument of economic power were used by the political authorities that managed it.
What is certain, however, is that monetary union would stand to change in major ways the prospects for inflation, employment, living standards, the balance of payments and regional problems.

Monetary union would establish a common inflation rate, which policy could seek to make a low one. It would much alleviate balance of payments constraints on economic policy. It would remove the present kind of vicious, speculative exchange rate instability that interacts so damagingly with inflation and business confidence. It could give the Community the great advantages of a stable and strongly backed world currency. These factors could combine to improve greatly the prospects for a more positive management of economic policy, which instead of being virtually paralysed as it is at present, could put the Community back on to the path of high employment and low inflation. Monetary union would have to be buttressed by a substantially bigger Community budget which would have the functions of a really significant regional policy and of redistributing public finance so as to ensure that the fruits of the increased economic wealth were distributed between member states and regions in a politically acceptable way in terms of employment and living standards.

The prizes to be gained are thus very great. But the problems would also be formidable: adapting wage bargaining behaviour to the disciplines of a common inflation rate, the large loss of national sovereignty, and the coordination of Community monetary policy with the budgetary powers that would remain predominantly at the national level.

Where do we go from here? The case for monetary union - with the right associated conditions - is far better than the present state of public opinion would suggest. The least to be done is to restimulate the debate on the economics, politics and institutional implications of monetary union. We need to reduce our present embarrassing reliance on rather dated, , gradualistic doctrines, which are not taken seriously by the press and are maintained by member states as cover for their lack of political will, and as intellectual imprisonment for the Commission. We should be able to conduct the debate in more fundamental terms (for example with the Parliament and public opinion).
We should be sympathetic to and play our part in sensible current business by way of economic policy coordination. But we need to talk also in terms of a bigger and politically more attractive proposition - which monetary union can be put to be.

ANNEX

National attitudes to monetary union. These are worth summarising, at the risk of caricature, because it shows where a new debate would have to start.

Germany. In principle for, especially for the political integration it would entail. But business interests tend to feel that the extra economic benefits, beyond the existing customs union and world trading situation, would be relatively small. Government argues that there has to be a prior convergence of other states on German stability ('le préalable allemand'); and feels that Germany pays quite enough through the Community Budget by way of fiscal transfers already. The Bundesbank is very happy with floating exchange rates, since this abates foreign money inflows which upsets their domestic monetary policy.

France. In principle for. There seems to be little awareness of the fiscal implications, and those who do know about federal budgets recoil because France is felt to be a rich but vulnerable economy: - i.e. wealthy but unable to pay. Some feel that the present state of the Community is optimal for France. Agricultural and trade benefits have been achieved. There is only the prospect of sovereignty and fiscal losses to come from further integration.

Italy. Very aware of the regional problem, and the tardiness of the Community in acting seriously over this. Would need convincing that the Community was really prepared to offer fiscal and regional policy guarantees in exchange for ceding exchange rate independence.

Benelux. All for because they have little independence to lose, only better European Government to gain. Strong small country bias in underestimating the scale of fiscal redistribution required to make monetary union viable as between larger countries.

U.K. Strong antipathy. Worried about the loss of the exchange rate instrument and the regional problem like the Italians, and are further worried about the loss of sovereignty. Moreover Whitehall is profoundly suspicious of other countries' attitudes: "the Germans think it just a question of discipline, the French think it can happen as an act of God".

Ireland. Sufficiently unhappy about floating with sterling to be interested.

Denmark. Interested if the others were serious.

In general this shows that a relaunching of monetary union would be an uphill struggle.

References

(1) Max Corden, Monetary Integration, Essays in International Finance, Princeton University, April 1972.

(2) Max Corden, Monetary Union, Main Issues facing the European Community, Trade Policy Research Centre, London, December 1976.

(3) R. Marjolin et al., Report of the Study Group on Economic and Monetary Union, Commission, Brussels, March 1975.

(4) Sir Donald MacDougall et al., Report of the Study Group on the Role of Public Finance in European Integration (Vols 1 and 2), Commission, Brussels, April 1977.

(5) W.E. Oates, Fiscal Federalism, Harcourt Brace Jovanovich, New York, 1972.

(6) W.E. Oates (ed), The Political Economy of Fiscal Federalism, Lexington Books, 1977.