

Report on the question of the European Unit of Account (Brussels, 4 December 1974)

Caption: On 4 December 1974, the Monetary Committee of the European Communities publishes a report on the question of the European Unit of Account.

Source: Report of the Monetary Committee on the problem of the European Unit of Account. II/703/74. Monetary Committee [online]. Brussels: European Communities, 4 October 1974 [accessed 29 May 2012]. Available on: http://ec.europa.eu/economy_finance/emu_history/documentation/chapter7/19741204en03reporteurunitacco.pdf.

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EUROPEAN COMMUNITIES

Monetary Committee

Brussels, 4 December 1974

II/703/74 - E

REPORT OF THE MONETARY COMMITTEE
ON THE PROBLEM OF THE EUROPEAN UNIT OF ACCOUNT

1. The Unit of Account to be utilized in the European Communities serves the following functions:-

- a) the denominator and measure of claims and obligations arising from intra-Community monetary transactions.
- b) the instrument to account for and, in certain cases, to determine the value of financial transactions and to maintain over time the relative value of rights and obligations, for example in the European Development Fund, the Social Fund and the European Coal and Steel Community.
- c) the instrument to make it possible to preserve a given and unified price structure in certain sectors of the Community such as agriculture.

2. Merely choosing the Unit of Account does not provide an adequate basis for solving all of the operational problems which may arise in any given sector. For instance the effective operation of the common agricultural policy and the Community budget depends not only on the choice and definition of the Unit of Account, but also and indeed mainly on political decisions concerning in particular the fixing of agricultural prices.

3. The functioning of the different Community mechanisms using different Units of Account has come up against great difficulties in recent times on account of the turbulent monetary events which have characterised the last few years. Unpredictable and large changes in the relative values of currencies have taken place. Although no Unit of Account, however defined, can prevent these changes from happening, it is felt that the objective should be to find definitions which would more readily accommodate these changes or produce more appropriate results than others, and not run the risk of becoming outdated.

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4. The Monetary Committee considered the choices of Units of Accounts which are available. It noted that 3 categories could be construed as effectively presenting two kinds of approach:-

- a) The par value or central rate grid approach. The accounting mechanism in the exchange operations of the E.M.C.F. is an example. A modified version is to be found in the European Coal and Steel Community, based on the fixed rate relationship between the snake currencies and on market rates for currencies outside the snake.
- b) The standard basket approach; A European Unit of Account in the strict sense would have to be based on an E.E.C. basket, the contents of which are considered in paragraphs 8 and 9 below. Another possibility which has been suggested is to use the world basket corresponding to the Special Drawing Right.

5. The essential difference between the approaches outlined in (a) and (b) is that the value of the Unit of Account would be determined by a small group of currencies in the first case and by the average value of a larger group of currencies in the second. Under (a) the small group of currencies would enjoy a fixed relationship with the Unit while other currencies would float in relation to it, whereas under (b) all currencies would fluctuate vis-à-vis the Unit of Account. It should be noted that - provided conversion between each currency and the Unit of Account follows exactly or very closely the market rates between currencies - the choice between the two approaches makes little or no difference to the relative value of national claims and obligations determined in units of account.

6. As regards the choice between the two alternatives within the standard basket formula outlined in 4 (b), it was noted that different operations might be more appropriately served either by an E.E.C. average or by a world average depending on circumstances. It was pointed out in this respect that the behaviour of these two units calculated over the last two years, would have shown only minimal divergence.

7. The Committee felt that an attempt to define the concept of an E.E.C. basket amounted in practice to define an embryo European currency. Although

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everybody recognised the ultimate need for this, it was felt that there would be dangers in doing so prematurely under present circumstances. Some members of the Committee pointed out that in a European basket, more than half of the total weights would be represented by floating currencies. This would result in an unacceptably high degree of uncertainty about the value of the Unit of Account. Other members, on the contrary, felt that a parity grid unit which would ignore the values of over half of the weight of participating currencies would be unrepresentative.

8. There is an almost limitless theoretical choice of weights for a Unit of Account defined in terms of an E.E.C. basket of currencies. Any realistic selection would need broadly to reflect the relative importance of the currencies and economies of member countries. Arrangements would have to be made for a procedure for reviewing the weights as in the case of the SDR.

9. The Committee found itself unable to make recommendations in favour of any particular Unit of Account to be used for the whole range of Community operations for which it is required. It suggests accordingly that the three formulae under consideration, namely parity grid, E.E.C. basket and the SDR should all be tested in each sector. In assessing the degree of applicability of the basket approach to each sector, an opinion would have to be expressed on the importance of the weighting in the basket and on the particular procedures for reviewing the weights. As an illustration of what a European basket might look like, and without prejudice to the final choice of the basket, the quotas in the Short-term Monetary Support system should be considered.

10. The Committee suggests that as a first approach and without prejudice to other procedures which may be followed at a later stage, it might undertake itself to test the 3 units of account under consideration, in cooperation with experts in the different sectors.