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Article

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Intereconomics

Suggested Citation: Werner, Pierre (1971) : Without monetary union there is no political integration, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 6, Iss. 8, pp. 232-235, http://dx.doi.org/10.1007/BF02927088

This Version is available at:
http://hdl.handle.net/10419/138509

FORUM

Floating and Monetary Union

The EEC has decided to carry through one of its most pretentious and fascinating projects: the European economic and monetary union. The question however is, whether floating exchange rates – in the Netherlands and the Federal Republic of Germany – are compatible with the monetary union aim.

Without Monetary Union there is no Political Integration

Interview with Minister of State Pierre Werner, Luxembourg

Mr President, of the alternative to plump either for a customs union with exchange rates of limited flexibility, or for an economic and currency union, the EEC has chosen the second one, which embodies more difficulties and risks. Which were the reasons for this decision?

It is an indisputable fact that the Common Market can only be fully utilised in all its vast possibilities if we transform it into an economic union, and it is impossible to build such a union without aiming at a currency union. Admittedly, the Rome Treaties did not yet foresee this dilemma, but the omission can be explained by the general conditions of the time. The atmosphere was then one of calm conditions in the field of currencies. On the other hand, even the Treaties of Rome contain a number of clauses which underline the need of closer cooperation in the economic and currency policies of EEC members. The Treaties speak for example of coordinated trading policies in relation with all countries outside the Community, and they also require all partners to act, in currency matters, in line with the common interest.

All through the past decade, I have often taken the opportunity to emphasise that recent processes of European economic integration, e.g. in the markets for farm produce, and the mounting world currency crises have made it absolutely indispensable for us to go beyond the letter of the Rome Treaties towards an economic and currency union.

Steps along the Road

It is a fact that we have just entered on the long road towards an economic and currency union. Which are the steps along this way which have already been firmly agreed on?

We have developed a plan for reaching our objective in stages, the first one of which will extend from January 1, 1971, until December 31, 1973, during which the six member states will take the most important measures for harmonising their economic and currency policies. The "Werner Plan" intended to achieve a compromise between the so-called "monetarists" and "economists" in Europe: that is why it foresees both the coordination and harmonisation of economic and financial policies, and the creation of a common currency machinery, e.g. the reduction of the margins of exchange rate fluctuations and common interventions in the dollar markets. During the second part of the first stage, it is intended to extend cooperation between central banks to the mutual issue of short-term credits and to the joint intervention in the markets for other currencies. If we extend and develop this machinery further, this must inevitably end in the creation of a joint reserve fund. Having reached this, the distance will not be great to achieving our aim of setting up, by 1980, a fully-fledged currency union.

I think that events in recent months have proved that we may advance pragmatically along our preordained path. But even in periods when the need for it is not so obvious, our actions must be deliberate and preplanned. Once the methods of using a given machinery are fixed for the long term, we shall, in all probability, be able to accelerate progress.

Clarity about Final Aim

In order to achieve economic and currency union, it is indispensable to be completely clear about the final aim, and about its economic effects. Is there really sufficient clarity about the ultimate objectives?

In drafting the Werner Report, we have taken immense trouble to give the clearest possible description of our aims, and I am glad that the decisions taken by the Council of Ministers, when it met in Brussels in February 1971, have largely adopted this description of the desired final state of affairs. It is true that our Report had outlined the institutional requirements much more precisely than did the decisions of the ministers, but even the Council of Ministers accepted the need for certain sovereign rights to be ceded by member states to the Community as a whole.

And what are in your opinion the chances for this?

The most important thing is the fact that all EEC members have proclaimed their willingness to cede some of their rights to a higher authority. Naturally, one may interprete this narrowly or more liberally – this is a problem of political philosophy.

There are some governments who are afraid that, once we have an economic and currency union, they will not longer be able to tackle structural problems without all the other community members wanting to interfere. But we in Luxembourg know from experience that it is fully possible to belong to a currency union without being prevented from carrying on a national economic policy with clearly-defined aims. For example, in recent years, we have endeavoured to diversify our industry which, in the past, was completely dependent on steelmaking. The fact that we have had a currency union with Belgium for many years has never been an obstacle for us.

The Problem of Floating Exchange Rates

Let us now bring forward a different problem: The Federal Republic of Germany has freed the exchange rate for the DM from all controls. Do you believe that floating exchange rates are a danger to the economic and currency union?

I believe that people in Germany, too, know very well that the present state of affairs must not be allowed to persist for too long a period, lest the economic and currency union is to be genuinely harmed, for it is of course true that whoever wants an economic and currency union must also accept fixed exchange rates between national currencies. I am firmly convinced that no other system could operate.

This does not exclude during the period of transition some shifts in exchange rates. For the purpose of harmonising national economic structures, this may even be inescapable at certain points, but once we have reached the ultimate stage, it will no longer be possible. But even so, too frequent shifts in the rates of exchange would be harmful. Moreover, they ought always be subject to the need of each member country of conforming to the general rules adopted by the Community. In other words, the various member countries must get closer to each other, and differences between them in the economic and social development must be evened out. Devaluations or revaluations which only serve national selfishness must not be repeated. Corrections of exchange rates, which may become necessary before our final aim is reached, may be tolerated providing they serve closer structural cooperation and progress on the way towards the economic union. But it will be impossible to permit exchange rates that fluctuate from day to day.

You mean, they threaten the completion of an economic and currency union?

Quite so. But, on the other hand, it is to be welcomed in the present development that nobody among our partners is today questioning the need to continue building our future economic and currency union. It is true that, immediately after the 9th of May, governments, economic experts, and the press were smitten by a feeling of uncertainty. But shortly after, nearly everybody saw the point that especially now, and because of this uncertainty, we must continue to work for our great agreed aim and to make progress on the way there.

There are two camps nowadays in economic policy: the one works for as stable prices and wages as possible, even at the expense of a stable currency, if need be; the other one, however, believes that there ought to be a fixed point for all the other economic factors – the currency. These two schools are opposed to each other. But I think I was able, during recent talks, to discern more mutual understanding developing between the EEC partners. We must overcome our differences.

Fixed Exchange Rates Necessary

Is it your view that Germany will have to return to the old DM exchange rate, or would its partners in the EEC show understanding for a revaluation of the DM?

I am unable to comment on revaluation or non-revaluation of the DM, beyond the Brussels statement of May 9, that no currency, including the DM, needs to be revalued for economic reasons. But I may state, with regard to progress to be made towards an economic and monetary union: it really does not matter whether the Federal Government will return to the old exchange rate or establish a new one. In the interest of our economic and currency union, the main aim is to return, as quickly as possible, to fixed exchange rates.

What will be the outcome of the current crisis? Will the margins between which EEC currencies may fluctuate against each other be narrowed, whilst they will be widened towards other currencies outside, in order to make a contribution to reforming the world system of currency relations?

This is indeed the question: Which would be the position taken by the EEC, as a whole, in regard to the studies of the International Monetary Fund currently under way about the desirability of a more flexible system of world currencies? Steps in this direction were being prepared in 1970, but they have been swept aside by recent events. Yet it might be accepted that the Six (and, it is to be hoped, the Ten) would be prepared, on the one hand, to reduce the margins within which their own currencies might float against each other, and to widen the margin for fluctuations against the currencies of countries outside the EEC, especially against the dollar. But how wide such flexibility might be is at present still subject to great differences of opinion. Yet, within limits, this kind of fluctuation would be acceptable, even for international trade. On the other hand, we must not forget that world trade would be adversely affected if the margins of floating individual currencies were too wide. In discussing these questions, we do not intend to dethrone the dollar but to reduce the pressure on it. I believe that the American currency authorities would be very glad if they could shed part of the burden which presses upon the dollar as a reserve currency.

Stability and Growth

Will the Federal Republic of Germany be obliged, in future, to revise its comparatively rigid ideas of stability and to adapt itself to the wishes of its partners for more rapid growth?

Stability and growth must be achieved as parallel developments. The fact that, at present, there are still differences among member countries about the varying degrees of priority which should be accorded to either growth or stability, is due to structural differences between the individual countries, and means that it will be necessary to harmonise these structures by taking a number of measures, which have been mentioned in our report.

This is to be done within the Community in a similar way as it is now being effected within nation states, through structural and regional policies designed to even out the differences. The organs and institutions of the Community have to be used for this purpose; with the help of various EEC funds and of the European Investment Bank quite a lot can be achieved at the official level. But this is also possible within the framework of a free and competitive economy, through spontaneous changes, because we do hope to avoid growing accumulations of people and production plants on a narrow geographical basis. Capital and private investments ought to be channelled into areas which are now economically weaker, thereby also inducing labour to migrate.

All this requires inevitably a determined Community policy. It is inadmissible to let things simply drift. The Community as a whole must design a concept of structural changes with the aid of its national governments. Finance for this will have to be found both by the Community and by national authorities, to arrive at the desired ideal situation, in which a harmonisation of aims will take place: because growth will then occur under conditions of stability, and stability will depend on growth.

Importance of Great Britain

After negotiations with the United Kingdom about its accession to the EEC have been concluded succesfully, the question arises: Will the enlargement of the Community perhaps delay its further progress towards becoming an economic and currency union?

If there should be any delay, this could only have technical causes. On the other hand, I see a big chance for our economic and currency union arising from

Britain's entry. By adding Britain to our Community, the currency union will for the first time gain the appropriate size. Only by taking in the UK, the Community will become a currency partner able to make a worthwhile contribution to reforming the currency system of the world. Britain's importance for the future economic and currency union derives, on the one hand, from the British economic potential, on the other hand, from the financial know-how, the immense experiences, and the influence of the City.

It is clear that there will still have to be discussions about the conditions for the integration of the sterling currency with the overall system of the EEC. But it is not absolutely necessary to delay, for this reason, the completion of the economic and currency union's first stage. As to the currency union, the British authorities have never made any adverse comment. Whenever I had talks on this subject with the highest British personalities, I was always told that they are willing to make their own contribution. When speaking to British partners, I found that they were much less sceptical about the economic and currency union than on numerous occasions many continental Europeans.

To conclude, let us assume that future developments will take the most unfavourable course: that there will be no economic and currency union, for whatever reason. What would be the effects of this failure for Europe?

Without doubt, this would gravely weaken Europe, both economically and politically. In the first instance, a number of achievements, which we have already reached, would be threatened. For example, I could not see how the common market for farm produce could then survive. If we give up work for unifying our currencies, the inevitable effect will be the revival of mutual trade barriers, of currency controls, of the trends towards autarky, which we have witnessed during the thirties. Trade between member countries would be badly affected. It might be perhaps possible to keep in being a free trade zone, but our economic importance would fade away.

Politically, too, a failure to build an economic and currency union would have highly adverse effects, for in the last analysis, the development which has started aims at political unification of Europe. It is true that we need not achieve a European confederation or federation tomorrow. But to arrive at this ultimate goal, we must first take the step of creating an economic and currency union.

Floating Exchange Rates Are No Panacea

Six Questions to Professor Raymond Barre, Vice-President of the EEC, Brussels

Are floating exchange rates a long-term danger for the projected economic and currency union?

There are various answers to this question, depending on whether all the national currencies within the Community are intended to be floating, independently of each other, or whether they will be floating together but on the basis of fixed exchange rates within the Community.

In the first case, the fluctuations would be in complete contravention to all that is needed for building an economic and currency union, and they could even prevent a common market from operating smoothly. In order to enable the policies of our governments, the strategy of our business entities, and the behaviour of our nations to treat the existence of the European Community as a decisive factor, it is the principal duty of the Community to provide them with the fundamental instrument of unambiguity of all their transactions, which is a common yardstick of value.

Moreover, if individual currencies within the Community were allowed to fluctuate separately and independently, the Community would be exposed to the risks of "rotating" speculation, feeding upon the immense reservoir of available international liquidity. This would create the danger of our currencies' exchange rates fluctuating in virtual independence from the basic facts which make up the situation of our national economies, in a similar way as stock exchanges are quoting certain securities much higher or lower,