

COMMITTEE FOR THE STUDY OF
ECONOMIC AND MONETARY UNION

31st January 1989

For the discussions of the Committee at its forthcoming meeting on 14th February, please find attached the draft of the revised Part II of the Report (CSEMU/10/89) and a brief note on "Propositions relating to the ECU" (CSEMU/9/89).

Sent Air Courier to all participants

31.1.89

+ Padoa-Schioppa

Dixon

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Propositions relating to the ECU

At the end of the January meeting the Chairman pointed out that some issues relating to the ECU needed to be clarified further. In order to facilitate the discussion of these issues this note recalls four propositions, which emerged at the last meeting.

1. "A parallel currency approach is neither a useful nor a desirable way to establish a monetary union." In accordance with this approach the ECU would be created independently of, and in addition to, national currencies, thus circulating in parallel with them and competing with them. The idea is that the ECU would "crowd out" national currencies, thus establishing a monetary union in a "painless" and non-institutional way. The Committee rejected this approach on two grounds. Firstly, it would not contribute to solving in an orderly manner the problem of co-ordinating national monetary policies; on the contrary, it would add a thirteenth player to an already difficult co-ordination exercise. Secondly, it could undermine a monetary policy oriented towards price stability, because it would add a source of money creation that is difficult to link to the needs of economic activity.

Concrete implications of this proposition are that before the achievement of the monetary union:

- the ECU should remain a basket;
- no independent monetary policy would be set up for the ECU;
- no link needs to be established between the private and the official ECU circuits.

2. "An "imprimatur" is given to the ECU as the future single currency of the Community." A single currency, while not strictly necessary for the creation of a monetary union, may be seen - for economic as well as

psychological and political reasons - as the natural and desirable further development of the monetary union. However, the decisive step before the Community can consider the adoption of a single currency is the irrevocable locking of exchange rates (and when this step will be reached might depend much more on an effective co-ordination of policies than a growing use of the ECU). Once exchange rates are permanently fixed the ECU will become a very close substitute for any national currency.

Concrete implications of this proposition are that:

- there should be no discontinuity between the present ECU and the future single currency, i.e. that any debt contracted in ECU before the introduction of the single currency would be payable at face value in ECU if, at maturity, the transition to the single currency has been made.

3. "All impediments to the voluntary use of the ECU as a common numeraire and a means of settlement by private economic agents would have to be removed." Barring official action discriminating in favour of the ECU (which would result in undesirable financial market distortions) and excluding a link between the official and the private ECU, there are, broadly speaking, two types of measures: direct encouragement (e.g. increased borrowing in ECUs by public sector authorities; increased use of the ECU by official entities in intra-Community transactions and, where possible, in international transactions; larger exchange market interventions in ECU; "greater official support" to the ECU clearing system) and indirect encouragement (e.g. removal of restrictions on the private use of the ECU by giving it in each member country the status of a foreign or national currency; demonstration effects through increasing operations in official ECUs within the EMS and by enlarging the group of "third" holders).

Concrete implications of this proposition are that:

- as a numeraire, the ECU would have equal, but not privileged, status compared to the national currency denomination; therefore
- the ECU would be added as a unit of account wherever national legislation specifies the use of a numeraire.

4. "The official ECU could play a role in the conduct of a common monetary policy in an advanced stage of monetary union." Gov. Ciampi presented a scheme in which the official ECU would be used as a reserve instrument in order to manage a common monetary policy in the Community. In the Committee the view was expressed that this scheme represents one, but not necessarily the only, way to give operational meaning to the concept of a single monetary policy. It was also observed that the introduction of such a scheme would be more appropriate in the final stage when a single monetary policy has become indispensable. Are other schemes for a common monetary policy conceivable in which the official ECU can play a role? In considering this question the Committee may wish to take into account that the ECU should not become a parallel currency (i.e. the official ECU must remain an asset used only within the circle of central banks) and the fact that the official ECU performs already now a number of functions in central bank operations.