

Berichte

The Monetary Committee of the European Community

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When creating the European Community, the authors of the Treaty of Rome thought it wise to establish, in that Treaty, a Monetary Committee which would advise both the Council and the Commission, at their request or on its own initiative. In the course of its confidential, regular meetings, of which several hundred have now been held, this Committee has developed an important role in the specification of economic and monetary policy at Community level and, more recently, in the strategic management of the evolving European Monetary System.

The Monetary Committee, when set up in 1958, opened up new forms of monetary cooperation in Western Europe. The initial conception of the Committee was strongly influenced by the example of the Managing Board of the European Payments Union which had prepared the way for the full convertibility of Western European currencies. Thus many of the Committee's members at its first meeting in June 1958 had served before on the EPU managing board. Some years later, when "Working Party Three" of the OECD was created, the Monetary Committee in turn served as its model. At that time the Chairman of the Committee also became the Chairman of that OECD Committee.

Today, over a quarter of a century since it was founded, the Committee operates in a Community of twelve members and in the context of the European Monetary System. It is the EMS which determines a major portion of its activities and, conversely, the management and future course of the EMS are in large part determined by the Monetary Committee.

I. The Effectiveness of the Committee and its Methods of Working

The rules governing the Committee provide for each Member State and the Commission to appoint two members. They are generally the head of the Treasury (or his deputy) and the "number two" of the central bank. In addi-

tion, two alternate members may be appointed; the alternates meet as a group and often play an important role in the preparation of meetings. The main analytical input to the Committee comes from the Commission's staff. There are close interrelations with the Committee of Governors of the Central Banks of the European Communities. Half of the Monetary Committee's members are also members of the Governors' Committee. The secretary of each Committee is present at the other Committee's meetings.

The strength of the Monetary Committee lies in the quality of its members and in its tradition of policy-oriented debates leading to operational conclusions. Members concentrate on those aspects which have an important bearing on the interaction of policies among Community countries. They report and comment on any change in their countries' policy lines and if possible indicate future orientations. Spontaneity is the rule and there is no reading of prepared briefs.

The efficiency of the Committee is enhanced by the guiding role of the Chairman, who determines the course of its deliberations and draws up its policy conclusions. The Committee's positions are finalized in the form of opinions and reports, and generally these take the form of Chairman's reports or statements to the Council. This technique of not committing every member to every sentence allows action to be taken and policy messages to be given quickly, and to go beyond the lowest common denominator.

With the successive enlargements of the Community, the Committee has doubled the number of its members. This jump from a small intimate group into a large family has led to new and less formal ways of working. The Committee has moved closer to the Council; it is an efficient and confidential group and in consequence the range of its policy discussions and the scope of its policy influence are widening all the time.

II. The Range of the Committee's Tasks and its Relation to the Council of Ministers

The Monetary Committee was set up by the Treaty of Rome which confers specific functions to it. Almost all Treaty articles dealing with capital movements, the balance of payments and the monetary dimension refer explicitly to it, giving the Committee an established institutional role from the beginning.¹ However, with the extension of the legislation and the machinery of the Community, additional tasks have fallen to it. Thus the granting of Com-

¹ These are in particular the following eleven Articles: 69 to 73, 102A and 105 to 109.

munity loans to Member States facing difficulties in their balances of payments cannot be decided upon by the Council of Ministers without a prior formal statement of its position from the Committee. Sometimes arrangements involve special surveillance by the Committee of a Member State's economic and financial developments. Other responsibilities of the Committee lie in the area of international monetary relations and decisions relating to the ECU. A special role has fallen to it in the continuing development and the management of the European Monetary System.

No less important than legal attributions are those which derive from the political weight of the Committee. Seldom does a meeting of economic and finance ministers pass without a request for preparatory work and a statement from the Monetary Committee. No important monetary decision in Community history has been taken without preparatory work by the Committee. Sometimes it is compared to the Committee of Permanent Representatives, but that gives a distorted picture. It is the combination of conceptual force with skill in the shaping of policy-oriented decisions which has made the Committee into a highly effective Community institution *sui generis*. It has thereby firmly established itself in the predecisionary field of economic policy and related action.

III. Making the Coordination of Economic Policies Operational

Within the Community, it is the Monetary Committee which closely monitors economic developments in Member States. At the beginning of each meeting, the *tour d'horizon* allows any important economic policy issue to be brought up. Regular country examinations, thoroughly prepared by the staff of the Commission, constitute the necessary groundwork for its tasks. After each such examination the Chairman's conclusions are prepared and form the basis of a confidential communication to officials or, in some cases, the government of the country concerned.

Another approach to the coordination of policy is the use of "horizontal" examinations of the stance of monetary policy in the Community as a whole. Particular stress is given in horizontal examinations to the counterparts of monetary growth because they allow discussion to extend beyond the field of monetary policy and to cover such important areas as public finance and wage developments. In this field the Committee is helped by the close cooperation which it has with the Committee of Governors of the Central Banks. The Monetary Committee generally receives all the analytical reports of the Governors' Committee.

One of the biannual examinations of monetary policies takes place at the end of the year, in time to discuss quantitative national targets for money or credit for the coming year. The other discussion around the middle of the year is generally devoted to the implementation of monetary policy in view of actual macro-economic developments. Particular stress is laid on showing the effect of Member States' policies on each other and on the early detection of any danger of diverging developments.

The purposes of coordination are largely determined by the objectives of the European Monetary System, and therefore coordination cannot be confined to monetary policy alone. There is a strong, practical need to include fiscal policy, because very often the size of the budget deficit and the stock of public debt determine the degree of monetary stability which can be attained in practice.

In addition to striving for the convergence of economic and monetary policies within the Community, the Committee is also the central body for the coordination of Member States' policies in the field of international monetary relations.² Discussions include international monetary policy issues arising in the IMF and the World Bank. International indebtedness is one of the key themes of the Committee. The development of the US Dollar and financial relations with Japan are more frequently on the agenda. From time to time there are also discussions in depth on the compatibility of economic policies at world level.

IV. The Task of Bringing Both the Objectives and the Results of Economic Policies on to a Convergent Course

The Committee works for the convergence of the orientations of economic policy in the member countries, and on this road good progress has been made in recent years; but what matters in the last analysis is that policies should lead to a convergence of economic performance. In the end it is the result and not the intention that counts. Moreover, convergence must be given a normative content. If all countries were to converge at a high level of inflation this would be contrary to the objectives of the EMS. Its logic implies undergoing the discipline of bringing down cost and price rises, so as to reduce inflation rates to as low a level as possible without provoking deflationary effects.

² A Council Decision of 8 May 1964 ruled that consultations between Member States in the field of international monetary relations shall take place in the Monetary Committee.

Convergence is not something which, once attained, can be maintained over time without special efforts. There is no room for relaxation when a relatively high degree of convergence has been attained. On the contrary, divergent forces constantly threaten to undo the progress achieved so far. Policy makers are therefore faced with the constant need to consolidate or revive convergence. There are continuous pressures which threaten stability, some of them of a structural and technical nature. They may give rise to divergence: for example faster technical progress in one country, leading to greater competitiveness; or an external shock which has a different impact on different Member countries. Furthermore, although nominal exchange rates are stable within the EMS over relatively long periods, a less successful policy performance in one country is bound to produce higher inflation than in partner countries; thus convergence of nominal exchange rates will be accompanied by divergence in real exchange rates.

The success which has been achieved in improving the economic fundamentals raises expectations that convergence will be extended to wider areas, and may even make this necessary. It is in the nature of convergence policy that, as one progresses, the objectives and the pressure to meet them grow even faster, so that there always remains a goal to be achieved.

The Committee's most important task is to strengthen the basic economic policy consensus built up during eight years of EMS practice, which has gained its own political weight. The EMS has become a zone of internal and external stability but this implies that the authorities are in a position to intervene with the full range of economic policy instruments. In recent years convergence has progressed reasonably well on the monetary side, but pronounced divergencies in the field of public finance have in some cases impeded progress in liberalizing capital movements. In more than one member country the public sector deficit is of such size that it limits the scope and the efficiency of monetary policy. Strengthening the EMS therefore means that, as a matter of priority, the public sector deficit will have to be reduced in these countries.

The Committee would not properly discharge its role if it were only a place for the confrontation of national policies and positions. There is a clear need for a "value added" and in particular for the development of an understanding of the optimal conduct of policy within the EMS. It is in this perspective that its deliberations have led to the formation of some common understandings. For example, to allow the disciplinary effect of the EMS to work effectively, it is generally agreed that a country which has not brought price and cost increases sufficiently under control must tolerate a rise in its real exchange rate as long as its current account does not deteriorate into

fundamental disequilibrium. Another understanding is that monetary policy should prevent domestic liquidity creation (including official public foreign borrowing) from fully compensating the liquidity loss caused by a current account deficit. If there were no tightening of liquidity, there would be no incentive for private capital flows to finance the current account deficit. Other understandings will emerge as the system is confronted with new challenges. For example it may become an understanding that in the event of large and persistent foreign exchange market intervention the economic policy of the country in question, and in particular its interest rate differentials, will be examined with a view to bringing this intervention to a halt. These understandings are never seen as formally binding rules, since policy actions must always be the result of judgemental decisions. However, to the extent that they facilitate prompt and predictable actions in support of the aims of the EMS they make its nature more clear to the markets and reduce destabilizing tendencies.

V. A Different Type of Conditionality

Conditionality in the Community, which has strong political links, is different from the conditionality of the IMF. It has its own flavour because it emerges from the process of continuous, month-by-month consultation outlined above. More political elements enter into consideration. Some of these factors may at first sight seem to imply a weaker form of conditionality; however, the life of the Community also opens up the possibility of using these political inter-relationships in a positive and constraining way in order to construct strong packages of economic adjustment which work in conjunction with other constraining obligations which derive from different parts of the Treaty of Rome, for example those relating to the free movement of goods.

A reading of the legal texts concerning the Community support mechanisms – above all the Community loan mechanism designed to support Member States in balance of payments difficulties – clearly reveals the specific surveillance role of the Monetary Committee in the decisive triangle which it forms with the Commission and the Council.

The activation of the EC's financial support arrangements, and the economic policy conditions attached to them, have generally been a success and have contributed to improved convergence. Straightforward messages from the Committee to the Council and to the Commission become very important in this context. "Keeping unter review the monetary and financial situation of Member States and of the Community and also the pay-

ments' system of Member States" (Article 1 of the Monetary Committee's Rules) gives it much opportunity to influence policy decisions. Through the years the Committee has developed its own particular tradition of analysing and evaluating economic policies, reflecting both the technical expertise and the political awareness of its members. Whenever necessary it has acted with clear statements although sometimes, for reasons of efficiency, these must remain confidential. An example of this kind was the introduction of a compulsory deposit on foreign exchange purchases by Italy in 1981 which prompted an immediate reaction by the Monetary Committee. It set up a specific surveillance procedure, increased pressure for the abolition of the import deposit scheme and prepared the ground for the Italian authorities to put the weight of their action rather more on measures directly affecting economic fundamentals.

VI. Realignments and Adjustment Measures

Parity changes within the EMS are not determined by a Council procedure. They are decided by mutual agreement between ministers in the constitutionally different setting of "cooperation in the framework of the EMS". According to internal rules, the Monetary Committee is the central institution which prepares these decisions. In certain cases, for example in March 1981 and in July 1985, it has taken the decision itself after having got the go-ahead from ministers. The convocation and setting-up of a ministerial meeting when necessary is the task of the Secretary of the Monetary Committee, who acts on instructions from the Chairman.

Realignment meetings are of crucial importance for the EMS. It is at this moment that the system has to withstand the acid test and make clear its adherence to the fundamental goal of internal and external stability. It is on this occasion that the Monetary Committee has to fulfil its function as a Community institution by finding a solution which serves the overall interests of the EMS and which strikes a balance between them and national interests. It is also on these occasions that the consistency between exchange rate policy and overall economic policy has to be verified and, if necessary, corrected. Experience has shown that each realignment is different. However, over the years the adoption of adjustment policies has become a more prominent and characteristic feature of realignments and some understandings have emerged which are particularly relevant for these critical periods:

- The size and the structure of the exchange rate changes must be determined by reference to both the economic fundamentals and the EMS objective of monetary stability. The credibility of exchange rate changes

depends on a close relationship to economic fundamentals and economic policies. If the size of the new spread of exchange rates were to go beyond what economic fundamentals justify and were determined by considerations of capital movements and by market expectations, then the EMS would lose its disciplinary effect and degenerate into a crawling peg system. Thus even small realignments should not become frequent.

- In line with final objectives and with the experience of the EMS, exchange rate changes must be accompanied by economic adjustment measures. Ideally, adjustment measures should be taken in good time, so as to avoid any need for realignment. In this sense they are a normal feature of the system and, indeed, its most important aspect. It was this consideration which once prompted a finance minister to underline that there should be an inversion of the previous order: in the first place should come the adjustment measures and then only as a secondary, accompanying move should there be a realignment.
- In all efforts to correct the results of defective policy in the past, the major thrust must come from adjustment measures in fields of economic policy other than the exchange rate. The defects of earlier policy should not be entirely compensated by the parity change. The EMS is not a system where from time to time the clock is turned back to zero and everything starts again from the beginning as though nothing had happened. Its disciplinary thrust must continue on the day after the realignment through adjustment measures. Experience has shown that no EMS country has ever asked for its accumulated cost differential to be fully absorbed by the parity change. This is of course nothing other than the expression in operational terms of the universally accepted stability constraint of the EMS.

The close relation of the size of the realignment to economic fundamentals is important if certain dangers are to be avoided: one danger is that of competitive devaluations, but it has so far only appeared as a threatening “writing on the wall”. Competitive devaluations have thus far been successfully avoided throughout the history of the EMS. Another danger is presented by the “credibility” argument which may push policy makers to excessive exchange rate changes. Any realignment must of course be credible but if this consideration is overstressed, markets will produce ever higher expectations in the future. The result would be a destabilization of the EMS. A strict regard for economic fundamentals and a willingness to take appropriate adjustment measures are therefore the best way to ensure credibility. Finally, there is the danger that in a realignment triggered by external strains and by unsettling capital movements while fundamentals are relatively good, too large a spread of exchange rate changes would of itself give

rise to destabilizing forces which would endanger fundamentals. A realignment operation of this type does not end with the publication of the new parity grid. It continues throughout the following months in the form of timely follow-up measures which ensure that interest rate differentials within the system are convincing.

VII. Conclusion

The Monetary Committee prepares most decisions which have to be taken at Community level in the monetary sphere. It also promotes the coordination of the policies of Member States in the monetary field to the full extent needed for the functioning of the common market and the European Monetary System. It is the Community body within consultations take place in respect of any important decision or position taken by Member States in the wider field of international monetary relations.

Over the years the Committee has moved from its original advisory status to that of a body with predecisionary powers. Quite early, drawing on his experience of the mid-seventies, one of the chairmen saw it as "the monetary think-tank of the Community as well as one of its most effective institutions". Since 1978 specific operational functions have been taken on which make the Monetary Committee a Community institution with special responsibility for the EMS.

Zusammenfassung

Der Währungsausschuß der Europäischen Gemeinschaft

Der Währungsausschuß der Europäischen Gemeinschaft blickt auf eine bald dreißigjährige Tätigkeit zurück. In dieser wechselvollen Zeit von Bretton-Woods, freiem Floaten und nunmehr schon nahezu einem Jahrzehnt Europäischem Währungssystem hat er der internationalen Währungspolitik zahlreiche Anregungen gegeben.

Neben dem Ausschuß der Zentralbankpräsidenten ist er zu dem entscheidenden Koordinierungsorgan der Europäischen Gemeinschaft geworden. In einigen Fällen, wie in den wichtigen Fragen der Leitkursänderung, obliegt es ihm, die Beratungen bis zur Entscheidungsreife voranzutreiben und gegebenenfalls im Auftrag der Minister zu treffen.

Seine fern jeglicher Publizität gehaltenen monatlichen Tagungen sind zum Katalysator europäischer Währungspolitik geworden. Dabei stoßen naturgemäß oft recht unterschiedliche Auffassungen aufeinander. Aber die Kraft dieser Institution liegt gerade darin, ohne verwässernde Kompromißformeln deutliche Leitsätze einer verantwortlichen EWS-Politik in der Praxis zu verwirklichen. Stabilitätsbewußte EWS-Politik ist nicht nur eine Sache des Wirkens der Mechanismen, sondern in erster Linie

das Ergebnis der politischen Bereitschaft und Durchsetzungskraft der Währungspolitiker.

Summary

The Monetary Committee of the European Community

The Monetary Committee of the European Community can look back on a history of almost thirty years. It has stimulated international monetary policy in multiple respects on this period of rapid change ranging from the Bretton-Woods regime of fixed rates of exchange via the free float to the European Monetary System, now almost ten years old.

Besides the Committee of Central Bank Governors, the Monetary Committee of the European Community has become the Community's central coordination body. In some cases such as the important issue of central rate changes its task is to push deliberations to the stage of decision-making and to take decisions on behalf of the Ministers, where appropriate.

Its monthly meetings out of the spotlight of publicity have become a catalyst of European monetary policy. This explains why – of necessity – rather divergent opinions often clash. However, the strength of this institution precisely is to implement unambiguous rules of a responsible EMS policy in practice without any diluting compromises. A stability-minded EMS policy is a matter of not only the working of mechanisms, but mainly the result of monetary policy-makers' political willingness and ability to win acceptance for their aims.

Résumé

Le comité monétaire de la Communauté Européenne

Le comité monétaire fait la rétrospective de presque trois ans de travail. Que ce soit pendant le système de Bretton Woods, des taux de change flottants ou du système monétaire européen, âgé de presque dix ans, il a conseillé maintes fois la politique monétaire internationale.

A côté du comité des Présidents des banques centrales, il est devenu l'organe coordinateur le plus déterminant de la Communauté Européenne. Dans certains cas, comme dans les questions importantes du changement des taux-clé, il lui incombe d'accélérer les consultations et de préparer les décisions et, le cas échéant, de décider lui-même par ordre des Ministres.

Ses séances mensuelles, loin de toute publicité, sont devenues le catalyseur de la politique monétaire européenne. Les membres du comité se heurtent naturellement souvent à des idées fort différentes. Mais voilà justement là que réside la force de cette institution: elle réalise dans la pratique des directives claires d'une politique monétaire européenne responsable, sans formules de compromis affadées. Pour que la politique du système monétaire européen assure la stabilité, il faut certes que les mécanismes fonctionnent. Mais il faut avant tout que les politiciens chargés de la politique monétaire le veuillent et aient la force de la réaliser.