

**Mr, Solchaga's statement on E.M.U.**

For brevity's sake, and in view of our Chairman's request, I will confine my intervention to the issue of phasing, which I consider a critical one. These are my main observations:

1. The Inter Governmental Conference must establish a precise date for stage 2 to start.

Specifically, I would suggest for stage two to start on January 1 st, 1994, a date which I consider preferable to January 1993, because it would give us a one-year experience with the full Single Market and would provide some leeway in case any of its measures were to be approved with some delay.

By the start of stage two, a number of conditions will have to be met. All exchange controls should have been removed, all currencies ought to be already within the ERM (although not all necessarily within the narrow 2,25% band), and the Single Market (including the envisaged measures on tax harmonization) should be a reality. Besides, a significant degree of convergence as regards inflation, budgetary stances and nominal interest rates will already be expected by that date, however automatic the entry into force of stage 2. Furthermore, Treasuries' access to national Central Banks would have already been banned, with all Central Banks enjoying by that date full independence from national Governments.

2. However, just establishing a date for the beginning of stage 2 will not be enough to lend credibility to and provide additional momentum for the required convergence process.

In this sense, Spain would favour the creation, right from the beginning of stage two, of a Community institution in the monetary field, as the one envisaged in the British proposal, which, while respecting the sovereignty of national monetary policies, would have the following features:

a) The institution would be independent from national Governments and, at the end of stage two, would transform itself easily into the European System of Central Banks.

b) It would issue, as in the British proposal, a new genuine currency, the so-called "hard Ecu", not to be subject to devaluation vis-à-vis any national currency in any potential currency realignment. In stage three, and after a period of irreversibly locked bilateral exchange rates, the "hard Ecu" would become the single currency of the Community.

c) It would put pressure, through the "hard Ecu" on national monetary policies, with a view to promote price stability.

d) It would serve as a coordination forum of national monetary policies during stage two, and would submit reports and proposals on economic policy to ECOFIN.

e) It would start to study the complex problems raised by the formulation and implementation of a common monetary policy during stage three.

Furthermore, during stage two the EMS would be strengthened by a gradual narrowing down of the current 2.25% fluctuation band to, say, 1%, and by central rates realignments becoming a most exceptional event.

3.- There is a compelling case for stage 2 not to be unduly short. Full economic convergence will not be achieved overnight: multilateral surveillance procedures (including growingly binding procedures on public sector budget deficits) will take time to yield results, and long ingrained economic and psychological habits (as regards, for instance, inflation expectations and risk premia implicitly included in nominal

interest rates) will change only gradually. Besides, the need for parallelism between economic and monetary progress, including the need for the Community budget to take on a more important role on infrastructure, education, research and development, etc. will argue in favour of not too short a stage two. Furthermore, the new Special Financial Support scheme envisaged in the latest Commission's document, which I see as a forerunner of more ambitious economic stabilizers to be considered further down the road, will take time to develop.

4. Although passage to stage 3 should not take place automatically according to a preestablished schedule, it should be an absolute certainty to all 12 countries. We consider that a 5 or 6 year stage two (which, if convenient, could be divided into subperiods with specific goals to be gradually achieved) might be reasonably expected, in principle, to be long enough for the overwhelming majority of countries, and the Community as such, to meet all the stage two goals to which I have referred before. Therefore, after 5 or 6 years into stage two, the European Council should take stock of progress achieved and consider whether the overwhelming majority of countries, and the Community itself, are ready for stage three. If that were the case and it were to be decided for the Community to move into full EMU, a special transitional arrangement might be provided for any country unable yet to participate in EMU in its final stage.

5. As regards stage three itself, to which some of the questions posed by Minister Carli referred, I should stress that, with the future ECU being one of the key elements of a growingly tripolar international monetary system, the ECOFIN will need to have a major responsibility in determining the ECU exchange rate policy vis-à-vis the dollar and the yen.

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Secretariat

DRAFT STATUTE

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This note has been prepared for the Alternates' meeting on 9th September 1990. Its main purpose is to take stock of the points of agreement and disagreement.

1. POINTS OF AGREEMENT

There is full agreement on the following issues:

- the objectives to be pursued by the System (Article 2) and broadly in its tasks (Article 3);
- the independence of the System, i.e.:
  - the System and members of its governing bodies are independent of instructions from Community institutions, national governments or any other bodies (Article 8);
  - appropriate security of tenure of the members of the Executive Board (Article 10) and of the national central bank Governors (Article 13);
  - appropriate instruments (Chapter IV);
  - no interference with monetary policy objectives through the obligation of public sector borrowing requirements (Article 19.1);
- the indivisibility of monetary policy whose formulation and implementation will be entrusted to the governing bodies of the System, i.e. Council and Executive Board respectively (Article 11).

## 2. POINTS OF DISAGREEMENT

There is disagreement about the following points:

- the distribution of responsibilities between the Council and the Executive Board in the decision-making process with regard to the conduct of the single monetary policy (Article 11);
- the degree to which the execution of operations may be decentralised without impairing the indivisibility of monetary policy.

The first issue needs to be reviewed by the Governors. The second issue is dealt with in Section 3 below.

## 3. CENTRALISATION VERSUS DECENTRALISATION

### 3.1. Possible solutions

(a) At one end of the spectrum - i.e. the most centralistic approach - would be a full integration of the national central banks into the System. This would imply that national central banks would become branches of the System and would require far-reaching changes in the present draft Statute; for instance concerning the legal personality, the status of national central banks in the internal organisation of the System, and the financial provisions.

A less radical, but nonetheless strongly centralistic solution, would be to allow national central banks to act only as agents of the central institution. This would not require the merging of national central banks into the System, i.e. they could maintain their separate legal personality but their capacity to act on their own would virtually be abolished. Under this solution, again, a number of Articles, such as those dealing with the role of the national central banks and the financial provisions would have to be reviewed.

(b) At the opposite end of the spectrum of possible solutions, each national central bank would become part of the System and keep - basically unchanged - its balance sheet. The central institution would not need legal personality and would not have a balance sheet of its own; the expenses of the centre would be funded by contributions from the national central banks (as is the case in the Federal Reserve System). However, the System's powers to give instructions to the

national central banks would have to be laid down clearly in the Statute. Consequently, in executing the instructions of the Council/Executive Board the national central banks would act as principal, i.e. operations would be for their account. However, as monetary policy decisions would have to be made on the basis of the balance-sheet position of all national central banks a consolidated balance sheet would be required to account for the System's operations.

A possible alternative to this solution, with only minor implications for the Statute, would be to give legal personality to the central institution but limit its capacity to act in its own name on matters of administration. A small balance sheet comprising buildings, pension funds and a modest capital base would be needed.

These two options would not entail substantive alteration of the draft Statute as presently drafted, although consideration would have to be given to additional provisions which would enable the System to perform its tasks in an equitable manner. For instance, how should interventions in the foreign exchange market be shared out among the different central banks? As regards the financial provisions, there would be no need for a mechanism for transferring assets and liabilities from national central banks to the central institution (Article 26), and the capital structure of the central institution would be simplified (Article 24). The profits and losses would be for the account of the national central banks, although a mechanism for pooling them could be devised.

(c) Between these two extreme solutions various combinations of centralised and decentralised execution of monetary policy operations are conceivable. According to one of these hybrid approaches (supported by several Alternates and as presented in Mr. Lagayette's note), all external operations would be centralised and recorded in the central institution's balance sheet, whereas the execution of domestic operations would remain the responsibility of national central banks. If this approach were followed, again Articles relating to the role of the national central banks and the financial provisions would have to be reconsidered.

### 3.2. How to conceive an evolutionary approach?

The present draft Statute attempts to accommodate an evolutionary approach whereby responsibilities for the execution of operations would gradually be transferred to the central institution. Given the uncertainties on the gradual path towards greater centralisation, it would be considered wise to leave the decisions about steps towards centralisation to the governing bodies of the System. The transfer of responsibilities in this gradual process, would entail little change in the right to dispose of assets, nor would it necessarily affect the earnings of the national central banks (which would be shareholders or depositors with the central institution). However, the transfer of responsibility in this gradual process would imply changes in ownership of assets which, in particular with respect to foreign exchange reserves, might raise sensitive political issues.

If the - necessary - flexibility of managing the System in the course of Stage Three is to be presumed, but if at the same time it is accepted that politically sensitive decisions need the confirmation of the Member States, there appear to be two approaches.

The first solution would be to specify in the Statute which of the decisions that will have to be taken on the way to the end of Stage Three should be subject to approval by the political authorities (i.e. decisions under secondary legislation). But even if the right of initiative were given to the System's governing bodies, this approach could mean a loss of flexibility and interference by political authorities in the evolution of the System's structure.

The alternative would be to draft the Statute mainly with a view to the situation at the end of Stage Three, i.e. when there will exist a high degree of centralisation. This would not necessarily mean that at the beginning of Stage Three the System would have to work on a fully centralised basis since transitional provisions could ensure a gradual progression to the final situation foreseen in the System's Statute.

The main difference in comparison with the first solution is that by describing clearly in the Statute the final structure of the System, this political approval in the form of Treaty notification may allow the System's governing bodies a more decisive role in determining the transitional arrangements.