

Meeting on 8th November 1988

(BIS, Room E)

M. J. Godeaux (First tape 110 - 247)

Mr. President, in my paper I did a few times sin against the English language for which I apologise, I also sinned against the necessary brevity, but I believe that on the whole I was - attempted at any rate to be - objective and balanced and point out what we have achieved, what remains to be achieved, and therefore I suppose that I can in this informal meeting state more explicitly than I did in my paper what I believe can be the next step for the future. Of course, in my paper you might say that in "coda venimen", because what is important in my view is the last page where I say "although the present strategy of voluntary policy co-ordination undoubtedly still leaves room for ample improvement, the question arises how long such a stance can continue meeting the increasing requirements of joint monetary policy-making and can remain a satisfactory answer to the expectations of market operators, of public opinion and of the political sphere". Then I said "not only must progress be made but it must be seen to be made", which means personally that either we are in a position to have a new Basle/Nyborg package, if that is what we prefer along the pragmatic lines, and I realise that when I say a new Basle/Nyborg package it is not so easy to define and we are faced with - let's put it frankly - when our German colleagues made a great effort to make the Basle/Nyborg package possible, they did say - I still hear Karl Otto Pöhl saying - now we must get rid of this problem for a number of years. But I believe that if we choose the pragmatic approach we must be able to put together some visible new package of measures. Alternatively, we may have an institutional step along the lines, for instance, that Jacques de Larosière has suggested, something that is not even a European Monetary Fund, that would not go to the extent that we have given up, which is the institutional phase of the

EMS. I said in my paper that nobody really expects us to make the second step - the institutional step - of the EMS when it was drafted in 1979. What could be this institutional progress? It seems to me at any rate that, in view of the expectations of our public opinions, of our governments, we must be able to achieve something visible, even though I am convinced that what we do between ourselves is very effective, is pregnant with much progress. The question then is what should be the content of an institutional step, or would be the content of a new Basle/Nyborg package? I believe that the content should be that we must try to have ex ante co-ordination more than ex post as we have had in the past. Secondly, I believe that we should have in the same lines, pre-co-ordinated interventions. That seems to me to be the inside of that. For the smaller central banks of the Twelve, for instance, we are often impressed by the fact that we hear afterwards what is the conclusion that, for instance, the Deutsche Bundesbank, the Bank of England, the Banque de France have drawn from the higher meetings and though it can be felt by the Bundesbank, for instance, that it is a hindrance to have a larger co-ordination before action, I think it would be an essential theme. I believe that - and that is difficult to make visible - that further "rapprochement" of our monitoring exercise. As the President, I was impressed by the fact today, for instance, that we saw how much Governors were interested by the idea that we would have a Raymond exercise more frequently and that monthly monitoring should be a combination of the exchange dealers' approach and the economists' approach. Then I add this, knowing that this shall not please Karl Otto - he may consider it as a non possimus - I believe that the next progress we could make would be in the diversification of reserves in our respective central banks and it would mean that, under some conditions and with limitations that would have to be invented, in case flows of funds do create tensions in the EMS because funds that flow out of dollar assets come into DM assets, a sort of recycling should exist and it would have to mean that the Deutsche Bundesbank would accept that part of its reserves would be held in other European currencies. I realise, of course, that many of our currencies, if they are in the package of reserves that must be used by the Bundesbank for intervention, are less usable and therefore they are not a progress, but I suppose there is a certain part that can be considered as reserves that can be held for a longer time and is not necessarily likely to be used for interventions.

This is what I said in order to start the ball rolling, and I will sum it up again. I believe that pragmatic co-operation as we have and which is very useful, must in our report acquire a certain visibility, we must do something, announce something that can be seen. Secondly, that the choice is between an institutional step, a new institution with some definite responsibilities, or a Basle/Nyborg package that we could define together. When you ask me what I could conceivably put into this Basle/Nyborg package, I said a few things that I believe we can say, even though I am not quite sure that this can have a sufficiently high visibility, that it is not too technical, understandable only by central bankers and not by the public opinion - they will say what does it mean your monitoring with the Raymond and Dalgaard groups? I realise that is difficult. That, Mr. Chairman, is my suggestion.

The Rt. Hon. Robert Leigh-Pemberton (589 - 661)

Thank you Mr. Chairman. I must say that I align myself more easily with the original stance of Jean Godeaux than with either President Pöhl or Jacques de Larosière in dismissing the sort of points that Jean Godeaux has made for us earlier on as being an important part of our report. We have acknowledged I think that Chapter I is going to describe the present situation and the progress that we have made. I think at some stage it is perfectly legitimate to point out to Heads of State the sort of progress we could continue to make without institutional or treaty changes. After all, pointing that out could have the modest practical merit that we could make some progress even if Heads of States are unable to agree on any of the rest of our proposals - let's hope that that is not so. There is that merit, I think, in the sort of points that Governor Godeaux has made. The discussion is immediately pointed up, of course, the point at which institutional change has to be made. I suppose one could describe that as the point at which maybe we crystallise events by seeking some sort of treaty change. My own feeling is that we have to be very clear in our minds about what we are doing before we actually do recommend or negotiate, or succeed in obtaining, a treaty change. I am inclined to think that we need to get used to what we have developed under Basle/Nyborg, building on that where we see a need, and also getting used to the changes in our environment that 1992 will bring, before we can really clearly see what

form of institutional change will be needed to achieve the eventual goal of economic and monetary union. It seems to me important to retain some flexibility about the form of monetary union and how to get there. Of course it is sensible to set out the intended course, but to make sure that we don't hinder changes to that course that might come to be seen as necessary in the light of experience. I would like to suggest that treaty amendment should not take place earlier than is absolutely necessary. It seems to me that we can take important early steps, such as greater ex ante co-ordination of policy which do not treaty amendment, in contrast to which treaty change - at this stage at least - might be a form of Pandora's box.

Let us go back to Governor de Larosière's paper, which presents a very useful step-wise approach and also allows I think for a learning process. I don't know that it is absolutely essential that we need to have a learning process of this nature, and I hope he won't mind it if I say that we need to be careful that we are not creating some sort of part-time central bank and then looking around for tasks for it to carry out until we have really reached the stage of proper monetary union. Could I suggest, Mr. Chairman, that the time to set up the institutional framework is once there is the political will for it to do a real job and to achieve something that national central banks jointly and severally cannot do. Could I put this way, in the form of a question, at what point does a centralised foreign exchange or money-market function provide added value, that is value over and above what can be achieved jointly and severally by national central banks? Governor de Larosière's proposal is an extremely interesting one, but will it be able to function effectively alongside national central banks who simultaneously it would appear will be continuing to operate their own monetary policy and may also simultaneously be operating their own exchange rate policy? It may be that the existence of this intermediate body will reinforce the processes of national central banks, in which case it will be a step in the right direction. If actually it is always reinforcing those policy actions by the national central banks, we have almost reached total union. If we have not then it seems to me that there will always be dangers of counter policies coming from one or other national central bank as against what the European Reserve Fund - or whatever title it may have - is undertaking. It may be that we can avoid such conflict between national banks and the European Monetary Fund, if so we will have very nearly got to total union.

M. A. Lamfalussy (662 - 825)

Thank you Mr. Chairman. I would like to make a few observations, which were inspired by reading Jean Godeaux report and Jacques de Larosière's proposal, and I think I will try to raise a few questions and try to answer some of them, not all of them certainly at this stage. As I see it the first practical step - and I am talking about that and not about the final stage - its main objective should be what I think Jean Godeaux described, especially here today, namely that somehow we should move from what I may call ex post information on policies and very occasional ex ante information or ex ante attempt of co-ordination towards something that is more explicitly ex ante co-ordination of policies in two fields - monetary policy and exchange market intervention. These are clearly two interconnected areas, on the one hand monetary policy is the single most important short-term determinant of exchange rates - it is not the exclusive determinant but the single most important short-term determinant of exchange rates - and secondly, exchange market intervention unless it is completely sterilised has an automatic impact on domestic monetary policy. The two areas are interconnected and that is why I very strongly approve Jacques de Larosière's approach of dealing with these two simultaneously because they are interconnected. You may have views on which should precede which and how to organise it, but the two have to happen together in some sense because they are functionally interconnected. If this could be regarded as the objective of the first step - moving from ex post more to ex ante co-ordination - then the next most important question is with what degree of institutional set-up? My own answer is that we need some institutional arrangement. Theoretically speaking, of course, in both these fields you could imagine that the Committee of the Governors could suddenly decide that until now we have talked to each other about policies and now we decide to consult each other before the policies. I think this is conceivable but it is not a very practical thing to do, it would not be credible at all to the public because the first question the people would ask is why is it that you haven't done it so far? Secondly, you would run into a number of other difficulties concerning the other participants in the policy measures, which are Ministries or Treasuries, in varying degrees of institutional commitment in the various countries. I think we need some sort of institutional arrangement for that but that, of course, raises all

the thorny questions that have not yet been addressed, i.e. what does it mean in terms of legislative changes; what does it mean in terms of procedures; how can one, nevertheless, respect the autonomy of decision-making on a national level, etc.?

The next step of my observations concerns I think a very important difference I would introduce between monetary policy co-ordination process and intervention co-ordination process, and there is I think one basic very important difference which can be very easily seen if I take the example of today. I didn't attend your meeting this morning but I know more or less what has happened and I know what the views are. Clearly we are moving towards a very favourable economic development in practically all of our countries, there may be dangers of overheating in some of the countries and that clearly could be an argument in favour of some monetary restraint. That is something that probably could be the outcome of an analysis of today and then the question immediately arises, well how should this be done in advance, can we look at it in such a way that one doesn't do too much and the other doesn't do too little? This is an objective thing that can be discussed in these circumstances and one could then try to get some sort of agreement, covering the next two, three, four months, that one looks ahead. If you look at the exchange rate situation, whilst you can make some guesses you can make no more than guesses, no-one knows what the dollar is going to do even in half an hour - whether it goes up or down - and it is very difficult to have any sort of peacefully concerted advance concertation about intervention policies. I think one has to treat these two areas in a rather different way.

Let me start with monetary policy for two reasons, partly because I believe that it is perhaps less daunting to imagine some sort of ex ante co-ordination, and also because I think in a certain sense it is the underlying problem for exchange rate determination. I don't want to put on the table any particular suggestion as to how this could be done, but I think you need some sort of institutional weight behind it, there ought to be some sort of agreement which has to be reached, which need not be shared by everyone but which should be known and should be brought to the attention of the national authorities. How you do that is something one has to look into.

When I come to the exchange market intervention part that is to my mind a much harder nut to crack. There are several reasons. I do agree

that the approach taken by Jacques de Larosière is an interesting one and probably - but I would like to reserve my judgment - the most practical I can imagine at this stage, because this sort of institutional set-up has an image effect, there is no doubt about it, or a signal effect, call it whatever you may, and of course it provides also a training ground for effective co-operation. It does raise a number of very difficult questions to answer. The first series of questions are really, you may call them technical questions, but they are extremely important in their practical effects and quite - for obvious reasons Jacques de Larosière didn't consider them because that was not yet the stage - but I may perhaps mention two or three of these practical questions that arise.

If you have a pooling of reserves what do the central banks get against the reserves which they sell to the joint institution? Are you going to get ECUs or what? Is it a sort of ? type of arrangement or the FECOM type of arrangement but in a final sense and not in a swap sense? This is not a minor question because all central banks are interested to know if they sell some of their reserves what they get in exchange, I think that is a fairly normal preoccupation. The answer you give to that question can have a number of very important impacts on the working of the institution itself.

Another question that arises immediately, and it follows from the answer you would give to the first question, is about the working of the profit and loss mechanism of the pooled reserves. How do you share out the profits and the losses, because there will be both, probably in a certain sequence?

These things can be written down and analysed very coolly and has to be done. I am not suggesting these are insuperable questions but of course they have to be dealt with.

Then I come to the second group of questions which to my mind I don't quite frankly see the answers. That is the decision-making process and the degree of competence of the managers or of the joint management of these pooled reserves in the field of intervention. You can imagine two sorts of options. You can imagine that the pooled reserves and the intervention carried out by these pooled reserves happen in a sort of agency function, that somehow the governors or the central banks give instructions to this reserve centre to carry out intervention, in addition to what they have decided themselves anyhow. Whatever you do in this

respect does raise the very difficult question of the technical speed of the intervention decisions. Here is the point that I wanted to make: while you can look ahead for monetary policy co-ordination on a longer perspective, you cannot talk about any practical intervention unless you are ready to explain who takes what decision and with what speed. You may give broad indications but these broad indications usually reveal themselves as being completely unrealistic the next day, so one has to tackle the practical problem in that respect. You could imagine then to leave to this fund a certain autonomy of decision-making in the intervention, but if you do that then you come up with the following alternative. Either you give them genuine autonomy for \$x billion, in which case you come up immediately against the barrier of domestic monetary policy because if you intervene in dollars you have to buy something or sell something against and you will disturb either the Deutsche Mark or the Dutch guilder or someone else, and that creates immediately a domestic monetary problem. Or else you can do it for very small amounts and you say well the amounts are so small that they don't really disturb domestic monetary policy, but then what is the purpose of the operation? These are very difficult questions to settle and I frankly at this stage don't see the answer, although I have an instinctive sympathy for the idea of the institutional approach, because if you don't do it on an institutional basis the danger is that you don't do anything at all. As a practitioner, which is the hat I am wearing at the moment, I wanted to put these preoccupations on the table.

Dr. W.F. Duisenberg (904 - 1005)

Thank you Mr. Chairman. A few statements. The end which we are striving for is economic and monetary union and I am in full support of that. One of the main characteristics of that we also agreed is that the task of a monetary authority in that context is the promotion of price stability, i.e. external price stability, exchange rates and internal price stability, and we should never forget that. I think also that these two - external and internal - can never be split, you cannot go after the one forgetting about the other. What we are discussing now, and I think there is a real difference in approach under the surface at least, is how to get there - the steps. One approach - Governor de Larosière's approach I think

to be very specific - is the way of transfer, of partial instruments (partial transfer of instruments, i.e. intervention mechanisms partially, maybe even interest rates partially) to a central body (maybe governed by governors or part of the governors), but it is a partial transfer of instruments. The other way it seems to me, and that is the way which has my support, is that of increasing centralisation of the decision-taking on general monetary policy, that includes exchange rate policy and domestic policy, but increased centralisation of decision-taking. In the words of M. Lamfalussy what we have now is ex post information, sometimes ex ante information, sometimes even as he said efforts to ex ante co-ordination, but not more than that. Then it seems to me there is something artificial in not discussing what steps the governors could take further on and what steps would require decisions by governments and institutional changes. I think there is a gradual process also there.

The reasons I am not very much in favour - not at all if I am honest - of the first avenue of partial transfer of instruments are the following. It is impossible to think of making interventions by other bodies than the national central bank or decisions on interest rates with a view towards exchange rate manipulation, without having that implications for the room for manoeuvre for domestic monetary policy and domestic interest rate movements. Interventions have money market consequences and most of the time they are only effective if they are also accompanied by interest rate measures and both are of utmost importance for the behaviour of the growth of the money supply, for example. Then you come to the goal of price stability, in other words I do not believe in a sort of dichotomy, a split between measures or instruments with an external impact and those with an exclusively internal impact on money supply and interest rates. In the proposals as we have before us, both M. de Larosière's proposals and also some of the thoughts of Mr. Thygesen, that is in first place as I said centralisation of instruments which are in the domain of the exchange rates, interventions and to a degree interest rates. That implies the danger as I see it that this central monetary authority or European Central Bank, or the nucleus thereof - whatever you might call it - puts the accent of its work, of its functioning, too much on the external side, exclusively on exchange rates, forgetting thereby the domestic, the internal, monetary implications which are also the results of the use of instruments in that. So exclusively or too much external consideration might determine the

policy and then the danger is large, as long as convergence of economic policies and economic performance has not been drastically improved and as long as exchange rates inside the system are not yet completely fixed, the risk is very large that the European authority would deviate, in my mind, too much from its central mandate, that is the promotion of price stability. I see a great danger there.

Therefore, to sum up, Mr. Chairman, partial transfer of instruments I think will not work, I would be in favour of increased centralisation of decision-taking in the monetary field in general and I do realise that also along that road you will very soon come up against the barriers that they also require institutional changes. If we move gradually in our work, also as a Committee of Governors, towards ex ante co-ordination and binding co-ordination of our policies, there also have to be institutional changes. It is unthinkable, for example let us take the three largest countries, that in the Committee of Governors we would agree that for the sake of price stability or exchange rate stability it would be desirable that in Germany the rates were to be lowered, in France they would remain unchanged and in the United Kingdom they would have to be raised. In all three cases I think to be very specific M. de Larosière would have to consult with his Minister of Finance and so would Governor Leigh-Pemberton and Governor Pöhl would say I agree with it, but it is the Zentralbankrat which makes the ultimate decision. In all three cases there would have to be a fall-back on the existing institutions in the various countries. So even ex ante co-ordination and binding co-ordination of policies would already imply institutional changes, be it by way of international treaty which supersedes the national legislation, be it by changing the respective positions and legal positions of the central banks and central bank governors involved. I think there is no escape in either approach, be it the partial instrumental approach or the approach of increased centralisation of powers, in both cases you would very soon come up against the necessity of having a treaty or at least institutional changes which would have to be underpinned by the treaty. As you notice I very much share the questions or at least the leading questions placed by M. Lamfalussy and given a choice I would be for intensification of the work of the Committee of Governors, realising that also there we would very soon have to go to our governments and say, well, if you want us to intensify our co-operative work further you will have to change the law.

M. J. de Larosière (1008 - 1080) (Interpretation)

Well, Mr. Chairman, I don't think that there is so much of a gap between Mr. Duisenberg's concept and mine. Firstly, in my mind I am not at all thinking of a huge intervention machine - this has to be understood - it is not at all a matter of setting up an intervention fund which would upset domestic monetary conditions, that is not at all my idea. My idea is this. There is a G-7 strategy, let us say vis-à-vis the dollar, it results in greater or smaller interventions, but anyway there is this strategy. My idea is not to innovate, my idea is to say, in addition to interventions undertaken by central banks - and this will happen in the majority of cases - one can practice on the basis of an understanding as to what the G-7 strategy really means, one can practice in making marginal interventions which would go in the same sense as the main interventions as the central banks by using common reserves, and if one does that one would not upset the domestic monetary situation. If one upsets it one upsets it within the more general framework of what has already been "upset" by national authorities because it is really an annex to something which has already been done. Therefore I do not accept that with a huge intervention machine one is going to upset domestic monetary conditions.

There is a great advantage in doing what I am suggesting, at least as I see it. Firstly, there is this message which is sent out as a result of what we do now - maybe you don't like this idea, you don't want to show in a somewhat concrete manner that you are moving in the direction of a future European bank, then I understand that it would be better for my paper to be put into the wastepaper basket and to agree that we shall continue arranging things amongst ourselves. But if one wishes to tell Heads of State, you have asked us to think about a process leading towards European integration, then it is helpful to have some sort of an embryo which would get us to work together. Mr. Lamfalussy was right putting concrete questions, it would be easier at the beginning and probably, because of what he said at the beginning, one would be very timid, one is not going to intervene, for instance, on a day when there is a difference of interpretation between the main operators, one will act when there is already an underlying consensus. It is not a bad thing to do something, it helps one to learn how to work together and it does send out the signal. I like the questions asked by Mr. Lamfalussy because it will force a small

group of people who know one another, who I think quite like one another - the heads of the dealing rooms - to work together and then to report to the governors. It is in this way that the Federal Reserve System started in 1913, it made a small start and, with due respect to what Mr. Leigh-Pemberton said earlier on, once it existed one has started hunting around for things for it to do. Therefore I am not at all upset by the stability objective suggested by Mr. Duisenberg, and he is also right to say that if you leave everything to co-ordination between central bankers at the Committee of Governors, you are going to run into this problem of differences of approach between central banks, the difficulty for them to work together a priori. Of course, I am going to allow Mr. Pöhl to talk, but accentuated co-ordination would pose constitutional problems for him. He has often told us that it is the Bundesbank's Council which reaches decisions and that one couldn't really hold lengthy consultations beforehand, therefore this problem will crop up. If we look at the institutional approach à la de Larosière and the practical approach of Mr. Duisenberg or Mr. Godeaux, if you look at all of this you will see that institutional problems will arise very soon and you will have to tackle them. Since you will have to tackle them anyway, why not make a start? Say that before we have these institutions we have to reinforce co-ordination within the Committee of Governors, yes alright, and I think that this strengthening will have to take place in any case, whether we do anything further or not, but this would not cause any philosophical difficulties for me. I look at this whole exercise in a pragmatic and modest manner, I do not place intervention at the heart of everything but I think it is not a bad thing to start working together.

Herrn K.O. Pöhl (1356 - 1535)

Mr. Chairman, I would like to come back to the question which was raised by Governor Hoffmeyer at the beginning, because I think that is the most important question, at least from a legal and institutional point of view, which we have to have in mind - the political reality in Europe. I fully agree with what he said, that we have to distinguish between two different models which I think we should propose to our principals. The one model is a model which needs a legal framework, call it a treaty, and in this context I think the proposals of both de Larosière and Thygesen

belong, because both proposals, but particularly the one of Jacques de Larosière, could not be implemented without legal changes to the legislation in the member countries. Then I think one has to take seriously the argument which was put forward by Governor Hoffmeyer that you cannot set up a treaty, a framework for a European central bank system, step-by-step because it is not conceivable that you can change the laws, the treaty, every three years. That means, by definition, that gradualism is hardly conceivable. In my view it is unrealistic and not helpful at all if one would suggest that, because you would come up with a fund for intervention, maybe the best under the circumstances, with a small, little, body but that could easily be the end of it, it could be a failure anyway and there is no guarantee that that would really develop into a European central bank system finally. I think it would be much better to draft a design for such a treaty, for such a framework - I am very much in favour of that - and then one should go further than you did, one should really make it a complete European central bank system, defining the tasks, the instruments and the institutional body as a model and telling the Heads of State that this could be a European central bank system one day, but it needs, of course, a lot of further legal, economic, study, etc. because nobody I think is seriously expecting that the European governments or parliaments would be ready today to pass, to transfer, substantial sovereignty rights in this area to such an institution. On top of that you always have in mind that this is not enough, you can have that only if at the same time you have institutional provisions for co-ordinated economic policies, etc. That is a long-term perspective, very useful and necessary, but it cannot be implemented in the near future. That is the one part.

The other part is what can be done without institutional changes of this far-reaching kind. There are two groups, one is the one Jean Godeaux mentioned which already falls in the competence of the central bank governors or in the competence of the finance ministers. As far as fiscal policy is concerned, they have the opportunity to co-ordinate their fiscal policy. We have the possibility, to a certain extent at least, to co-ordinate our interventions in the exchange markets and actually we are doing that, our operators are in touch four times a day if I am not mistaken. There is a very close co-ordination and co-operation within the given framework and of course one can discuss other changes, the kinds Godeaux mentioned, e.g. diversification of reserves, etc. This is nothing

we have to suggest and propose to the Council. There is a second group of changes which one could envisage without changing the law and without setting up a treaty which needs parliamentary approval and would be very very difficult to get through in all member countries - then you get the problem that it doesn't go through in all member countries and do we really want two groups, two classes of members, etc.? There is another kind of group and that is strengthening the existing institutions, in the first place and particularly from our point of view, the Council of Central Bank Governors. The Council of Central Bank Governors was set up in 1964 if I am not mistaken by a resolution of the Council, the Ministry Council, like the FECOM by the way, and if you read the text you see that the tasks of the Committee are very clearly defined in that resolution and I wonder whether one shouldn't go a little more into that legal question of whether the tasks of the Committee as they are defined in the text could not be enlarged by a resolution of the Council, without changing national law and without affecting the competences of national monetary authorities. I think that is a very crucial point because there will be a lot of opposition in all countries to any change - in my country I could easily describe what would come close to a revolution if you would really try to reduce the so-called independence of the Council of the Bundesbank. They have the only right to decide on interest rates, etc., if that should be transferred to an institution in Basle, Strasbourg or Brussels or wherever, it would create a lot of problems. The same would happen in other countries where the finance ministers have that competence which they wouldn't like to transfer to this Committee. The utmost we can hope for is, maybe, at least we can propose it, that the Council of Governors would be strengthened and would get the authority to give recommendations to the national monetary authorities, be it the Central Bank Council in the case of Germany, or central bank plus finance ministry in other countries, giving recommendations in all areas which affect both price stability, monetary stability, exchange rate system, where we are in charge, particularly of course all questions which affect the management of the exchange rate mechanism or the EMS which as you know is our main task - the management of the exchange rate mechanism. So I could imagine that one could grate(?) the Council of Governors, maybe we call it the European Central Bank Council, an anomaly to the German, but that is already beginning to be a little delicate, but to give the whole thing, Jacques, a little more symbolic,

more institutional meaning. Call it a European Central Bank Council, you have a Chairman who would be elected not only for one year but for three years and who could attend the meetings in Brussels, could get a little more profile, etc. and then this Council could give recommendations, let us say on monetary policy in the respective member countries of the EC, on economic and fiscal policy even, if it affects the exchange rate stability, price stability in the EEC. One example for that exercise was this morning, if we would be authorised to send a letter to the German Finance Minister telling him that the Governors have discussed that matter and a great majority came to the conclusion that higher indirect taxes in Germany are not fully consistent with the objective to reduce imbalances in the EMS, I think that would have some effect. I am not sure we have the authority to do that.

Other subjects would be intervention, Jacques, and there I come to your ideas. I don't think we need a fund because that would raise all the legal, institutional questions we have to answer if we set up a central bank system, for instance, to solve the questions of who takes the decisions, as M. Lamfalussy rightly mentioned - it is only one illustration - who takes the decision? In your paper you are saying decisions should be taken in consensus and on a collegial basis, but that is very impractical because you cannot take a decision on intervention if everybody agrees that the EEC style but you cannot pursue monetary policy with consensus amongst twelve members. You raise all these kinds of questions if you set up a new institution, but if we would discuss intervention vis-à-vis third currencies and even if we reach no agreement we could at least say that the majority is of the opinion ... and we give this view to the central banks or the governments who are in charge of intervention. It is different in different countries, in some countries it is the government which decides on intervention - in most countries I think - and in other countries like in Germany it is the central bank. There is another area where we, as an upgraded Committee of central bank Governors, could give advice in a very delicate area, but I think we should be courageous, and that is exchange rates. I wonder why that hasn't been mentioned in the whole context? If we really want to achieve more stability in the EMS - well maybe it was mentioned, but not in your paper for instance - we cannot rely on intervention alone, of course, we need better convergence of fiscal economic policy but if that does not happen we need from time to time

realignments, if we don't need any realignment then we have reached the state of a monetary union. That is fine but not very likely to happen in the next couple of years. I can easily conceive situations in which we as central bank Governors come to the conclusion that further or even more intervention in the exchange markets would get in conflict with our monetary targets with the main objective of monetary policy, i.e. to maintain price stability. Mariano, I don't think the central banks are created to operate in the exchange markets, that is not the main task of a central bank, at least not in my country. (Rubio: they were in the 19th Century.) Maybe, but in the Bundesbank law which was only approved in 1957 and is a little more modern, it is said expressively that it is the main task to maintain the stability of the currency. If that would get in conflict - interventions in the exchange markets - we could maybe ask the governments to change the exchange rates. I have no illusions, Jacques Delors and myself tried to persuade the Ministers to give this authority to this group but as you know we didn't succeed. Frankly speaking I never expected to succeed, it was more a kind of provocation, but necessary maybe to show how difficult it is to transfer powers from one institution to another. We could suggest that at least we examine whether the exchange rate pattern is reasonable, appropriate, I think there is no better institution than the Council of Central Bank Governors to come to an objective judgement and if we would come to such a conclusion that would be very rare of course and wouldn't happen very often, but let us assume we would say with these surplus' in Germany the best thing to do is to have a little realignment. With this kind of approach we would avoid a lot of problems which are in my view not solvable and which are raised in your proposal, Jacques. For instance, the problem of voting rights. Is it really a good proposal from our group to say that only central banks who participate in the ERM are allowed to participate in this fund, or in other words, you can only be a member of the fund and participate in this decision-making process, European co-ordination process, if you participate in the exchange rate mechanism. It would be a very strong political decision if one would say that, if the Council would say that, and if we would propose it. I would hesitate to make such a political proposal. In my suggestion this problem would not appear because we could give a recommendation on exchange rates including our British, Spanish, Greek and Portuguese colleagues, we could give a recommendation even without reaching

a full agreement. That I think has some advantages. I think there are a lot of other advantages, the only doubt which I have is - and I have to check that with my lawyers - whether such a decision of the Council saying that we give the authority, adding to Article 2 of the Council Decision of May 1964 two or three paragraphs saying that we, the Council, authorise the Council of Governors, which we will call the European Central Bank Council in future, to set up a Secretariat maybe and to give recommendations on all these subjects to those national authorities which are responsible. Whether that is possible, in the case of Germany I don't know, in other countries and I would be grateful if you would maybe check that also, without rather far-reaching changes in legislation. I think it is possible, there will be an uproar, if I think what happened when this German/French Council was established, but in my view and my judgement something like that would still be within the given leader framework conceivable. That is what I wanted to add to the discussion at this point. Maybe if you want me to write that down in more detail, particularly with the legal aspect, I am fully prepared to do that and to provide you with not a long paper, not 50 pages this time, but a little paper on that subject.

M. J. de Larosière (1535 - 1621)

I am sorry to intervene perhaps a little more than I usually try to do in these meetings, but as it is my paper which has been the focus of this discussion I feel entitled to say a few words if only to tell you what I have in mind. I understand what you say when you say that my concept, to use a short expression, is not compatible with gradualism, that is the argument made by Mr. Hoffmeyer which you followed up. I agree with the following qualifications and understandings. It is perfectly correct to say that the institutional changes that are implied by my proposal are destined, are intended, to be completed, supplemented, by further institutional changes in the direction of full monetary integration. In this respect I fully agree with you both when you said that you are proposing something that is a part of a whole dynamics. But, and here I would make my qualification, I would very strongly say that the different steps towards this full monetary integration have to be staged, staggered, and that each of the steps will have to be the object of probably unanimous agreement by all the members concerned by, or participant in, the general

endeavour. You could imagine that if the consensus was not there, to move towards the final stage you would indeed have only an initial or some preliminary steps without the remainder following. I would also agree that that would be an incomplete outcome of what I had in mind.

Secondly, I understand very well what Karl Otto was saying and I appreciate what he has been putting on the table because it is an effort to put a little more precision in what can you do with this Committee of Governors, how can you beef it up, put some muscles and teeth in it and make it a little more credible and effective? I appreciate that because it goes in the right direction. With due respect, I don't think it is exactly what we have been asked to do, because one of the great merits, as you said, of your proposal is derived from something that I am not extremely impressed by and that is that it doesn't involve legislative changes, it does not complicate the political settings nationally, it is compatible but you are not even sure that it is compatible, you are going to have to study that, it is more or less compatible with the present setting. On this I have an intellectual reservation. We have been asked by the Heads of State, whether we like it or not, and I may well understand that some of us have other profound problems with the whole exercise, but we have been asked to make some proposals or write a report on the subject: how do you reach monetary integration and economic integration? Although it is a very realistic thing to say let us try and see how we could go in that direction without changing anything of the legal setting, I am very much in favour of what Mr. Ciampi said, we have an historical opportunity to answer that question and if we start by saying we are going to answer it in a way that doesn't disturb anything in the present setting, I think we haven't really done what we were asked to do. I think we can develop these ideas and show them that would look like that, but I don't think you could really argue that this is a major determining criterion in our work. (Pöhl: Jacques you forgot the first part of my proposal which was ...) Yes, but I have a little bit of suspicion here that if you put my proposals in the same bag - and you very artfully do that with some of your friends - this is the utopian thing, OK you have got the very far-away utopia of Mr. Thygesen's report and even the more further one that you have asked him to work on and then you put de Larosière in that because that is one parcel, and then you have the realistic guys who are going to suggest that we beef up the monthly meeting in Basle. Now, you haven't said that and I would perfectly

admit that I am being a little bit provocative in putting it that way, but you see we have to also look into the institutional aspects, as Carlo Ciampi said, if we have good ideas on the contents, on the substance, then let us look at the legal aspects. We are not parliaments today and we are allowed to look into these things. I am going to tell you something which is a little bit the reverse of what you have in your own view: it is clear that what I am suggesting in my paper implies, I didn't put it that way but it does imply, a very profound modification of the relationship between the governing body of the Banque de France and the Ministry of Finance. In my view it is absolutely clear, I didn't stress it but it is there. I would like that to happen and I know there will be upheaval in the Treasury, but it is also something we have to see as the positive side. Don't you think Europe would be stronger with central banks that would be more independent, autonomous, in a structure like the one I described than not to change anything in the legal aspects and to sort of muddle through? (Pöhl: that is a little bit unfair, because these proposals would have some weight ...)

Now, I am going to be completely unfair on my last point and then I will shut up. When you say that it is a bit provocative not to make two categories of countries, those who are in the ERM and those who are not, I would say that I explained that it was a logical out-grow of what I had in mind. I wouldn't see very well how a country that is not in the narrow band could really mix into those types of decisions on inter-European currency interventions. In a way, you said that it is a very political proposal to leave them out, I would say that it is a very political decision for them to have been left out of the ERM and of course they are welcome in.

M. P. Jaans (1653 - 1705)

The European Council has asked us to say how to come to monetary union. We have discussed what monetary union is, it basically means fixed exchange rates and freedom of capital movement, and I think this Committee has to indicate quite clearly to the European Council that the way to get there implies the creation of a mechanism of decision - of common decisions and of binding decisions - and these decisions have to be taken under a specific mission, which also has to be defined clearly and legally, i.e. the maintenance of internal price stability and eventually in the countries the institutional frameworks and relationships between the Treasuries and

the central banks would have to be changed, but the important thing is to state quite clearly that we cannot, so to say, steal ourselves around on that road, around a common and binding mechanism of decision-making. One will probably have to give a description of how that mechanism has to look and even if it is a disgrace ... (Pöhl(?): is that in the first step?) Well, I think in our report and the first step on that road really is to have a political consensus that that is the road. One may now postpone the moment when the decisions made in ? become binding in a couple of years or some time horizon, but I think it would not be responsible on the part of this Committee to say that there is a kind of half-hearted, partial, way of coming to something where the public might believe it could be a monetary union. I think one has to be quite clear about the political price in terms of amending sovereignty which is pay there. (?)

With regard to the implementation of such decisions, I think we can have, of course, all kinds of recipes and instructions like the ones presented by Prof. Thygesen or Governor de Larosière, but the aim being coming to fixed exchange rates, these common decisions can very well be implemented through the existing central banks and the common decisions can be limited to what is necessary to come to fixed exchange rates or to the stability of exchange rates. That means basically interventions and it means interest rates and interest rate differentials, eventually also realignments. To come on that road - and one of the difficulties in our discussion I think is how to slice it into stages, since in the mandate the word stages or steps is used. Why not slice that in a gradual narrowing of the bands? If one aims at stability of exchange rates, at some stage one will have to abandon the $2\frac{1}{4}$ thing we have now and one will have to decide whether we go to zero right now or whether we go to one or whatever - but that may well be the road. The final stage, which should be described or outlined at least - a final architecture so to say of a European Central Bank - that need not be indicated that it should be there by 2000 or 2010, but if through the decision mechanism and its implementation through the existing central bank, one comes to a stage where the parities are durably fixed, then it can be simply an enabling decision for central banks to merge in a joint venture or whatever. That would be just one way and I think at this stage that is not so important.

With regard to this mechanism of common decisions, of course, we could take as a point of departure the Committee of Governors, but it would

be a totally different Committee of Governors with regard to its competences. Just an upgrading, so to say, of the present Committee of Governors without the necessity for legal changes, possibly, I would even hesitate to offer that kind of thing in the report because that is the kind of slippery road to steal out, so to say, politically. I think that would immediately be seized as a way out and insofar I am not so convinced about the second part of your exposé, President Pöhl (... it's a good session!) since the real road, the sincere road, probably has a number of political difficulties but why shouldn't politicians acknowledge that there are difficulties there.

The approach by Governor de Larosière, of course, has the merits of having a kind of learning institution, but again since it is only a partial thing, the risk is that it could be seized, all the more so as it is visible - that seems to be a very important concern. It would be visible but it could stay very partial and become less and less visible, so to me that way is a little too homeopathic perhaps. That was all I wanted to say at this stage. (M. Lamfalussy: What is your ? - only one jump?) No, actually the road to monetary union, that is to fixed exchange rates, could well pass through the existing central banks with common decision-making at some level and through a gradual narrowing of margins, and that can be left to the central banks.