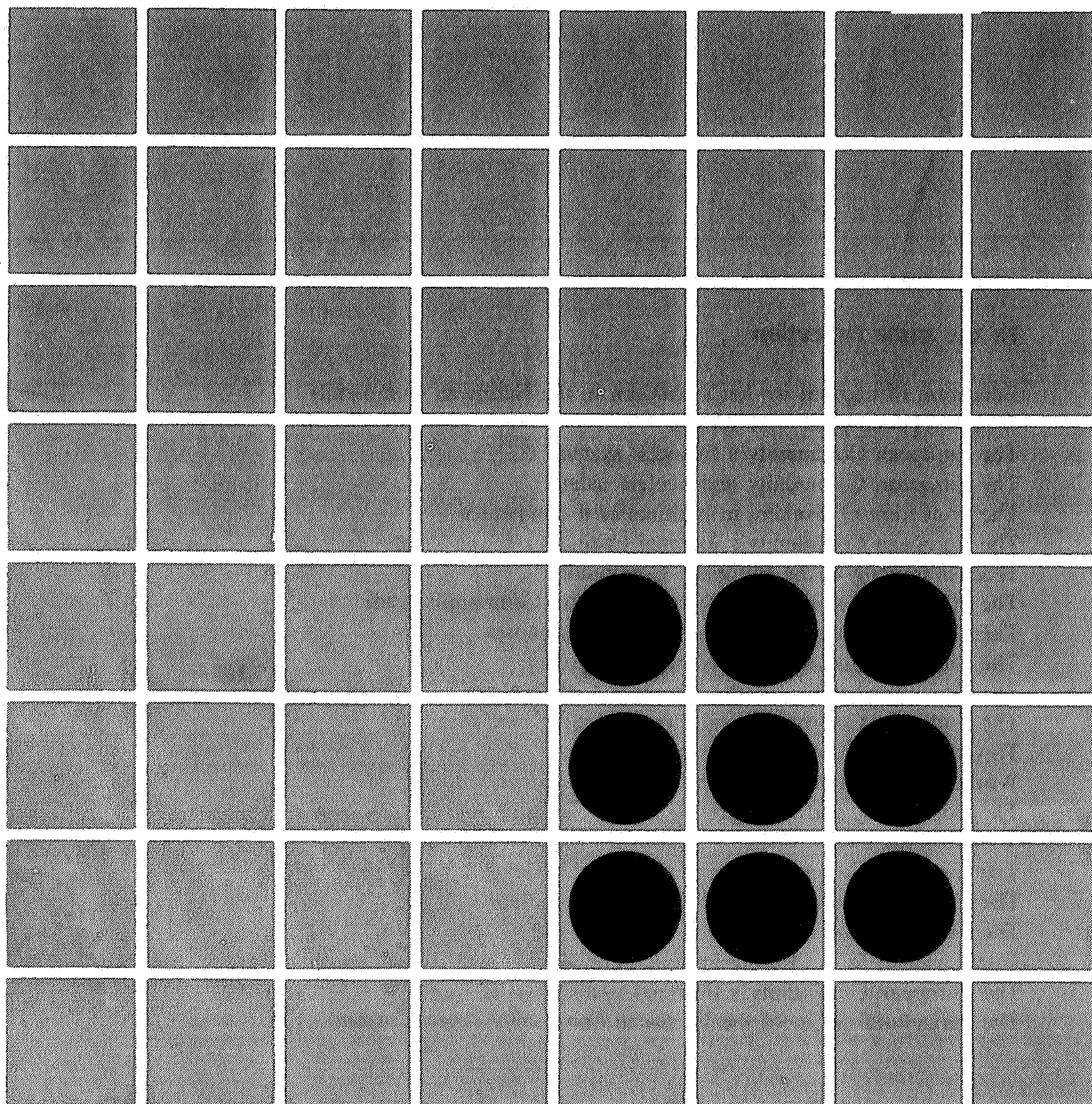
European economic and monetary union



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I — WHY DOES EUROPE NEED ECONOMIC AND MONETARY UNION?

In its most extreme form, economic and monetary union means a single economy and a single currency, with centralized economic decision-making. The architects of the European Economic Community (EEC), who drew up the founding Treaty of Rome in 1958, believed that free trade between the member countries would lead progressively to greater economic union, but they made no specific provision for its attainment. Instead they concentrated on achieving a customs union and drew up a 12-year, stage-by-stage plan for the dismantling of intra-Community customs barrier. But it soon became clear that the Community could not stop at free trade and that, for their own sakes, the Member States would have to look beyond their customs union as growing economic interdependence pointed to the need for greater economic and monetary integration.

1. **Interdependence of highly industrialized economies**

The customs union, achieved ahead of schedule in July 1968, was a resounding success and intra-Community trade in goods and services expanded rapidly — now accounting for half of Member States' total foreign trade as against one third in 1958. During the same period, Member States' foreign trade increased 275% in real terms and now accounts for no less than one quarter of gross Community product (ie. one quarter of the aggregate amount of all services supplied and goods produced in the nine countries). In some member countries (Ireland, Belgium, the Netherlands and Luxembourg), the share of foreign trade actually exceeds 50%, while the figure for Denmark is 33%. In the Federal Republic of Germany and the United Kingdom, the share has risen from around 20% to just under 30%, while in Italy and France the figures are around 25 and 20% respectively.

A quarter of the manufactures, farm products, and services produced by the 258 million people living in the Community are exported, and, as a result, foreign trade accounts for a quarter of the income of the Community's population. However, this crucial last 25% of their income is highly vulnerable as long as frontier posts remain in existence and as long as currency exchange rates can fluctuate sharply enough to price a country's products out of foreign markets altogether. The EEC customs union has eliminated the fear that tariff barriers between Community countries might be restored overnight against member countries' goods, perhaps depriving entire industries of their export markets. By contrast,

it has not managed to prevent excessive exchange rate fluctuations, which can have a similar, if not greater, disruptive impact on trade than customs duties. As a result, intra-Community trade is still fraught with uncertainty despite the fact that the customs union has brought about an unprecedented degree of interdependence between the Member States of what is a highly industrialized Community.

The fact that the Member States already carry out 50% of their foreign trade with one another reflects a degree of mutual reliance never before witnessed in history. Indeed, Ireland and the three Benelux countries carry out between two-thirds and three-quarters, and France, Italy, Denmark and the Federal Republic of Germany half of their trade with other member countries. The United Kingdom is the exception, transacting two-thirds of its foreign trade with non-member countries.

Given this high degree of interdependence, a customs union alone cannot provide the necessary long-term security: one pillar cannot suffice indefinitely to support the edifice formed by the objectives laid down in the Treaty, namely improvement and alignment of living standards and uniform development of all regions without structural imbalances and distortions to competition. To this end, what is needed is the economic union which is advocated in the Preamble to the Rome Treaty and which itself cannot be attained without monetary union. Only within such a union can the convertibility of all member countries' currencies at fixed exchange rates be guaranteed thus preventing money market fluctuations distorting competition and intra-Community trade.

The authors of the Treaty were quite content initially to urge in general trems coordination of monetary policy 'to the full extent needed for the functioning of the common market' with each Member State undertaking to 'pursue the economic policy needed to ensure the equilibrium of its overall balance of payments and to maintain confidence in its currency, while taking care to ensure a high level of employment and a stable level of prices'. In addition, each member country was to regard its exchange rate policy 'as a matter of common concern'. It was only at the summit conferences of the Heads of State or of Government held in the Hague in December 1969 and in Paris in October 1972 that the objective of creating an economic and monetary union within ten years and also of striving to achieve European Union was defined in concrete terms.

2. Securing growth and full employment

This major venture had, however, to be embarked on in the midst of a major crisis in the international monetary system by a Community that was also preparing for the accession of Denmark, the United Kingdom and Ireland. With little or no synchronization of national economies and no Community exchange rate system to ensure monetary cohesion, the currencies of the nine Member States making up the newly-enlarged Community also diverged in the wake of the successive international monetary crises.

Those Member States whose currencies were substantially revalued were compelled to adjust their economies to the higher rate, to neglect branches of the economy with lower value added and to undertake as much rationalization as possible. As a result, they now possess an efficient and modern industrial structure but for the time being there is a serious shortage of customers for their sophisticated products and services. The Member States