

**MÓNETARY COMMITTEE
OF THE EUROPEAN COMMUNITIES**

**TWENTY-FIFTH REPORT
ON THE ACTIVITIES**

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Twenty-fifth report on the activities

I. Introduction

1. The world economic scene brightened up during 1983 and the major industrial economies returned to a path of real growth. Economic activity in the United States recovered first and grew strongly. In Europe too, expansionary forces gradually gained strength although with differentiation among countries.

2. The slightly faster pace of activity in Europe was spurred principally by the improvement achieved in the underlying domestic conditions for growth in certain countries. It was also supported to some extent by the expansion in the United States. However, for the EEC as a whole during 1983, the recovery remained well below that in the US and did not halt the further rise in unemployment.

3. For the Community as a whole in 1983, GDP grew by about 1.0% in real terms. This growth performance and the divergences within the Community reflected the staggered introduction of adjustment policies. The Member States whose corrective policies were most advanced registered the first signs of economic recovery. The main external factor influencing the Community's performance was the improvement in world trade, to which the US made a substantial contribution.

4. The Community was confronted during the whole of 1983 with difficult external and internal problems. World-wide interest rates began to rise again from their already very high levels and presented a grave danger for the development of balanced and sustainable growth. Although they did not prevent the revival of economic activity, they constituted a serious burden and a risk for the continuation of the recovery. Internally the Community countries strove to improve their fiscal performance in order to strengthen the groundwork for lasting economic growth.

5. Within the Community and especially among EMS countries, the orientations, particularly of monetary policy, in Member States became increasingly convergent; in most Community countries, measures were pursued to correct the imbalances on the external account, budget positions and inflation. Among the most encouraging developments in 1983 was the continuing fall in inflation. Every EMS country with an external deficit had an improvement in its current account during 1983 and, for most, the improvement was substantial. The aggregate budget deficit for the Community as a whole fell slightly as a percentage of GDP in 1983 as some Member States made important progress in consolidating their public finances.

6. Monetary policy in several Community countries was easier than in 1982 and was also easier — especially in the first half of 1983 — than originally expected. This development was associated with improving performance of fundamental economic

variables. However, in a number of countries the continued heavy recourse to foreign borrowing to cover internal and external disequilibria, the high level of domestic credit expansion and, in certain countries notably credit to the public sector, or the risk of overshooting the quantitative monetary objectives, remained a factor of concern. In the second half of 1983 monetary expansion decelerated so that for the year as a whole most countries met, or only slightly exceeded, their targets.

7. As a whole 1983 saw a strengthening of the EMS, although the exchange rate mechanism again underwent severe temporary strains. Indeed the economic adjustment policies applied up until then proved to be insufficient to achieve lasting convergence in the economic fundamentals of the EMS countries. This led to the general realignment of 21 March 1983, resulting in a shift between the extreme currencies of about 9%, compared with about 10% in June 1982. The realignment was accompanied by additional stabilization measures: in particular the French Government reinforced its adjustment package so as to consolidate the new EMS parities. The resulting convergence in policy orientations in a more favourable external environment progressively strengthened the EMS during the remainder of the year. In general, the EMS has continued to contribute to intra-European exchange rate stability during a period of international monetary turbulence and to more equilibrated balance of payments situations.

II. Community actions and the activities of the Committee

8. Against this general economic and monetary background and with a view to achieving more monetary stability through the smooth functioning of the EMS and through other forms of international cooperation, the Committee organized its work around the following main themes: the monitoring of general economic developments and the examination of monetary and financial policies in the Community with a view to encouraging further convergence of economic performances; the analysis of the international monetary environment and of the effects of the economic policies implemented by the Community's main partners, especially in the area of exchange rates; common Community positions with regard to the activities of international organizations.

9. The Committee's work concentrated as a matter of priority on the economic and monetary trends and policies both in the individual Member States and at Community level. In early 1983 severe tensions arose within the EMS exchange rate mechanism, due to the continued large differences in cost and price developments, which were reflected in heavy pressures on weaker currencies, especially the French franc, calling temporarily for massive intervention. After strenuous negotiations a general realignment took place on 21 March 1983. The realignment of the French franc was accompanied by a programme of internal economic adjustment designed by the

French Government to correct the current account of the balance of payments and reduce inflation, so as to break out of the vicious circle of devaluation and inflation. The programme adopted by the French authorities was also in the interest of the Community since it strengthened the cohesion of the EMS and accorded with the view, strongly held by the Monetary Committee, that it is in principle desirable that new EMS parities be supported by internal adjustment measures towards monetary stability; indeed such practice has become more frequent in the recent past. On 16 May 1983 the Community granted France a loan of 4 000 million ECU as support towards correcting its balance of payments difficulties. These adjustment measures and those taken by other Community member countries helped the balance of payments and other economic fundamentals during 1983 to become basically more favourable for an extended period of exchange rate stability within the EMS.

10. An important task of the Committee every year consists in examining the economic and financial situations in the Member States. This allows members to take into account each other's economic and monetary experience and thus indirectly influence policy decisions in the individual member countries. The Committee's work in these areas contributes to the coherence of economic and monetary policies and hence to the convergence towards monetary stability in Europe. The object of these examinations is to identify both potential economic or monetary problems in order to discuss possible remedies.

11. As usual, the Committee held an *ex-ante* exchange of views towards the end of the year on the targets which the monetary authorities of the Member States adopt and it followed closely the actual development of monetary aggregates. Monetary policy continued to be a key element in the policy mix of the Member States' economic policies. There was some easing of monetary conditions in the majority of EEC countries in the early part of 1983 when monetary and credit growth was rapid and sometimes volatile. During the second half of the year, however, there was a slight firming of monetary policy, though this only partly compensated for the evolutions earlier in the year. The developments in the first part of 1983 can be traced essentially to domestic factors, although speculative capital movements before and after the EMS realignment in March contributed to the uneven and volatile growth profile of the monetary variables. By mid-year there was a progressive deceleration in monetary expansion in most EEC countries, strengthened by action from monetary authorities, so that the money supply or credit targets set in the large EC countries for 1983 were attained or slightly overshot.

12. The country examinations and the discussions on member countries' monetary policies are important catalysts for coordination within the EMS. In such a way a consensus forms on the diagnosis of the problems and on the general direction of economic and monetary policy required. The points of reference for the orientation of national monetary policies are the developments in the counterparts of the money supply in member countries. A schematic view of the circumstances in 1983 brought out two aspects of particular interest to the Committee:

- (i) In countries with large deficits in the balance of payments on current account, it is not enough to ensure that the rate of monetary expansion is apparently consistent with the guidelines; the expansion of domestic credit and the external counterpart of monetary creation must also be closely monitored. A strong expansion of domestic credit reinforcing the trade deficit and supporting outflows of capital is incompatible with a balanced development of the economy.
- (ii) In countries where public sector borrowing is the main source of monetary creation, the achievement of monetary expansion consistent with stability represents a very difficult problem: the choice is between, on the one hand, reducing credit to the private sector substantially and, on the other, accepting excessive domestic credit expansion while continuing to tolerate the destruction of liquidity by external transactions; indeed, both alternatives may be adopted simultaneously. More intensive recourse to non-monetary financing for the public sector is a first step towards putting things right; by putting upward pressure on long-term interest rates this course reveals clearly the fact that the financial demands of the public and private sectors are in competition for the limited supply of savings. In the final analysis, the only solution will be to reduce the public deficit.

13. The Community's aggregate current account improved further in 1983. This was due mainly to the success of some EEC deficit countries in reducing external imbalances under the impact of improved competitiveness and lower domestic demand resulting from the adjustment measures taken. Accordingly, there was a welcome convergence in developments on Member States' current accounts, also reflecting, in part, changes in countries' cyclical positions. In 1983 organized borrowing abroad by EEC deficit countries was smaller in volume than in 1982, although sometimes remaining heavy and well in excess of current account deficits.

14. In view of the unstable and unbalanced world-wide pattern of exchange rates experienced in 1983, the Committee devoted considerable attention to analysing the reasons for these developments and their consequences for the Community, in particular with respect to the US dollar, whose rise was viewed with concern. Exchange rates which do not reflect fundamental economic factors will have a negative effect on the production and allocation of resources and on trade flows and will also increase the danger of protectionism. Moreover, balanced economic policies geared towards a non-inflationary and lasting growth lead to benefits both domestically and for the rest of the world. This is especially relevant for the US authorities, the impact of whose policies is of such dominating importance for the monetary and economic situation of other countries, in particular those countries which are heavily in debt. The Committee was particularly worried by the continued high US budget deficit and the prospect that it will continue to go uncorrected despite widespread agreement, even in the United States, on the necessity for a substantial reduction in the deficit.

15. In accordance with its general responsibilities, the Monetary Committee continued its task of coordinating the policies of Member States in the field of international monetary relations. It examined in 1983 in particular the monetary and

financial questions raised during the preparation of Unctad VI and, in this context, emphasized the important role of the Bretton Woods institutions, the IMF and the World Bank, without which the international monetary problems cannot be solved. As to the general problem of indebtedness, a long-term remedy to excessive indebtedness can only be found by applying sound domestic policies notably under the auspices of the IMF and by creating the conditions for a stable world-wide recovery. In particular there is no ground for revising the principle of case-by-case treatment of debt difficulties, for example within the Paris Club, whose effectiveness has been widely demonstrated.

16. As in past years the Committee contributed to the formation of common Community positions for the spring and autumn meetings of the Interim Committee of the (IMF) and for the annual meetings of the Fund and the World Bank. In preparing the statements to be made at these meetings on behalf of the Community, the Monetary Committee stressed that the viability of the world financial system is linked to the freedom of world trade. The Community remains firmly committed to an open multilateral trading system, and despite the present international difficulties it will continue to pursue a trade policy that ensures the openness of its markets.

17. The IMF has an important role to play in strengthening efforts to ensure a world recovery and a return to economic stability through surveillance of exchange rate policies and as a source of temporary financing. This temporary financing should aim to promote adjustment and serve as a catalyst for complementary financial flows from other official and private sources. The Committee reaffirmed that the Fund's primary source of financing should continue to be quota subscriptions, and that the revolving character of its balance of payments support should be preserved.

18. The Committee welcomed the solutions and the generally satisfactory compromises found in 1983 for many of the problems concerning the activities and financing of the Fund, in particular concerning the eighth review of quotas and the GAB. The solution to the Fund's financing problems by means of new credit lines arranged mainly under the aegis of the BIS found support. In this context Saudi Arabia's contribution was welcomed. At the same time it was regretted that not all industrial countries considered it possible to take part in the joint effort.

19. The Committee stressed the importance of an adequate transfer of resources to less developed countries and in this context it is important that the International Development Association be provided with a sufficient level of funding in order to enable the Association satisfactorily to continue its action in support of the poorest countries. The efforts made by the management of the IDA to mobilize additional resources were followed with special interest.

20. Finally by the end of 1983 it was noticeable that remarkable and effective adjustment measures were being taken in many developing countries in conjunction with the Fund. Continued support from the international community, including the

Fund and the World Bank, is needed to ensure that these countries will be able to adjust in a way enabling them to regain the momentum of growth and development. Support is critical, in particular for those least developed countries which have limited production potential and few basic resources.

List of members and alternates of the Monetary Committee

Chairman

J.M. Camdessus Directeur du Trésor (Paris)

Vice-Chairmen

Sir Kenneth Couzens Second Permanent Secretary, HM Treasury (London)
(until 5. 1. 1983)

Dott. L. Dini Direttore Generale, Banca d'Italia (Rome)
Prof. Dr P. Korteweg Thesaurier-generaal bij het Ministerie van Financiën
(The Hague)

G. Littler Second Permanent Secretary, HM Treasury (London)
(since 6. 1. 1983)

Dr H. Tietmeyer Staatssekretär, Bundesministerium der Finanzen (Bonn)

Members

M.J. Balfour Assistant Director, Bank of England (London)

D. Chalikias Vice-Governor, Bank of Greece (Athens)

Prof. T. Dimopoulos Special Adviser, Ministry of Coordination (Athens)

(until 8. 2. 1983)

M.F. Doyle Secretary, Department of Finance (Dublin)

(since 16. 12. 1983)

Dr L. Gleske Mitglied des Direktoriums der Deutschen Bundesbank
(Frankfurt-am-Main)

P. Jaans Directeur Général, Institut Monétaire Luxembourgeois
(Luxembourg)

G. Janson Directeur à la Banque nationale de Belgique (Brussels)

Ph. Jurgensen Directeur-adjoint, Ministère de l'économie (Paris)

E. Kestens Directeur général, Ministère des finances (Brussels)

(since 11. 3. 1983)

R. Kirsch Conseiller du gouvernement, Ministère des finances
(Luxembourg)

D. McCutcheon Department of Finance (Dublin)

(until 16. 12. 1983)

Dr P. McGowan Assistant General Manager, Central Bank of Ireland
(Dublin)

R. Mikkelsen Member of the Board of Governors, Danmarks
Nationalbank (Copenhagen)

J.P. Mingasson	Director, Directorate-General for Economic and Financial Affairs, Commission of the European Communities (Brussels)
T. Padoa-Schioppa (until 31. 3. 1983)	Director-General, Directorate-General for Economic and Financial Affairs, Commission of the European Communities (Brussels)
A. Prate	Premier sous-gouverneur de la Banque de France (Paris)
M. Russo (since 5. 4. 1983)	Director-General, Directorate-General for Economic and Financial Affairs, Commission of the European Communities (Brussels)
Dott. M. Sarcinelli	Direttore Generale, Ministero del Tesoro (Rome)
Dr A. Szasz	Directeur, De Nederlandsche Bank NV (Amsterdam)
S. Thomadakis (since 9. 2. 1983)	Adviser, Ministry of National Economy (Athens)
N. Ussing	Kommitteret, Det økonomiske Sekretariat (Copenhagen)
J. van Ypersele de Strihou (until 10. 3. 1983)	Chef de cabinet du Premier ministre (Brussels)

Chairman of the alternates

J.-J. Rey	Sous-Directeur, Banque nationale de Belgique (Brussels)
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Alternates

Dr D.H. Boot	De Nederlandsche Bank NV (Amsterdam)
P.J. Bull (until 6. 10. 1983)	Bank of England (London)
Dr F.A. Engering	Ministerie van Financiën (The Hague)
G. Fitchew (since 5. 9. 1983)	HM Treasury (London)
Dr W. Flandorffer	Bundesministerium für Wirtschaft (Bonn)
R. Floc'h (until 23. 4. 1983)	Banque de France (Paris)
R. Granet (since 24. 4. 1983)	Banque de France (Paris)
J. Guill (since 1. 9. 1983)	Institut Monétaire Luxembourgeois (Luxembourg)
Mrs M. Hedley-Miller (until 4. 9. 1983)	HM Treasury (London)
G. Kamas	Bank of Greece (Athens)
J.E.W. Kirby (since 7. 10. 1983)	Bank of England (London)
G. Malakis	Ministry of Coordination (Athens)
Y. Mersch (since 22. 2. 1983)	Ministère des Finances (Luxembourg)

Dott. S. Micossi
(since 2. 8. 1983)

J. Ovi

D. Quigley

G. Reynolds

Dr W. Rieke

R.P. Rigaud

(until 14. 5. 1983)

Dott. F. Saccomanni

(until 1. 8. 1983)

D. Samuel-Lajeunesse

(since 15. 5. 1983)

M. Schmit

(until 21. 2. 1983)

J. Thomsen

J. Vanormelingen

P. Zimmer

(until 31. 8. 1983)

Dott. A. Zodda

Banca d'Italia (Rome)

Danmarks Nationalbank (Copenhagen)

Department of Finance (Dublin)

Central Bank of Ireland (Dublin)

Deutsche Bundesbank (Frankfurt-am-Main)

Ministère de l'Economie (Paris)

Banca d'Italia (Rome)

Ministère de l'Economie (Paris)

Ministère des Finances (Luxembourg)

Det økonomiske Sekretariat (Copenhagen)

Ministère des Finances (Brussels)

Institut Monétaire Luxembourgeois (Luxembourg)

Ministero del Tesoro (Rome)

Secretariat

Dr A. Kees

R. Barthélemy

C. Boyd

(since 16. 5. 1983)

Secretary of the Committee (Brussels)

European Communities

Washington, 10 February 1983

Statement by Mr G. Stoltenberg, President of the Council of the European Communities, to the IMF Interim Committee meeting

1. Since the Federal Republic of Germany is at present exercising the Presidency of the Council of the European Communities, I have the honour of presenting to you the Community's views on the economic outlook and on Fund issues.
2. The global economic picture is becoming more differentiated. The current setting remains critical and unemployment has reached intolerable levels. Nevertheless the underlying conditions have improved in some important respects and, with appropriate policies, there is a reasonable hope that, during the year, business activity will gradually improve, and that, over the medium term, a more satisfactory, sustainable rate of growth may be resumed.
3. The economic climate is still one of widespread uncertainty. Uncertainty has been created by repeatedly disappointed hopes for economic revival, by the tremors in the international financial system, by pressures for protectionism and by the behaviour of exchange and interest rates. The rigours of economic adjustment are straining the social and political fabric of societies. Particular hardship is involved for the developing countries which are beset with the multiple problems arising from weak demand for their exports, deterioration of their terms of trade and increased financial strain.
4. However, in some fields, considerable adjustment has taken place and further improvement is under way. Inflation, in a number of industrial countries, has markedly declined. Along with strengthening price performance, interest rates, though still very high in some instances, especially in real terms, have come down. Energy constraints have eased. At great sacrifice and in spite of the difficult international environment, substantial internal and external adjustment has also been achieved by developing countries.
5. Although the world debt problem remains a cause of real concern, the immediate, acute tensions have been reduced. An effective cooperation of governments, central banks and international financial institutions has contained the damage to the international financial system and the countries involved. And, with the assistance of the Fund, progress towards more lasting solutions has been initiated. This cooperation should be continued.
6. Economic recovery would go a long way towards easing present financial strains. An important prerequisite for sustained growth, however, is greater market

