<u>Confidential</u> (Translation)

MINUTES*

OF THE 225th MEETING OF THE COMMITTEE OF GOVERNORS OF THE CENTRAL BANKS OF THE MEMBER STATES OF THE EUROPEAN ECONOMIC COMMUNITY HELD IN BASLE ON TUESDAY, 10th MAY 1988 AT 10 a.m.

Those present at the meeting were: the Governor of the Banque Nationale de Belgique and Chairman of the Committee, Mr. Godeaux, accompanied by Mr. Janson, Mr. Rey and Mr. Michielsen; the Governor of Danmarks Nationalbank, Mr. Hoffmeyer, accompanied by Mr. Mikkelsen; the President of the Deutsche Bundesbank, Mr. Pöhl, accompanied by Mr. Gleske and Mr. Rieke; the Governor of the Bank of Greece, Mr. Chalikias, accompanied by Mr. Papademos and Mr. Karamouzis; the Governor of the Banco de España, Mr. Rubio, accompanied by Mr. Linde and Mr. Durán; the Governor of the Banque de France, Mr. de Larosière, accompanied by Mr. Waitzenegger and Mr. Cappanera; the Governor of the Central Bank of Ireland, Mr. Doyle, accompanied by Mr. O'Grady Walshe and Mr. Reynolds; the Governor of the Banca d'Italia, Mr. Ciampi, accompanied by Mr. Dini and Mr. Masera; the President of De Nederlandsche Bank, Mr. Duisenberg, accompanied by Mr. Szász and Mr. Boot; the Governor of the Banco de Portugal, Mr. Tavares Moreira, accompanied by Mr. Pêgo Marques; the Governor of the Bank of England, Mr. Leigh-Pemberton, accompanied by Mr. Loehnis and Mr. Price; the Director-General for Economic and Financial Affairs of the Commission of the European Communities, Mr. Costa, accompanied by Mr. Louw; Mr. Kees, Secretary of the Monetary Committee; the Director General of the Luxembourg Monetary Institute, Mr. Jaans. Also present at the meeting were Mr. Raymond and Mr. Dalgaard, Chairmen of Groups of Experts. The Secretary General of the Committee, Mr. Morelli, his Deputy, Mr. Bascoul, Mr. Scheller and Mr. Cook, and Mr. Bockelmann and Mr. Dagassan also attended.

The <u>Chairman</u> opened the meeting by proposing that items II and V of the agenda be discussed at the same time in view of the links between the subjects covered.

^{*} Final text approved at the meeting on 13th June 1988, which incorporate some drafting changes.

I. Approval of the minutes of the 224th meeting.

The <u>Committee</u> unanimously approved the minutes of 'the 224th meeting, on the understanding that the editorial amendments suggested would be incorporated in the final text.

- II. Monitoring of economic and monetary developments and policies in the EEC based on:
 - Preparation by the "Dalgaard Group" and discussion by the Committee of Alternates;
 - Statistical charts and tables.
- V. Examination of current monetary policies in EEC member countries based on Report No. 32 of the group of experts chaired by Mr. Raymond. Adoption of a mandate for the "Raymond Group" concerning the improving of monetary policy co-ordination between EEC member countries.
 - A. Statement by Mr. Dalgaard

The dollar had continued to move within a narrow band whose limits, from November 1987 to the beginning of May 1988, were \$1 = DM 1.65 and 1.70. In mid-April it had recorded a brief decline following the publication of the US foreign trade figures, but this had been quickly halted by quite substantial, concerted interventions by several central banks. The stability of the dollar had been helped by two factors: the markets' perception that the central banks would not allow the dollar to fall much further and the rise in short and long-term interest rates in the United States. This upward trend had spread to some other countries, in particular France and Germany, at least as far as long-term interest rates were concerned. It could still not be ruled out that the dollar would fall further later, for example if inflation were to rekindle in the United States, if there were further unfavourable US foreign trade figures, or if the Federal Reserve appeared hesitant as to the policy to pursue, in particular as regards accepting higher interest rates.

The yen had continued to appreciate also vis-à-vis the European currencies and had returned almost to its level of the summer of 1986 vis-à-vis the Deutsche Mark. Within the EMS there had been some movement in the relative positions of currencies, and some interventions had been made. Overall, however, the situation had been calm, particularly when it was considered that there had been elections in two countries, viz. France and Denmark. In fact, the French elections appeared to have had a greater influence on the Italian lira than on the French franc, which had not experienced any tensions. The authorities had let the exchange rate slip, but only very slightly; there had been no interventions; and interest rates had not been changed.

The Italian lira had weakened from mid-April onwards, and sizable interventions had been made in the market. Substantial outflows of capital had in large measure represented a reversal of the inflows which had occurred in the wake of the reintroduction of exchange controls in 1987; by this means the Italian banks had reduced the exchange risks they had incurred.

The political tensions in Denmark in mid-April had resulted in a slight weakening of the Danish krone and some firming of market interest rates, but the calling of elections and the election campaign had not had any impact on the exchange rate.

The other EMS currencies had remained stable. All in all, the experience of April and the beginning of May had been satisfactory and had shown that the flexible deployment of the various instruments could be highly effective; in particular, it appeared that even modest exchange rate movements within the band had a considerable stabilising effect. These positive results had been possible because the market did not anticipate a realignment in the near future and assumed that, even were there to be a realignment at a later date, it would be a minor one and would probably leave market rates more or less unchanged. In this situation the market tended to focus on small variations in interest rate differentials. In the three countries already mentioned, viz. Denmark, France and Italy, non-resident capital inflows had persisted right up to the elections, taking advantage of the high rates of interest.

In the Netherlands the introduction of a system of compulsory reserves had been announced with the aim not of tightening monetary policy but of enabling De Nederlandsche Bank to retain its influence on short-term interest rates.

Outside the EMS exchange rate mechanism, mention should be made of two currencies. The pound sterling had remained strong; pressure had eased somewhat with the fall in oil prices and the rise in interest rates

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in some countries, but recently sterling had strengthened further. In the longer term, however, it was expected to weaken. The Spanish peseta had appreciated further, and the Banco de España had made sizable purchases. The 0.7% increase in the consumer price index in March, much larger than expected, had led to a rise in market interest rates, resulting in fresh inflows of capital and a firming of the exchange rate.

The "Monitoring Group" had also discussed the question of the choice of intervention currencies on the basis of the situation in April, when there had been at the same time sizable sales of Deutsche Mark by the Banca d'Italia and substantial purchases of that currency by the Banco de España. This situation had not given rise to any real problems, but the group was agreed that in future intervention policies should be better co-ordinated and that there should be closer co-operation between the central banks concerned.

B. Statement by Mr. Raymond

The development of the economic situation was undoubtedly more favourable than expected, but the financial and exchange markets were nonetheless not immune to further disturbances.

For its part, the European Community was encountering some particular difficulties of its own.

Firstly, it appeared to constitute an area of lower growth within the OECD group and was, unfortunately, likely to remain so. It could suffer as a result of a more aggressive posture by the Far East and improved American competitiveness. Some EEC countries, in which the growth of domestic demand had been too rapid, now had to restrain it. In the countries subject to the narrow-band exchange rate regime, the forecasts did not predict any overall acceleration. This was understandable for those of them which had balance-ofpayments difficulties. It was a different matter in the case of Germany, where the authorities considered that at present they had little scope for a relaxation of monetary policy or for greater fiscal stimulus. This standpoint, which had been put to the group by the representatives of the Deutsche Bundesbank, had met with differing reactions.

Secondly, the European Community still suffered from insufficient convergence in certain economic fundamentals.

Price convergence was making progress, with a slight acceleration in the rise in prices in countries with close to zero inflation and a further curbing in the high-inflation countries. On the other hand, certain countries

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with close to 4% inflation did not envisage any improvement, which would mean, for example, the persistence of a gap of several percentage points vis-à-vis Germany, possibly giving rise to problems with the exchange rate relationship against the Deutsche Mark.

In the field of current payments, the reduction in the German surplus was continuing in volume terms, but this improvement (from the adjustment point of view) was masked by terms-of-trade developments. It was to be feared that the surplus in value terms would decrease only very slowly in the coming years and, moreover, that the overall deterioration in the Community's current account, already referred to indirectly in connection with Asian and American competition, would affect the countries already in deficit just as much as Germany.

What could be envisaged to reduce these divergences which, over time, could threaten parity stability? A first instrument was monetary policy; Chapter II assessed its current stance. Neither the results nor the degree of constraint exerted on the real economy appeared to have changed much in the last six months. The monetary aggregates, generally the broader ones, were growing faster than predicted or desired. This was due in part to a preference of economic agents for assets bearing short-term market rates of interest in a period of uncertainty about the future of long-term rates, which appeared to be firming, and in part to an acceleration, the rate and recency of which varied between countries, in the growth of domestic lending.

Monetary policy was considered to be relatively accommodative in Germany, where the monetary aggregates, even the narrower ones, had now been growing rapidly for over two years. Conflicts had emerged between external and internal objectives in the United Kingdom and Spain, where it had been necessary to lower short-term rates, despite domestic overheating, because of the growth in the foreign exchange reserves.

The current monetary expansion was not considered a threat to the credibility of monetary policies, at least in the immediate future. However, it did warrant a degree of caution for the future, as had been pointed out by the Group in its previous reports.

The German representatives felt that they had now practically exhausted their room for manoeuvre, given both the accumulation of liquidity in the economy and the low level of nominal interest rates reached. Some

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other members of the Group were of the opinion that the German authorities were in a position to be flexible.

In those countries with a deteriorating current balance the view had often been expressed that a further raising of already high interest rates would be detrimental to the already weak rate of growth in Europe.

These discussions showed that there was little hope of seeing any major spontaneous adjustments in monetary policies with a view to strengthening the convergence of economic performances. The same could be said with regard to fiscal policies, even though the situation in some countries still required correction because the deficit or public-sector debt remained high. Germany, for its part, considered it had taken a step towards international adjustment in 1987 but did not feel it could move any faster, especially in 1989, a standpoint which was questioned by some.

However, the members of the Group considered it dangerous to create a situation in which the burden of countering divergences and exchange market tensions rested solely on the instrument of monetary policy. They had also urged that structural reforms such as would improve the overall efficiency of the European economies should not be neglected.

C. Statement by Mr. Janson

1. The Alternates had taken into consideration:

- the oral report presented by Mr. Dalgaard, which focused essentially on the current situation on the exchange markets; and at the same time
- Report No. 32 of the "Raymond Group" which had a longer-term perspective and dealt chiefly with more fundamental questions.

The Alternates had noted with satisfaction that the current exchange market situation, both within the EMS and worldwide, was free of major tensions, but they were concerned about certain developments that might cause disturbances in the future.

2. With regard to the current situation the Alternates had noted in particular:

 the psychological impact of the co-ordinated interventions carried out on a large scale when the dollar was suffering a bout of weakness in the wake of the publication of less satisfactory current-account figures; in the view of the Alternates it was

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necessary to seek to maintain this psychological impact as far as possible;

- the fact that within the EMS the election period had passed without any major tensions; this good performance was attributable not only to the flexibility of interest rates but also to progress in convergence, especially between France and Germany;
- the need for close and frequent consultation on the choice of intervention currencies, in particular among the central banks that were signatories to the EMS Agreement.

3. As far as the longer-term outlook was concerned, the attention of the Alternates had been focused on two problems:

- the rise in long-term interest rates, which had so far been more marked in the United States than in Europe and had had the effect of widening long-term interest rate differentials;
- the Community's inability to achieve stronger economic growth and a higher degree of convergence among member countries, which carried the risk of engendering tensions at the international level and within Europe (which was the principal argument of Report No. 32, as M. Raymond had just pointed out).

Given the role played in this context by the economic policy pursued by Germany, the Alternates had considered it essential to hear the opinion of the German representative. Mr. Gleske had made an interesting statement. The Alternates had noted with satisfaction that the Bundesbank did not intend to alter the stance of its monetary policy at present and that it did not consider the rate of growth of the monetary aggregates to be a factor likely in itself to jeopardise price stability. The Bundesbank's representative had pointed out, however, that a close watch had to be kept on the rapid pace of monetary expansion insofar as the pressures coming from the real economy indicated a certain deterioration in the climate of price stability.

The Alternates had also noted that, again in the opinion of the German authorities, the low rate of growth in Germany had its origin in demographic and structural factors. A policy of stimulating domestic demand would therefore be unlikely to remedy this problem. As far as monetary policy was concerned, any action by the authorities aimed at lowering shortterm interest rates would prove counter-productive since it would entail,

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through the intermediary of inflationary expectations, a rise in long-term capital market rates.

On the other hand, it had been noted that a tightening of monetary policy could be counter-productive: a rise in interest rates would contribute to capital inflows (or a reduction in capital outflows) and thus serve to increase liquidity. At the same time, the rise in interest rates would have repercussions throughout Europe. Such an impact could only be avoided at the cost of greater exchange rate variations, both within the EMS and internationally. Greater exchange rate flexibility, however, would not be in the interest of the European countries; it would not serve the purpose of greater convergence and would have adverse consequences for the management of the EMS.

D. Discussion by the Committee

Mr. Duisenberg offered some explanations regarding the introduction of a system of compulsory reserves in the Netherlands. Hitherto, the Nederlandsche Bank had used the two instruments of official discount and lombard rates and quantitative credit restrictions, but it also wanted to be able to influence the yield curve in the long-term sector. To that end, an agreement had been reached with the Government, and the central bank would be able to carry out open market operations in the long-term sector; in an initial stage it would build up, over a period of eighteen months to two years, a portfolio of government securities amounting to around Fl. 3 billion. Given that it was not a question of financing the budget deficit, the total of short-term Treasury paper held by the banks would be simultaneously reduced by a comparable amount. This would result in an increase in banks' liquidity and, with their agreement, this additional liquidity would be frozen by means of the compulsory reserves during the transitional period. Once the portfolio of government securities had been built up, the Nederlandsche Bank would be better able to influence long-term capital market interest rates.

<u>Mr. Pöhl</u> expressed his satisfaction that the issue of interventions and of their co-ordination had been discussed by the "Monitoring Group"; exactly that subject fell within its brief, and it was the duty of the central banks to co-ordinate their efforts to stabilise exchange rates within the EMS and also against the dollar. Within the EMS, there were

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clear rules of procedure governing co-ordination, written rules laid down in the Agreement establishing the EMS and in the Basle/Nyborg Agreement of September 1987. These rules stipulated that, for interventions in EMS currencies, whether purchases or sales, the consent of the central bank issuing the currency used was required. These rules were fundamental and had to be respected by all the members of the Community, both those participating in the exchange rate mechanism and the others.

The remarks made by Mr. Raymond and Mr. Janson, in particular regarding the lack of convergence within the Community, deserved to be looked at more closely. Admittedly, there was a lack of convergence as far as current accounts were concerned; the disequilibria had even increased slightly as a result, in particular, of the fall in the price of oil and natural gas. It was necessary to consider also the development of domestic demand and inflationary pressures and to concentrate on the current accounts rather than external trade, since the former included intra-EEC transfers and tourism, which were very large components. It was debatable whether, as had been pointed out, the existing substantial imbalances posed a threat to the stability of the exchange rate mechanism. That was perhaps true in the long term, but in the short term there did not appear to be any tensions in spite of those external imbalances and the holding of elections. It would be interesting, nevertheless, to look more closely at the reasons for this calm. The imbalances did not entail tensions or problems as long as they were offset by capital movements. Those movements should not represent simply lending or borrowing but, above all, direct investment, and the deficit countries should improve the conditions for direct investment in them.

It was also debatable whether it was necessary to reduce the external imbalances, and what would be the best way to go about it. Adjusting the exchange rate was one way but, for very good reasons, that was more or less out of the question at present, and in any event minor adjustments had no effect on the current-account balance. Nonetheless, the exchange rate was still an appropriate and classic method of correcting external imbalances. The other method, which consisted in taking action in the areas of general economic and budgetary policy, did not fall within the province of the Governors. They should make it clear that the principal aim of monetary policy was not to put right the errors of budgetary policy but to maintain price stability. In that respect, German monetary policy was if anything

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expansionary, judged by the monetary aggregates and the low level of interest rates. Thus, even if that meant there were no margin for manoeuvre, for the moment there were no plans to change this accommodative attitude.

The <u>Chairman</u> remarked that the Governors had emphasised on several occasions the need for better co-ordination of interventions and had pointed out that the communication channels for this existed. The question was thus in what form, and in what forum, could improved co-ordination be achieved in concrete terms.

<u>Mr. Rubio</u> said that Spain did not participate in the exchange rate mechanism and thus did not have the same legal obligations; however, it did inform its partners of its interventions and had avoided purchasing Deutsche Mark during periods of tension or pressure. Moreover, there were times when it was necessary to intervene very swiftly and when prior notification or prior consultation was impossible. These problems should be discussed in a more general context. Thus, the problem of interventions was linked to that of the composition of reserves; Spain had, in fact, a lot of dollars for the size of its economy, and did not want any more. The Banco de España was therefore prepared to discuss all these issues, in particular the aspect of reserves composition, which had never previously been raised, and was ready to present its case and to listen to the others.

<u>Mr. Tavares Moreira</u> expanded on a number of remarks concerning Portugal in Report No. 32. The Report suggested, for example, that the slowdown in the growth of the monetary aggregates had been less than forecast. In fact, the slowdown had been in line with projections in connection with various factors, such as inflows of capital, public sector indebtedness and the reclassification of certain bank deposits held by non-resident Portuguese. It was true that, in the current inflationary environment, the inflexibility of monetary policy instruments had made it impossible to reduce monetary growth further, but the central bank should soon have more flexible instruments at its disposal. As far as the Portuguese current account was concerned, the mention of a substantial deterioration in 1988 should be corrected insofar as the current account was nonetheless forecast to remain in surplus to the tune of around \$600 million.

<u>Mr. Duisenberg</u> wondered whether there were not some misunderstanding on the part of Mr. Rubio in respect of interventions. Article 15 of the EMS Agreement did, indeed, stipulate that interventions in Community currencies could only be carried out with the consent of the issuing central bank, but that rule bound all the signatories to the Agreement and not just those participating in the exchange rate mechanism.

<u>Mr. de Larosière</u> observed that, in addition to the legal aspect which Mr. Duisenberg had just mentioned, there was a more general aspect. It would, in fact, pose a great danger to the balance of the EMS if the European central banks were to intervene individually in the currency of their choice for any desired amounts with the intention of modifying the composition of their reserves. Such a policy would have very disruptive repercussions on the members of the exchange rate mechanism, who were obliged to maintain very close relationships at all times between their exchange rates and that of the Deutsche Mark, for instance. There was a real problem there, which had been raised some time ago, under different circumstances, with their colleagues from the United Kingdom.

<u>Mr. Pöhl</u> followed up the remarks made by Mr. Duisenberg and Mr. de Larosière by recalling that the EMS Agreement of 13th March 1979 was general in application, which meant that all the signatories were obliged to respect it, not simply the members of the exchange rate mechanism. Furthermore, the Governors had always been in agreement on the principle that interventions should be co-ordinated. To that end, a telephone network had been installed and four concertations took place each day. It had all worked very well, and within this framework several central banks, such as the Banque de France, had accumulated considerable holdings of Deutsche Mark in consultation with and, in short, with the consent of the Deutsche Bundesbank. Such a rule was fundamental to the EMS, and also to co-operation within the G-7 countries. Clearly, one central bank could not be expected to buy dollars while others were buying Deutsche Mark.

<u>Mr. Rubio</u> expressed surprise at and disagreement with Mr. Duisenberg's intervention and his interpretation of Article 15 of the EMS Agreement of 13th March 1979. He voiced his conviction that the Banco de España had respected its legal obligations under the Agreement by providing the required information on its operations in the framework of the concertation system; in his opinion, the Agreement did not involve any other legal obligation for the Banco de España since the latter was not subject to the discipline of the exchange rate mechanism. He added that he did not believe the legal aspect was the most important one; on the contrary, he believed the economic aspect was, and he noted that in this respect the Banco de España had supported the US dollar strongly in 1987 and during the early months of 1988 by absorbing a very considerable proportion of the dollars accumulated by the EEC central banks. He also indicated that the Banco de España was ready to collaborate with the other EEC central banks at times of crisis and to discuss problems related to intervention currencies and the composition of reserves if it was wished to study this question in its entirety.

<u>Mr. Hoffmeyer</u> recalled that the concertation telephone network had been set up within the EEC at the beginning of the 1970s precisely for the purpose of enabling the member countries to co-operate; it was only later that other countries, in particular the United States and Japan, had been connected. Consultation before intervention was a permanent principle which had always been followed.

In the experts' Report No. 32, the question of the stability of the EMS which had been addressed raised two principal issues, namely the development of the competitive capacity of the European countries and that of their balances of payment, in particular the German foreign trade surplus. As far as competitiveness was concerned, the results and the conclusions which could be drawn varied depending on the criteria used, the rate of inflation, the GDP deflator or unit costs. In spite of the technical difficulties involved, it might be interesting to take hourly labour costs, and, based on this criterion, the conclusions might be less negative than those in Report No. 32. The German foreign trade surplus was still worrying. Economic growth in 1988 would indeed be more vigorous than forecast, perhaps rising as high as 3%, which might explain the increase in industrial exports from Denmark to Germany. However, two comments should be made. Firstly, the State of Schleswig-Holstein, adjacent to Denmark, was a depressed area with a high unemployment rate, and it was therefore very difficult to export there. Secondly, projections for growth and the current-account surplus in Germany in 1989 were somewhat pessimistic and might entail an adjustment of exchange rates.

The <u>Chairman</u> referred to Mr. Pöhl's remarks on the disequilibria within Europe vis-à-vis Germany and on the possible remedies. European countries did not seem to be performing very well on the German market, since the growth of their exports was weaker than that of countries outside the EEC. A theoretical or textbook solution consisting in the adjustment of

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exchange rates had been put forward, but one had to realise that prices were not the only factor to have a bearing on competitiveness. The case of Belgium was significant in this respect: its currency had appreciated vis-à-vis the French franc and depreciated in relation to the Deutsche Mark and the Dutch guilder, but Belgian exports to France were growing faster than those to Germany and the Netherlands. It therefore appeared that modification of the exchange rate parities was not the only means of correcting external imbalances and certainly not the most important one.

<u>Mr. de Larosière</u> noted that this varied performance of Belgian exports was due to the fact that the growth of domestic demand was faster in France than in Germany.

<u>Mr. Pöhl</u> acknowledged that the five German research institutes were predicting a slowdown in economic growth in Germany in 1989, which was partly associated with the increase in taxation that had been announced. This, however, was an area for which the Ministers of Finance were responsible. In addition, it might be desirable to tell the Ministers that the existing disequilibria could not be corrected either by modifying exchange rates - which the Governors considered inappropriate under the present circumstances - or by monetary policies. Other methods had to be implemented by the governments.

The <u>Chairman</u> recalled that the Governors had to adopt a mandate for the group of experts under the chairmanship of Mr. Raymond on the improvement of monetary policy co-ordination and that the Alternates had studied this topic and proposed a draft dated 9th May 1988.

<u>Mr. Janson</u> pointed out that the Alternates had, in fact, studied three drafts proposed by various central banks and attempted to synthesise them. The result was the draft of 9th May 1988; the first four items were based on a consensus, but there had been no agreement on item 5 and three versions had been submitted to the Governors: the first tended to represent the argument put forward by the Banque de France and the Banca d'Italia, the second was drawn from suggestions made by the Bank of England, while the third was an attempt to find a compromise by the office of the Chairman.

<u>Mr. Leigh-Pemberton</u> appreciated the fact that the draft submitted by the Alternates contained the second version of item 5, but he would accept the third version, which clearly explained what the "Raymond Group"

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should do; in addition, he suggested a few minor improvements to the wording of the English version of the mandate.

<u>Mr. de Larosière</u> pointed out that he concurred with Mr. Leigh-Pemberton and therefore favoured the third version of item 5; he proposed, however, that the term "emergence", which was really very vague, be omitted and that the French read "to facilitate the discussion of the monetary policies envisaged with a view to developing a co-ordinated approach".

<u>Mr. Ciampi</u> specified that his preference was for the first version of item 5 but that he would accept the third; in addition, he suggested that in English the term "fostering" be replaced with a slightly more dynamic word like "developing".

The <u>Chairman</u> noted that the Committee had agreed to adopt the mandate for the "Raymond Group", having accepted the third version of item 5 and the editorial changes proposed by Mr. Leigh-Pemberton, Mr. de Larosière and Mr. Ciampi. (See Annex 2, final version of the mandate.)

In reply to a question from the Chairman, <u>Mr. Raymond</u> pointed out that the mandate which had just been adopted by the Committee seemed to him appropriate for the work of the group of experts. The group had already to some extent anticipated the Governors' wishes by giving indications in Report No. 32 of Europe's relative position vis-à-vis the rest of the world and devoting quite lengthy discussions to the theme of convergence. The mandate could therefore only strengthen the willingness of the experts to continue on this path. It would, however, be desirable if the Governors informed their experts that they were free to discuss the topics and that they were not participating in the work merely as advocates of the policies pursued in their own countries.

III. Adoption of the Committee's report to the EEC Ministers of Finance on developments on the foreign exchange markets of the nineteen countries participating in the concertation procedure during April and the first few days of May 1988.

The <u>Chairman</u> took note of the Committee's approval of the "concertation report", which would be submitted as usual to the EEC Ministers of Finance.

IV. Continuation of the exchange of views on the monetary structure of Europe, based on the draft report by the Chairman of the Committee of Alternates and the discussion the Alternates will have on this subject on 9th May 1988.

The <u>Chairman</u> recalled that the President, Mr. Stoltenberg, had distributed the agenda for the next informal meeting of the ECOFIN Council, to be held in Travemünde on 14th May 1988, in which it was planned that the Chairman of the Committee of Governors would present a brief oral report on European monetary co-operation. It was with this imminent objective in view that the Alternates had worked at their meeting on the Monday and that the Governors should embark on a discussion.

A. Statement by Mr. Janson

Mr. Janson began by saying that he had distributed to the Alternates a second working document whose purpose had been, and was now, to summarise and review the areas that had already been the subject of exchanges of views by both the Alternates and the Governors in April. It was, therefore, not a text to be approved as a report by the Chairman of the Committee. However, the Chairman would have to make a brief report to the Ministers; on the basis of the discussions that had been held up to the present, this report might draw on the following outline, taking into account any remarks the Governors might now make.

"1. The Governors have conducted an initial exchange of views regarding the ideas contained in the memoranda to which they have been asked to give their attention.

2. The questions raised are fundamental ones which relate both to the present operation of the European Monetary System and to the future of the European monetary structure. A study of these questions demands considerable preparation and the Governors' observations are confined at this stage to the procedure to be followed for their examination.

3. The Governors note that many of the questions raised relate to areas that lie specifically within their competence.

A number of aspects of the desired strengthening of the European Monetary System have already been the subject of decisions on their part within the framework of the Basle/Nyborg agreements; moreover, the Governors have taken the necessary steps to take further their examination of other aspects, linked to the full liberalisation of capital movements, in particular possible ways and means of improving the co-ordination of monetary policies. (This the Governors had just done by giving the mandate to the "Raymond Group".)

4. The Governors intend to examine the other aspects of the proposals put forward, to the extent that they lie within their sphere of competence. They consider it desirable that, both as regards the strengthening of the system and for the prospective studies on the subject of the European monetary structure, the necessary work should be carried out within the competent Community institutions, in which all member countries and all the central banks concerned are represented.

5. The Governors are in agreement as regards the underlying approach to the work which is to be conducted:

- the need to consolidate the achievements of the European Monetary System in terms of internal and external stability and to build the future progress of the system on these foundations;
- the scrutiny of the ideas that could help strengthen the system and bring advances, in a balanced way, towards the objective of economic and monetary union;
- the desirability of focusing the examination on the concrete proposals that have been put forward, taking account of the basis on which they rest and of their technical aspects.

6. The Governors will take all steps to ensure that the work is brought to a successful conclusion in reasonable time, but will give themselves time for a thorough examination of these various questions."

B. Discussion by the Committee

<u>Mr. de Larosière</u> considered that, on the basis of the discussions the Alternates and the Governors had already had, the report to the Ministers could be a little more detailed. It had seemed, in fact, that in April the Governors had been agreed on two ideas. The first had been to undertake a study of the adjustments that could be made in order to strengthen the present operation of the EMS; various suggestions had been put forward in memoranda, and Mr. de Larosière recalled that he wished the question of <u>Mr. Leigh-Pemberton</u> noted that several Governors wished to stress to the Ministers that monetary policy had its limits and that overall economic policy, in particular budgetary policy, should play its role. It would be useful to be a little more explicit and, drawing on Mr. Janson's report dated 27th April 1988, underline the need:

- for progress in areas outside the competence of the central banks, such as the co-ordination of overall economic policies and action on structural obstacles to growth; and
- to avoid any changes to the EMS which would risk destabilising the economy.

If, in fact, certain countries were to yield to the temptation of pursuing a more expansionary budgetary, and even monetary, policy, without tackling structural problems, not only would they fail to achieve faster growth but they would also risk destroying the EMS and stability.

<u>Mr. de Larosière</u> said that he was broadly in agreement with what it was proposed to submit to the Ministers, in particular on what the Governors had done and intended to do, and added that he did not wish to give the impression that the concept of symmetry had the Committee's approval. However, it should be clear that in the Committee's subsequent work on the concrete proposals the question of greater symmetry in interventions would not be evaded. This question could even be mentioned in the Chairman's oral report as being an idea put forward by the Governor of the Banque de France.

<u>Mr. Pöhl</u> pointed out that he was perfectly willing to see the Governors discuss the idea of symmetry, but it should be extended to include economic performances and not limited to interventions. However, it seemed preferable to avoid using this term, since even if there was some asymmetry in economic performances the Governors should not give the impression that they recognised that there was asymmetry in intervention obligations.

The <u>Chairman</u> wound up the discussion by noting that the various comments made by the Governors were sufficient to draw up a preliminary

symmetry to be discussed in this context. The second idea had been to begin examining a much more distant question, viz. monetary integration within Europe and the institutional and practical aspects this might comprise.

It would be desirable if these two ideas were to be reflected in the oral report to the Ministers.

The <u>Chairman</u> pointed out that point 5 of the outline presented by Mr. Janson stated that the Governors were in agreement as regards the underlying approach to the work to be conducted, viz. the need to consolidate the achievements of the EMS and to build the future progress of the system on these foundations and the scrutiny of the ideas that could help bring advances, in a balanced way, towards the objective of economic and monetary union. This was certainly a framework that could be expanded upon.

<u>Mr. Janson</u> recalled that point 5 of the outline for a report also mentioned the desirability of focusing the examination on the concrete proposals that had been put forward, taking account of the basis on which they rested and of their technical aspects, which meant that the Governors were indicating their willingness to take into consideration all the memoranda that had been presented.

Mr. Pöhl recognised that it was not easy to submit a report on questions that had not yet been discussed in detail. The message to be sent to the Ministers could be grouped under three headings. Under the first reference could be made to the action the Governors had taken to implement the Basle/Nyborg agreement, for example the important steps taken to improve the co-ordination of monetary policies, including the mandate given to the Group of Experts, and also the use of the new credit facilities and the co-ordination of intervention policies. A second section would indicate the Governors' willingness to study the technical modifications to the operation of the EMS that had been suggested, in particular by the French and Italian authorities, but it would be desirable not to use the term symmetry, which was both misleading and a source of disagreement among the Governors. The various proposals could nonetheless be referred to briefly, indicating that time would be needed to examine them and thus to report to the Ministers. Finally, a third section could mention the institutional framework for the development of monetary union, but with prudence and circumspection. The political thinking in this area was not clear, and it

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would be preferable to await the European Council meeting at the end of June before deciding anything. If the Heads of State were not to take any decision in this area, it would be premature or risky to forge ahead at this stage; were they actually to agree to set up a group of experts, the latter would have to work in contact with the central banks, and the Governors would be able to keep this work under scrutiny.

<u>Mr. Ciampi</u> considered that the suggestions put forward by Mr. Janson for the outline of the report by the Chairman of the Committee reflected the state of progress of the discussions by the Alternates, which made it impossible to go much beyond a preliminary report. However, it was necessary not to let questions that fell within the competence of the central banks be taken out of their hands, and it would therefore be useful to give a rather more precise list of the topics the Governors would be examining; to this end some of the comments made, in particular by Mr. de Larosière, could serve to flesh out the proposed outline of a report. It would also be desirable, as Mr. Pöhl had pointed out, to emphasise the limits of monetary policy, which could not support the whole burden of adjustment; budgetary policy had an essential role to play, while the objective of monetary policy was above all to ensure price and exchange rate stability.

<u>Mr. Duisenberg</u> accepted that the European Council at the end of June might not take any decision on the subject of monetary integration, but it would not be desirable to take this for granted. It was important that monetary issues and the further development of the EMS should continue to be studied by the competent bodies, namely the Monetary Committee and the Committee of Governors, and the latter should make this position clear to the Ministers.

The <u>Chairman</u> pointed out that the outline of the report contained two important statements in point 4, viz. that the Governors would examine the aspects of the proposals put forward that lay within their sphere of competence and that it was desirable that the studies on the strengthening of the EMS and on the European monetary structure should be carried out within the competent Community institutions, namely the Monetary Committee and the Committee of Governors. However, as Mr. Pöhl had pointed out, if the Heads of State wished to set up a group of experts, this should not be opposed.

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oral report¹ and stressed that the Governors were agreed that none of the ideas presented in the various memoranda should be disregarded; they would all be examined in due course, and there would be an opportunity for all opinions to be voiced.

VI. Other matters falling within the competence of the Committee. Problems encountered by European banks operating in Japan.

<u>Mr. Janson</u> mentioned that the Alternates had received a request from the services of the Commission, aimed at inducing the Committee to make representations to the Bank of Japan. The object would be to persuade the latter to remove certain barriers encountered by foreign banks in Japan as regards the terms of deposit collection and the operation of the interbank market. This question had already been raised within the Monetary Committee and views had been divergent.

The Alternates were of the opinion that bilateral representations by the countries concerned would be more appropriate and effective than a joint approach by the Committee of Governors. That had been the course adopted, with some success, by a number of countries, among them the United Kingdom and the United States. Moreover, it was necessary not to underestimate the domestic political problems raised in Japan by deregulation and the relaxation of requirements.

The <u>Chairman</u> noted that the Committee shared the opinion of the Alternates that no joint representation should be made to the Japanese authorities and that it should be left to individual countries to take the initiative of bilateral representations.

1 The text forming the basis of the Chairman's report is attached as Annex 3.

The next meeting would take place in Basle at 10 a.m. on Monday, 13th June 1988, i.e. just before the BIS Annual General Meeting. The June meeting was traditionally confined to one or two items only, such as the approval of the Minutes and of the "concertation report". As in previous years, the latter report would be prepared at a meeting to be held by the "Concertation Group" at 8.30 a.m. on Monday, 13th June. The "monitoring" exercise, which had not existed in June 1987, might be carried out without a meeting of the group of experts but during Friday afternoon's telephone concertation which, for the occasion, might be protracted so as to enable Mr. Dalgaard to make a report to the Governors on the Monday. Of course, should the situation so require, the "Monitoring Group" could meet in Basle during the weekend. The same would apply to the Committee of Alternates but, as yet, there were no plans for such a meeting. Committee of Governors of the Central Banks of the Member States of the European Economic Community

10th May 1988 Confidential

BRIEF REPORT ON

DEVELOPMENTS ON THE FOREIGN EXCHANGE MARKETS OF THE COUNTRIES WHOSE CENTRAL BANKS PARTICIPATE IN THE CONCERTATION PROCEDURE

APRIL 1988

This report summarises developments on the exchange markets of the countries whose central banks participate in the concertation procedure¹ and briefly describes their interventions during April and the first few days of May 1988.

I. EXCHANGE RATE DEVELOPMENTS

The main features of the foreign exchange market during April 1988 were:

- The US dollar firmed slightly vis-à-vis most currencies.
- Stability within the EMS continued although there were minor changes of positions.
- The positive economic trend registered generally and fears of inflation caused a rise in interest rates in some countries.

The <u>US dollar</u> moved marginally higher on balance against most major currencies. Throughout the month the dollar was underpinned by rising US interest rates as well as expectations of further increases. The dollar came under a bout of selling pressure following the announcement of a slight widening of the US trade deficit in February. However, the dollar's

¹ The central banks of the EEC, Norway, Sweden, Finland, Switzerland, Austria, Japan, Canada and the United States.

decline was held in check as widespread reports of concerted intervention reinforced the sense that official co-ordination was continuing. The dollar closed the month approximately 3/4% higher against the Deutsche Mark and 1/2% higher against the yen.

The <u>EMS</u> remained stable. There were, however, some changes in the positions of the individual currencies. In particular the Italian lira and the Danish krone weakened.

The <u>Deutsche Mark</u> proved to be relatively stable. At the end of April, its export-weighted index vis-à-vis fourteen industrial countries (172.8%) was slightly below the level reached at the end of March (173.1%; 1972=100). Small exchange rate gains were shown against the Swiss franc, the Italian lira and the Danish krone, whereas losses were registered vis-à-vis the US dollar and the pound sterling.

In the election environment, the <u>French franc</u> moved within rather narrow limits. The publication of less satisfactory economic figures had no significant impact (external trade deficit of Fr.fr. 5.2 billion in February, following Fr.fr. 0.6 billion in January; price increase of 0.3% in March, following 0.2% in February).

The <u>Dutch guilder</u> showed a firm tone vis-à-vis the EMS currencies throughout the month. The Nederlandsche Bank bought a moderate amount of Deutsche Mark to smoothen this tendency.

The <u>Belgian franc</u> slightly improved its position within the EMS. No change in official interest rates took place.

The <u>Danish krone</u> weakened by 1/2% within the narrow EMS band in the middle of the month in connection with a difficult political situation which resulted in a call for a general election.

The <u>Irish pound</u> was relatively stable, remaining in the upper half of the EMS band during the month. Over the period the Central Bank of Ireland effected net purchases of foreign currency to absorb continuing net inflows and reduced the short-term facility rate by 3/4 percentage point to 8 1/2% on 11th April.

The <u>Italian lira</u> was subject to some pressure, as market participants continued to reduce short-term borrowing in foreign currencies, ahead of the French presidential elections. The Banca d'Italia intervened on several occasions in the market and accepted a slight depreciation of the lira against the Deutsche Mark, while keeping the lira/French franc rate stable. Sterling was very firm and some periods of strong overseas demand were seen. A 1/2% cut in UK base rates on 8th April (to 8%, their lowest level for ten years) tempered enthusiasm for a while, but further inflows were seen following the disappointing US trade figures for February. Although there was some precautionary profit-taking ahead of the UK trade figures for March, the pound recovered on news of the reduced deficit and sterling ended the month on a firm note. Its trade-weighted index rose by 0.4 per cent. to 78.4 (1975=100).

In the course of the month the <u>Greek drachma</u> weakened against both the US dollar and the ECU by 0.9% and 0.2% respectively. In effective terms it declined by 0.5%.

The <u>Spanish peseta</u> ended the period 0.8% higher with respect to the EMS currencies in effective nominal terms, due to continued capital inflows and in spite of some purchases of foreign currencies by the Banco de España. With respect to the US dollar, the peseta strengthened by 0.2%.

In line with the exchange rate policy defined by the authorities, the monthly depreciation of the <u>Portuguese escudo</u> in effective terms was reduced by 0.1 percentage point to 0.3%.

The <u>Swiss franc</u> weakened vis-à-vis all currencies. In relation to the US dollar the depreciation amounted to just over $1 \ 1/2\%$. Its exportweighted value dropped by 1.6\%. This trend is attributed to the domestic interest rate level which continues to be low.

The <u>Austrian schilling</u> weakened vis-à-vis the US dollar by 0.8%, the monthly spread amounting to 2%. As against the Deutsche Mark the schilling fluctuated by a mere 0.06%.

Supported by a continued currency inflow which increased during the last days of the month, the <u>Swedish krona</u> firmed against its currency index which moved from 130.75 to just above 130.00, i.e. the lower limit of the band. In order to curb the rapid credit expansion and to reduce domestic demand, the discount rate was increased from 7.5% to 8.5% as from 29th April.

The <u>Norwegian krone</u> strengthened further, appreciating by 1.6% in effective terms. Firmer oil prices and the high level of domestic interest rates continued to be the main factors. Although the interest rate differential narrowed somewhat against the basket currencies, it remained on average as high as 6 3/4% at the end of the month.

In effective terms, the <u>Finnish markka</u> strengthened slightly. Finlands Bank made some intervention purchases.

The <u>Canadian dollar</u> appreciated, improving by 0.4% against the US dollar to close at US\$ 0.8130 and improving by 0.6% on a G-10 tradeweighted basis. The strengthening was in response to Canada's continued strong economic performance, favourable terms of trade, and favourable spread between comparable US and Canadian money market rates.

The <u>Japanese yen</u> traded within a relatively narrow range against the US dollar, depreciating marginally by 0.3%. The yen's stability was brought about partly by concerted intervention by the major central banks, particularly in mid-April, and by the fact that previously expected large dollar sales by Japanese institutional investors did not materialise. Vis-à-vis the major European currencies the yen appreciated by 0.3%.

II. INTERVENTIONS

A. Interventions in US dollars

In April the central banks effected net purchases amounting to US\$ 4.6 billion compared with US\$ 2.5 billion in March. Gross purchases amounted to US\$ 5.2 billion (of which US\$ 2 billion in concerted action to support the US dollar around the middle of the month). The main buyers were the Bank of Canada and the Bank of Japan. Gross sales amounted to US\$ 0.6 billion.

B. Interventions in Community currencies and in private ECUs

Interventions in EMS currencies by Community central banks amounted to the equivalent of US\$ 2.8 billion compared with US\$ 5.3 billion in March. These interventions mostly consisted of sales of Deutsche Mark by the Banca d'Italia and, to a lesser degree, of purchases of Deutsche Mark by the Banco de España.

III. DEVELOPMENTS IN THE CURRENT MONTH, UP TO 6th MAY

The upward trend of the US dollar continued vis-à-vis all currencies except the Japanese yen. Within the EMS, there was a slightly greater variability of exchange rates. EVOLUTION DE L'ECU, DU COURS MEDIAN DES MONNAIES PARTICIPANT AU MECANISME DE CHANGE DU SME ET DES MONNAIES DES BANQUES CENTRALES DE LA CEE NE PARTICIPANT PAS A CE MECANISME, SUR LA BASE DES COURS RELEVES LE 31 DECEMBRE 1986 VIS-A-VIS DU \$EU*



* Voir page suivante.

6.5.1988



EVOLUTION DES MONNAIES DES BANQUES CENTRALES HORS CEE PARTICIPANT A LA CONCERTATION, SUR LA BASE DES COURS RELEVES LES 31 DECEMBRE 1986 VIS-A-VIS DU \$EU*

• ECU 0,93425; £ 0,6773; DR 138,7601; PTA 131,8700; ESC 146,0995; FIM 4,7925; \$Can 1,3805; FS 1,6215; Yen 159,7993; KRS 6,7750; KRN 7,3975; Sch 13,6520; cours médian des monnaies participant au SME 0,92913. Le cours médian des monnaies participant au SME représente la moyenne journalière des cours des deux monnaies à marge de fluctuation de 2,25% qui se sont éloignés le plus de leurs cours-pivots bilatéraux actuels.



MOUVEMENT A L'INTERIEUR DE LA GRILLE DE PARTIES DU SME CALÇULES SUR LA BASE DES COURS DE L'ECU DANS LES DIFFERENTES MONNAIES PARTICIPANTES

6.5.1988



EVOLUTION DE L'INDICATEUR DE DIVERGENCE*

• L'indicateur de divergence a pour but de mesurer, sur une base comparable pour toutes les monnaies participant au mécanisme de change européen, la position d'une monnaie vis-à-vis de son cours-pivot ECU. L'écart maximal de divergence est le pourcentage maximal par lequel le cours de marché de l'ECU dans chaque monnaie peut s'apprécier ou se déprécier par rapport à son cours-pivot ECU; il est exprimé par + 100, le seuil de divergence étant + 75. Les données qui ont servi de base à l'établissement de ce graphique sont les cours de l'ECU exprimés en termes de diverses monnaies, cours qui sont toutefois corrigés des effets des fluctuations de la lire italienne, de la livre sterling et de la drachme grecque audelà de la marge de 2,25% vis-à-vis des autres monnaies participant au SME.



EVOLUTION DE LA LIVRE STERLING, DE LA DRACHME, DE LA PESETA ET DE L'ESCUDO PAR PAPPORT A L'ECU SUR LA BASE DES COURS DU MARCHE RELEVES LE 31 DECEMBRE 1986*

* <u>#</u> 0,724942; DR 148,526; PTA 141,151; ESC 156,382.

6.5.1988



EVOLUTION DES MONNAIES DES BANQUES HORS CEE PARTICIPANT A LA CONCERTATION PAR RAPPORT A L'ECU SUR LA BASE DES COURS DU MARCHE RELEVES LE 31 DECEMBRE 1986*

* \$EU 1,07038; \$Can 1,47766; FS 1,73562; Yen 171,046; KRS 7,25181; KRN 7,91812; Sch 14,6128; FIM 5,12978.

6.5.1988

Committee of Governors of the Central Banks of the Member States of the European Economic Community 10th May 1988

Final version

MANDATE FOR THE GROUP OF EXPERTS CHAIRED BY M. RAYMOND

The Governors consider it desirable to improve the co-ordination of monetary policies between the member countries of the EEC, particularly in view of the full liberalisation of capital movements, and to supplement the monthly monitoring procedure. To this end the group of experts chaired by M. Raymond shall seek, in particular, in its semi-annual reports:

- to draw attention to any lack of convergence of macro-economic variables which might jeopardise external or internal monetary stability, analysing the causes and suggesting suitable corrective measures;
- 2. to evaluate, especially from the point of view of monetary policy, economic performances in the Community and to analyse their possible deficiencies with respect to the economic objectives of the Community;
- 3. to specify what contribution, within the whole range of economic policy instruments, monetary policy could make to the adjustments called for by the above-mentioned analyses;
- to examine their implications for the development of the monetary aggregates and the conditions for the financing of economies in the future;
- 5. to provide the Committee of Governors in its autumn report with the data and analytical background necessary to facilitate the discussion of prospective monetary policies with a view to developing a co-ordinated approach.

Committee of Governors of the Central Banks of the Member States of the European Economic Community

13th May 1988 (Translation)

NOTES FORMING THE BASIS FOR THE PRELIMINARY ORAL REPORT BY THE CHAIRMAN OF THE COMMITTEE TO THE INFORMAL ECOFIN COUNCIL MEETING ON 14th MAY 1988 ON THE STRENGTHENING OF MONETARY CO-OPERATION WITHIN THE EEC

1. The Governors have conducted an initial exchange of views regarding the ideas contained in the memoranda to which they have been asked to give their attention. This account of their discussions in my capacity as Chairman of the Committee is purely preliminary.

2. The questions raised relate to two sets of concerns. The first is connected with the operation of the <u>European Monetary System</u> and the ways in which it might be further modified without altering its institutional character. The second relates to the future of the <u>European monetary structure</u>, that is to say the realisation of the goal of economic and monetary union and the ways and means of making concrete progress along this path.

3. Before dealing with these two areas in turn, I should like to draw attention to a number of points to which the Governors attach great importance in connection with the two aspects I have just mentioned.

(a) Whether the focus is on the short term or the more distant future, it is important that the work, whose successful conclusion will require a general consensus, should be carried out in fora in which the <u>twelve parties involved</u>, be they governments or central banks, are represented. In the opinion of the Governors it would therefore be highly desirable that the task of examining the proposals for strengthening European monetary co-operation be entrusted to the <u>appropriate Community institutions</u>, viz. the ECOFIN Council, the Committee of Governors and the Monetary Committee.

(b) The questions raised relate, inter alia, to areas that lie within

the <u>competence of the central banks</u>. Proposals affecting the powers of the central banks and, a fortiori, the arrangements concluded between them, should as a matter of course be examined in the first instance by the Governors.

(c) The reinforcement of European monetary co-operation is a process which builds both on day-to-day practice, in the form of permanent concerted contacts between authorities and markets, and on an examination of the extent to which the existing arrangements are adequate to achieve the goals pursued, which may lead to decisions of a more systemic nature. It is important that any modifications to the existing rules, procedures and mechanisms should derive directly from the realities and needs of co-operation. They must be seen as the fruit of <u>continuous</u>, <u>coherent and balanced progress</u> based on the <u>consolidation of what has already</u> been achieved.

4. Some of the proposals put forward are expressly designed to contribute to the <u>strengthening of the European Monetary System</u>.

The strengthening of the EMS is a constant concern of the Governors which may be reflected, when necessary, in amendments to the rules and procedures in force, the most recent example being the <u>Basle/Nyborg</u> agreements, drawn up with a view to the full liberalisation of capital movements. The improvements in the facilities for financing and settling interventions resulting from these agreements have already been put into practice. For example, a sizable amount of intra-marginal interventions (ECU 3.4 billion) has already benefited from the new financing terms. The monitoring of developments in the member countries and in the capital markets has been intensified, and the close concertation between central banks, which has at times taken the concrete form of co-ordinated action in the markets, has undoubtedly contributed to the smooth functioning of the system in recent months. The Governors have, moreover, taken the steps announced in their recent report on the full liberalisation of capital movements to reinforce the process of monetary policy co-ordination among the member countries.

5. The wish has been expressed in a number of quarters that <u>various</u> <u>other modifications</u> to the operation of the European Monetary System be examined, chiefly, according to their advocates, with a view to promoting a

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better <u>balance</u> between economic performances, economic policy objectives and the constraints bearing on the different participants.

The Governors propose to examine these proposals insofar as they lie within their sphere of competence. They will seek to examine all the <u>concrete</u> proposals that have been put forward, taking account both of their underlying motivations and of their technical aspects. The proposals concerned, in particular, are those relating to the intervention mechanism, reserve asset diversification, the ECU creation mechanism, the development of the use of the official and the private ECU, the expansion of the role of the EMCF and a new credit mechanism connected with the full liberalisation of capital movements.

In this examination particular importance will be attached to the concern to consolidate the achievements of the European Monetary System in terms of <u>internal and external stability</u> and to build the future progress of the system on these foundations. In this context, it has been pointed out that focusing priorities more sharply on economic growth would carry the risk of destabilising the EMS without achieving the desired objective. Clearly, the balanced operation of the system and, a fortiori, the achievement of a higher rate of growth and the reduction of external imbalances within the Community <u>do not depend exclusively on the central banks, the mechanisms</u> <u>in place or monetary policies</u>, the limits of which must be clearly recognised. Overall economic policies, including structural policies, must play an important part in these areas.

6. As regards the <u>future of the European monetary structure</u> and the more ambitious steps it implies, the Governors have already stressed that they <u>support the objective of economic and monetary union</u> and so are willing to examine any ideas that could help to achieve this objective.

In the light of the Governors' discussions, I should like to emphasise two fundamental considerations.

Firstly, while the prospect of the full implementation of the internal market in 1992 naturally raises the question of the monetary environment in the single market, progress in European monetary integration must be <u>a balanced process</u>. Increased integration of central bank responsibilities is only conceivable if paralleled by increased integration of responsibilities for economic policy formulation and implementation and in a context of progressive convergence of economic, social and fiscal structures.

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Secondly, should there be the political will to address the whole set of issues raised in a balanced manner and <u>subsequently to take on all</u> <u>that it entails within a European framework</u>, I feel certain that the Governors will not delay in instituting a constructive examination of all the implications of the process for the exercise of their responsibilities and of the intermediate stages that will make for coherent progress towards the aimed-for objective.