

RESTRICTED

FM BONN

TO PRIORITY FCO

TELNO 613

OF 141151Z MAY 90

INFO ROUTINE ALL EC POSTS

FRAME ECONOMIC

MY TWO IPTS: AGECE: ECONOMIC AND MONETARY UNION (EMU)

SUMMARY

1. POEHL HINTS AT THE POSSIBILITY THAT EMU COULD PROCEED WITH LESS THAN TWELVE MEMBERS.

DETAIL

2. THE HIGH POINT OF THE MEETING WAS A LUNCH AT THE BUNDESBANK ATTENDED BY POEHL, WHO SPOKE IMPROMTU FOR ABOUT HALF AN HOUR ON EMU AND THEN ANSWERED QUESTIONS.

EMU

3. REFERRING TO HIS ARTICLE IN 'THE EUROPEAN' OF 11 MAY COPIES OF WHICH HE CIRCULATED, POEHL SAID THAT HE HAD BEEN WIDELY MISUNDERSTOOD. HE HAD NOT PROPOSED EMU: THAT WAS FOR THE POLITICIANS TO DO. HE HAD SIMPLY EXPLAINED HOW IT COULD BE DONE IF THE POLITICIANS DECIDED TO PROCEED. TWO OF THE THREE ELEMENTS NEEDED TO SUPPORT EMU WERE ALREADY ALMOST IN PLACE: AN INTEGRATED MARKET AND A SYSTEM FOR FIXING EXCHANGE RATES (ERM) WHICH HAD GONE A LONG WAY TOWARDS ACHIEVING FIXED PARITIES. THE THIRD ELEMENT, CO-DECISION, WAS THE POLITICAL CORE OF THE ISSUE: SHOULD THE DM BE REPLACED AS THE ANCHOR OF THE EMS BY A COMMON CURRENCY? HE UNDERSTOOD WHY THE FRENCH WANTED THIS, BUT THEY COULD ONLY HAVE IT THROUGH A EUROPEAN CENTRAL BANK (ECB) COMMITTED TO MAINTAINING PRICE STABILITY, AND THE COMMON CURRENCY COULD NOT BE THE ECU, WHICH WAS ONLY A BASKET INCLUDING SOME WEAK CURRENCIES.

4. AN ECB WOULD HAVE TO HAVE A MONOPOLY OF MONEY CREATION, WHICH MEANT THAT GOVERNMENTS WOULD HAVE TO GIVE UP SOVEREIGNTY IN THAT AREA. HE WAS STILL SCEPTICAL THAT ANY GOVERNMENT, INCLUDING FRANCE, WAS READY TO DO THIS. HE WAS NOT OPPOSED TO THE GERMAN GOVERNMENT DOING SO ON THE RIGHT CONDITIONS. HE DOUBTED WHETHER ALL TWELVE WOULD AGREE TO DO SO HOWEVER. SOME WERE INCAPABLE: OTHERS UNWILLING. THE RISK WAS THAT GOVERNMENTS WOULD AGREE INSTEAD ON A HARMFUL COMPROMISE, IE. A CENTRAL BANK WITH NO POWER AND THEREFORE

NOT ABLE TO PURSUE THE RIGHT-STRICT-POLICIES. SINCE SUCH AN OUTCOME WOULD AFFECT THE BUNDESBANK, HE WOULD RESIST THIS STRONGLY. ANOTHER POOR ALTERNATIVE, BUT ONE WHICH WAS NOT UNLIKELY, MIGHT BE AN ECB OUTSIDE THE EC TREATY WITH FEWER THAN TWELVE MEMBERS BUT WITH A STANDING INVITATION TO THE REST TO JOIN, LIKE THE ERM.

5. ASKED WHY HE THOUGHT THIS A POOR ALTERNATIVE, POEHL SAID THAT IT WOULD BRING ABOUT TWO SPEED EUROPE LEAVING SOME MEMBER STATES AFFECTED BY THE OPERATIONS OF THE MARKET OUTSIDE THE DECISION MAKING PROCESS.

6. THE SAME THEME HAD COME UP AT AN EARLIER STAGE OF THE MEETING, WHEN JELONEK (AUSWAERTIGES AMT) SAID THAT THE GERMAN GOVERNMENT WANTED TO PRESS FORWARD WITH EMU: THEY WERE NOT AIMING AT A SEPARATE TREATY OR AN INNER CAUCUS, BUT IF SOME COULD NOT PARTICIPATE FROM THE START, AN ARRANGEMENT MIGHT BE FOUND TO ENABLE THEM TO JOIN LATER. THE GERMANS WOULD PREFER EVERYONE TO JOIN, ESPECIALLY THE UK, BUT A DECISION COULD NOT BE PUT ON ICE INDEFINITELY. CROCKETT, BANK OF ENGLAND, AND EVANS, HMT, EXPLAINED THAT BRITAIN WOULD PARTICIPATE FULLY IN THE WORK OF THE IGC BUT THAT THE BRITISH GOVERNMENT DID NOT ACCEPT THE AIM OF A COMMON MONETARY POLICY NOR THE NEED FOR CENTRAL INSTITUTIONS.

ERM: BRITISH MEMBERSHIP

7. POEHL SAID HE HOPED BRITAIN WOULD JOIN THE ERM. BRITISH MEMBERSHIP WOULD GIVE THE SYSTEM MORE EQUILIBRIUM THAN WAS ACHIEVED BY FRANCO GERMAN DOMINATION. HE THOUGHT THE PRESENT STERLING/MARK EXCHANGE RATE WAS ABOUT RIGHT, BUT WE SHOULD WAIT UNTIL OUR INFLATION CAME DOWN SOMEWHAT.

COMMENT

8. IT IS A FREQUENT PLOY OF POEHL TO REPRESENT HIMSELF DISINGENUOUSLY AS THE HUMBLE TECHNICIAN WHO LEAVES POLITICAL DECISIONS TO GOVERNMENTS. FROM OUR POINT OF VIEW, THE DANGER OF HIS INSISTENCE THAT ONLY A CENTRALISED INSTITUTIONAL FRAMEWORK CAN DELIVER THE RIGHT POLICIES IS THAT, IN THE HANDS OF OTHERS, IT WILL SERVE TO FOCUS THE DEBATE ON INSTITUTIONS AT THE EXPENSE OF THE POLICY ISSUES. HE HIMSELF RECOGNISES THAT SUCH A DANGER EXISTS (PARAGRAPH 4): BUT IT IS LESS CLEAR THAT HE UNDERSTANDS THAT HIS OWN POSITION CONTRIBUTES TO IT. HE SEEMS INCREASINGLY TEMPTED TO SOLVE THE DILEMMA BY GOING FOR A SMALL MONETARY UNION INVOLVING ONLY THOSE COUNTRIES WHICH ARE LIKE MINDED ON POLICIES AND INSTITUTIONS DESPITE THE FACT THAT SUCH A UNION WOULD BE A DISTINCT SECOND BEST.