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## On the origins of the Franco-German EMU controversies

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# **NATIONAL BANK OF BELGIUM**

## **WORKING PAPERS – RESEARCH SERIES**

### **ON THE ORIGINS OF THE FRANCO-GERMAN EMU CONTROVERSIES**

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I. Maes<sup>(\*)</sup>

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## **Abstract**

EMU is, to a large extent, the result of a process of Franco-German reconciliation and understanding. However, in the postwar period, there were significant differences in ideas and economic policy-making in Germany and France. France was dominated by the "tradition républicaine", giving a central role to the state in economic life. In Germany, the federal structure of the state went together with the social market economy. In this paper an analysis is presented of these differences in thought and economic policy-making, how they evolved through time, and how they contributed to shaping the nature and form of the European Union. The focus is on the Rome Treaties, the Werner Report and the Maastricht Treaty process.

JEL codes: A11, B20, E58, F02, P16.

Keywords: EMU, economic thought, economic policy-making, France, Germany.



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## 1. INTRODUCTION

The Franco-German debates on European monetary integration are widely known as the controversy between the "monetarists" and the "economists". The "monetarists", with France as a dominant player, were in favour of plans for greater exchange rate stability and exchange rate support mechanisms. They saw a driving role for monetary integration in the process of European integration. The "economists", under the leadership of Germany, emphasised the coordination of economic policies and the convergence of economic performances, especially inflation, as a precondition for EMU. According to their view, the so-called coronation theory, monetary union could only be the last and crowning phase in the process of economic integration<sup>1</sup>.

The purpose of this paper is to investigate the underlying paradigms behind these controversies. A useful starting point is Tinbergen's view of economic integration as concerning the regulation of international relations. As such, economic integration is in essence a question of the organisation of economic policy. A crucial question is the degree of centralisation: "Which functions in international economic life should be subject to central control and which should be left to individual countries, enterprises or persons?" (Tinbergen, 1954, 98). The answer to this question depends largely on two elements: the view on the role of the state in the economy and the view on European integration. Moreover, it is important to look at, even more deeply situated, "meta-cultural" beliefs, which are related to fundamental constitutional issues as the design and functioning of the state and its legitimacy. These meta-cultural beliefs largely influence the views on economic policy and European integration.

The focus of this paper is strongly on the role of ideas in the process of European integration. This does certainly not imply that power issues were not important. On the contrary, any transfer of sovereignty has profound consequences for power relations, both between and inside countries. Crucial power issues in the Franco-German EMU debates were the German sovereignty in the field of monetary policy (and the de facto determination of the orientation of monetary policy in the EMS by the Bundesbank), and the granting of independence to the Banque de France, a profound change in French society.

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<sup>1</sup> Naturally, EMU is not an exclusive Franco-German matter. See, for instance, Maes & Quaglia, 2002, for an analysis of the Belgian and Italian approaches and contributions.



Moreover, it is important to keep in mind that the crucial proposals for European monetary integration were Franco-German political initiatives at the highest level: the Brandt-Pompidou proposal at the Hague, the European Monetary System by Giscard and Schmidt, and the Maastricht Treaty process with Kohl and Mitterrand. The technical monetary experts were rather more reserved.

The paper starts with a presentation of the main lines of thought and economic policy-making in France and Germany. Thereafter, the focus is on three important stages in the development of the European Union: the Rome Treaties, the Werner Report and the relaunching of the monetary union process in the second half of the 1980s. The paper ends with the agreement on the Maastricht Treaty<sup>2</sup>.

## **2. MAIN LINES OF THOUGHT AND ECONOMIC POLICY-MAKING IN GERMANY AND FRANCE**

In the post-war period, there were some significant differences in economic ideas among policy-makers in Germany and France. These were based on fundamental characteristics of their history and society. The analysis will focus on three levels, which are strongly interrelated: (1) meta-cultural beliefs, (2) views on economic policy-making, and (3) views on European integration<sup>3</sup>.

### ***2.1. France: the "tradition républicaine" and a centralisation of power***

France had a long tradition of a strong central state. As remarked by Rosanvallon (1992, 64), the "State" preceded the nation in France, and gave France a coherence and an identity<sup>4</sup>. An important element of the central state was the creation of a strong national elite, formed in the "Grandes Ecoles" (Ecole Polytechnique, Ecole Nationale de l'Administration, ...). The graduates of these "Grandes Ecoles" move quite easily between the public and the private sector.

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<sup>2</sup> It is not the purpose of this paper to make an assessment of the functioning and legitimacy of EMU (or the relation with political union). See Eijffinger and de Haan, 2000, Hodson and Maher, 2001, Issing, 1999, Padoa-Schioppa, 2001, Quaden, 2000, Verdun and Christiansen, 2000 and Wessels and Linsenmann, 2001. Also, this paper will not go into the issue of optimum currency area theory, see Mongelli, 2002.

<sup>3</sup> The analysis will be restricted to the main lines for views on European integration, especially the functions which should be exercised at the European level and the nature of the European institutions, supranational or intergovernmental.

<sup>4</sup> According to legal experts, the French civil law system was designed to be an instrument of power of the state. This contrasts with the Anglo-Saxon civil law system where the protection of the citizens against the government is at the core.

The Revolution of 1789 abolished the monarchy and reduced the role of religion, placing "Reason" at the center of French society. This further reinforced the role of the state in French society<sup>5</sup>. It gave birth to "la tradition républicaine", focused on the "one and indivisible" republic, a view which would permeate France. Fundamental to the republican state was the primacy attached to the sovereign nation as the source of legitimacy. The task of the state was to ensure the unity of public power in the service of the nation<sup>6</sup>.

The "tradition républicaine" stressed also the political direction of policy (Howarth, 1999). It implied the primacy of political will on the markets. Economic policy had then a strongly "voluntarist" element. The republican tradition legitimated a centralisation of power, also in the area of economic and monetary matters. So was the Banque de France considered as a part of the "circuit du Trésor", a far cry from an independent central bank<sup>7</sup>.

There was further a long tradition of state intervention in economic life in France, famous with Colbertism and the establishment of the "manufactures royales". This came to the foreground in the role of the state in industrial policy (like already in Colbertism) and the importance of planning in the postwar period.

In France "Le Plan" and the Planning Office would play a crucial role in the post-war reconstruction. Post-war planning was instaurated by an ordonnance of De Gaulle of January 1946. Jean Monnet was the first Commissioner of the Planning Office. The purpose was to mobilise resources in order to modernise France. As such, it fitted into the French centralist tradition. Moreover, the French felt that the weakness of their steel sector was an important reason for their defeat in 1940. This was a further factor in favour of a more planned modernisation of the country.

In essence, the plan was a strategy around a medium-term framework, which provided an orientation to the economic actors, reducing so uncertainty. It aimed at creating coherence, introducing "un élément souhaitable de rationalité" (Marjolin, 1963, 18), a key concept of the Republican tradition. Important was further the sectoral approach, which aimed at identifying sectors where bottlenecks would occur, which could then be eliminated. The Plan was so at the heart of the French industrial strategy. French

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<sup>5</sup> So took the state an important role in education, which in France is called "éducation nationale".

<sup>6</sup> It went together with a French emphasis on institutions, something which was very typical of Monnet's approach to European integration: "Rien n'est possible sans les hommes, rien n'est durable sans les institutions" (Monnet, 1976, 412. See also Fontaine, 1990, 19 or Duchêne, 1994, 401).

<sup>7</sup> In an article of 1992, Christian Noyer, then at the French Treasury, wrote about central bank independance as "l'exception au principe démocratique" (Noyer, 1992, 17).

programming was also "voluntarist" (Massé, 1963, 45). It aimed both at a somewhat higher expansion than would be realised by the spontaneous working of market forces, and at correcting certain imbalances of the market mechanism.

Planning was in line with the engineering tradition in economic thought in France. This tradition was especially strong among the graduates of the "Grandes Ecoles", civil servants and top managers (Schmidt, 2000, 129). Moreover, there was a relatively strong influence of Keynesian economics at the French Planning Office (Rosanvallon, 1987, 40). A special example was Robert Marjolin, the Deputy Commissioner of the Plan and one of France's first prominent Keynesians (Arena and Schmidt, 1999)<sup>8</sup>. However, the Plan had much less influence at the powerful Finance Ministry, which had a more pragmatic attitude.

It is less easy to distinguish clear tendencies or schools of thought with respect to macroeconomic and monetary policy in France during the postwar period. All the major parties pursued, during their terms in office, quite diverse economic policies. Moreover, several persons favoured different kind of policies at different moments of time.

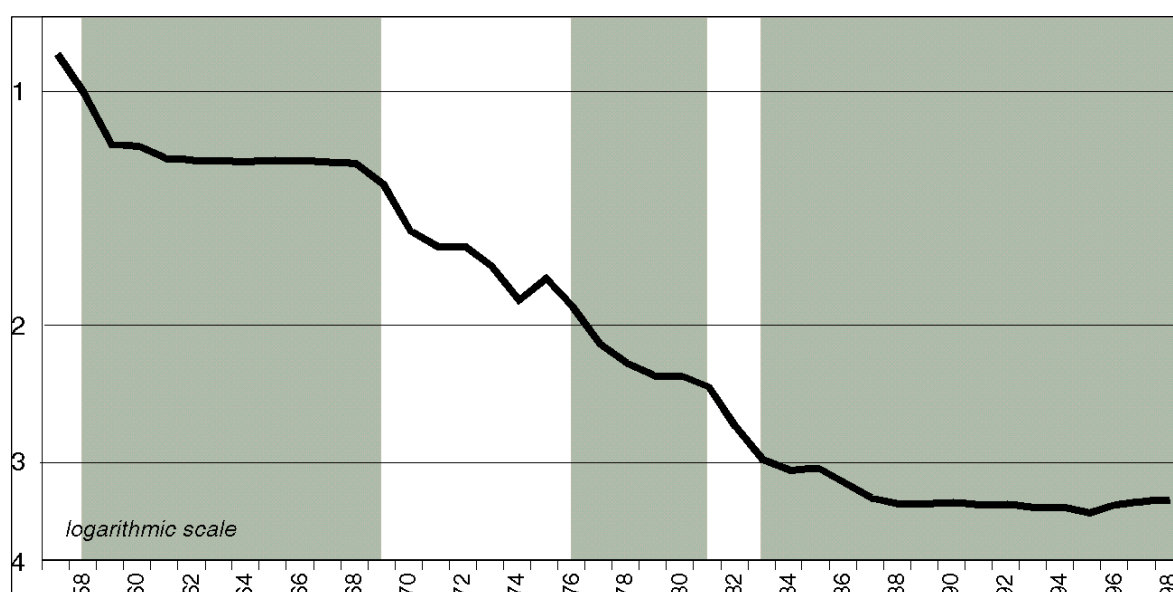
Basically, one could argue, that there was a tension between two approaches: one focusing on domestic policy priorities, especially economic growth, and taking a more relaxed view of the exchange rate, the other advocating "discipline" and in favour of a stable (or strong) French franc. The first tendency, focusing on domestic policy objectives, was more in line with the traditional French "voluntarist" approach. It drew support from different quarters, both in socialist and gaullist milieu's, as well as among employers and trade unions. The main objective of economic policy was to stimulate economic activity, even at the cost of a higher rate of inflation. Ensuing competitiveness problems were mainly tackled by devaluations of the franc. This line of thought dominated during the Pompidou presidency (1969-1974), the Chirac prime ministership (1974-1976) and the first years of the Mitterrand presidency (1981-1983). It could draw on support from more pragmatic Keynesians and left-wing economists. On the other hand there was the more "orthodox" line, emphasising discipline: a strong French franc, wage moderation and sound public finances. It could be characterised as the line "Rueff-Barre-Delors". It dominated French policy-making during the presidency of De Gaulle (1958-1969), with the Rueff-Pinay stabilisation plan, during the Barre prime ministership (1976-1981) and after Mitterrand's decision to stay in the EMS in March 1983. Traditionally, this line was more supported by liberal, free market oriented economists. This "orthodox" line was, generally,

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<sup>8</sup> In the postwar period left-wing ideas, partly Marxian inspired, were quite influential in France.

also the more pro-European line. The control of inflation in the 1960s made it possible for France to participate in the creation of the common market<sup>9</sup>. The European Monetary System was created during the Barre prime ministership. European motives were crucial for Mitterrand to stay in the EMS. Generally, the European constraint was influential in pushing through more orthodox economic policies, while a strong franc (with sound fundamentals) was important to be a strong and solid partner in the European debate<sup>10</sup>.

**Chart 1 - Exchange rate of the french franc against the german mark**



Regarding views on European integration, the republican tradition, emphasising the "one and indivisible" state, made French policy-makers generally more reluctant to transfer sovereignty to the European level. Moreover, they were in favour of an intergovernmental approach.

## **2.2. Germany: a federalist approach with a division of power<sup>11</sup>**

In Germany, Nazism and the second world war marked a fundamental break with the past. Nazism had shown the dangers of a centralisation of power. This centralisation was also evident in the economic field. National socialism had, step by step, introduced a centrally

<sup>9</sup> During the Rome Treaty negotiations, the French negotiators were very concerned about France's competitiveness and insisted on safeguard clauses. However, for de Gaulle, the European Community and the competition which it entailed, was important to push for the modernisation of France's economy.

<sup>10</sup> Naturally, during the 1960s, currency issues were mainly international monetary issues, in the framework of the Bretton-Woods system. For De Gaulle a strong French franc was very much a symbol of a strong France.

<sup>11</sup> The word "federalism" is here used in a "continental" sense (especially application of the subsidiarity principle) and not a "British" one (transferring power to Europe).

administered economy. The central bank became known as the "specialised printing office" of the government.

A crucial element of the new economic and political system in postwar Germany was "decentralisation". This was a reaction against the centralisation of national socialism. It was also the result of very strong American influences in the reconstruction of West Germany (federal State, federal central banking system, anti cartel policy, ...).

Decentralisation not only applied to the political organisation of the country, such as the federal structure of the state. It was also a basic principle of the organisation of economic policy. So was the central bank responsible for monetary policy, but not for banking supervision. The market economy itself is a decentralised structure, which goes together with Germany's federal state (Molitor, 1980, 838).

Germany's economic system in the postwar period can best be characterised as a "social market economy", a phrase coined by Alfred Müller-Armack, a professor at the University of Köln and State Secretary of Erhard at the Economics ministry. He conceived the social market economy as combining the principle of freedom in the market with that of social balance. In contrast to "laissez-faire" capitalism, the concept of the social market economy requires above all a clear legal and political regulatory framework, or "Ordnungsrahmen" (Tietmeyer, 1999, 6).

During the war, "ordo-liberal" ideas were developed by a number of economists in Germany, known as the Freiburg School<sup>12</sup>. They became very influential in the postwar period. Ludwig Erhard, the first Economics minister, and an economics professor himself, was very much influenced by them. These ordo-liberal ideas were an important source of inspiration for the economic reforms of June 1948, with which the market economy was restored.

When trying to understand the development of economic thought it is helpful to focus on important historical events. After the war, the reconstruction and recovery of the economy on the European continent was such a crucial event. However, the experiences of France and Germany were different, contributing to different economic paradigms. In France, the recovery was strongly associated with "Le Plan". In Germany, the recovery, "Das

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<sup>12</sup> For an analysis of postwar German economic thought, see Hagemann, 2000, Klump, 1997, Rieter & Schmolz, 1993, Schefold, 1998 and Watrin, 1979.

Wirtschaftswunder" (the economic miracle), was associated with the return of the free market economy.

The ordo-liberal economists emphasised that economic policy was, in essence, "Ordnungspolitik", i.e. a policy to create a sound and secure framework within which markets can operate. As such, they laid great emphasis on the interdependence between the economic order and all other forms of order (i.e. legal, social and political). The main tasks of economic policy are : (a) monetary policy: assure price stability; (b) fiscal policy: rather limited task for the government; and (c) structural policy: a more passive role, competition policy is emphasised.

In its emphasis on historical and institutional aspects of economic problems, the ordo-liberal approach drew to a significant extent on the ideas and approach of the historical school (Hutchison, 1979, 435). Moreover, prominent members of the Freiburg school (e.g. Böhm) were jurists, contributing further to the emphasis on the economic order.

The decisive social element, in the opinion of Erhard and Müller-Armack, is the freedom with which the market economy is associated (Tietmeyer, 1999, 6). Competition is herefore very important, as it limits the exercise of economic and social power. The social market economy also encompasses supplementary social provisions and safety nets, provided that they are consistent with market principles. The social market economy should then not be considered as a "third way", but is clearly a market economic system.

According to the advocates of the social market economy, a strong state is necessary, but one with limited functions. The main role of the state is to set the framework conditions, as these are decisive for the development of economic activity. The fundamental task of the state is "rule-setting": to set the rules for economic processes, monitor compliance with them, and punish infringements. The aim of these rules is to set a framework that permits the highest possible degree of freedom and ensures lasting maintenance of effective competition. Important elements are clearly defined property rights and an active competition policy<sup>13</sup>.

A constitutive element of the social market economy is monetary stability (Tietmeyer, 1999, 138). Monetary stability is important for economic reasons, as inflation damages the

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<sup>13</sup> Ordo-liberalism is then in first instance a "functionalist" approach, in which first the functions have to be defined. The elaboration of institutions should be related to the function which has to be fulfilled (von der Groeben, 1995, 270).

steering function of the price mechanism and creates uncertainty, which hurts investment. It is also important for social reasons, as inflation causes a redistribution of income, to the disadvantage of the weaker groups who cannot protect themselves. Memories of this were still vivid in Germany, with the hyperinflation of the 1920s. The task of ensuring monetary stability became the responsibility of the, independent, Bundesbank<sup>14</sup>. Moreover, this goes along with the German "federalist" tradition of preferring decentralised and compartmentalised structures (Tietmeyer, 1999, 165).

The more Keynesian tendency in Germany, with Karl Schiller as an important representative, put more emphasis on active government policies. Schiller's ideal of economic policy was to combine the market economy (the "Freiburg imperative") with active macroeconomic policies (the "Keynesian message"). This tendency was influential at the end of the 1960s and the early 1970s, when the social democrats participated in the government, with Willy Brandt as their leader and with Schiller as economics minister. This group had also links with the trade unions and favoured a dialogue ("konzertierte Aktion") between the social partners, trade unions and employers, as an element of their economic strategy.

The "decentralist", federalist German philosophy went along with a positive view towards European integration and the transfer of sovereignty to supranational European institutions. Moreover, foreign policy was dominated by the belief that European security and Franco-German reconciliation was the most vital of all interests for Germany. In line with the federalist concept of "checks and balances", German policy-makers insisted on strengthening the role of the European parliament.

### **3. THE CREATION OF THE COMMUNITIES**

#### ***3.1. The Rome Treaties***

The real start of the process of European integration can be traced back to the Schuman Declaration of May 1950, which provided the basis for the European Coal and Steel Community. The Declaration stated clearly that: "The solidarity in production will make it plain that any war between France and Germany becomes not merely unthinkable, but materially impossible ... this proposal will build the first concrete foundation of a European federation which is indispensable to the preservation of peace".

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<sup>14</sup> During the discussions on the Bundesbank law of 1957, Erhard supported the independence of the Bundesbank, while Adenauer, initially, was not so much in favour (Marsh, 1992, 167, see also Bibow, 2002 and Bundesbank, 1998).

In October 1950 a new French plan followed, the Pleven Plan, which aimed to establish a European Defence Community (Vanthoor, 1999). However, it was defeated in the French Assembly in August 1954 by a coalition of Gaullists and Communists. It showed that defence was too close to national sovereignty to be transferred to the European level. European integration could only make progress along less sensitive economic lines. New negotiations followed, initiated by the Benelux countries, leading to the Rome Treaties and the creation of the European Economic Community and the European Atomic Energy Community in January 1958.

In Germany, for Adenauer, the Chancellor, and Hallstein, his influential State Secretary for Foreign Affairs, foreign policy objectives, in casu the status of the Federal Republic in Europe, were of fundamental importance. Franco-German reconciliation was at the heart of their foreign policy (Küsters, 1998, 62). The formal recognition of the Federal Republic of Germany as a sovereign state in May 1955 marked an important step. It also increased the margin of manoeuvre for Germany. One of Germany's leading negotiators, von der Groeben, later remarked: "In the negotiations on the EEC the Federal Republic for the first time participated as a free and equal partner" (von der Groeben, 1979, 496). Erhard, the Economics Minister, was against the European common market. He feared that a European customs union would hinder a world-wide liberalisation of trade. However, Adenauer overrode his objections<sup>15</sup>.

For the German government the new European economic system to be created was of utmost importance. One of the main German aims was that the European common market would have the same economic order as the one in the Federal Republic, based on the principles of a market economy and a liberal trade policy. The Germans feared that interactions with more statist and planned systems, through the common market, could imperil the consistency of their own economic system (von der Groeben, 1979, 496).

France was living through the Fourth Republic, characterised by mostly short-lived coalition governments and political instability. A very sensitive political issue was decolonisation, with Indochina and Algeria. Also, France's economic position was vulnerable. The French government was divided on the issue of European integration. However, the prime minister, Guy Mollet, and the minister for foreign affairs, Christian Pineau, were in favour. Among French pro-European policy-makers, Monnet was very

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<sup>15</sup> Initially, Adenauer was not so much in favour of the common market as he feared it could complicate negotiations on the EDC.



influential. He lobbied for a further push towards European integration along sectoral lines, focusing on transport and energy (Monnet, 1976). However, it was clearly in France that resistance against new initiatives at European integration was the strongest. This was both for political reasons (the aversion against supranational institutions, especially, but not only, among the Gaullists) and for economic reasons (fear, both from businessmen and trade unionists, for German competition, which could endanger France's industry and the "acquis social").

During the negotiations, the French government was in first instance concerned about the Euratom Treaty<sup>16</sup>. At some point, it even considered postponing the negotiations for the common market. The French also favoured a greater role for the State in economic life. In a Memorandum the French government proposed the idea of planning on a European scale: "A policy of expansion ... implies investment which, in the basic industries, in the chemicals industry, in many of the processing industries, rests on a precise conception of the targets to be assigned to production over a period of several years. Convergence of the different national economic policies can therefore be ensured only by reconciling and harmonising national production objectives." (as quoted in Marjolin, 1986, 287).

Moreover, the French government was very concerned that France was not in a position to engage in competition on equal terms. It was therefore in favour of harmonisation of legislation which affected the competitive position, especially social legislation. The French argued further that agriculture had to be included in the common market and that France had extra costs, due to her responsibilities in her overseas territories.

Looking then at the Rome Treaties from an economic thought perspective, the European Atomic Energy Community, bears a heavier French imprint, with its sectoral approach, while the European Economic Community, with the abolition of barriers which hindered the free movement of goods, services, labour and capital in the common market and strong emphasis on competition policy, has a stronger German sounding<sup>17</sup>. The chapter on competition policy (articles 85 to 94) is very comprehensive. It covers: (1) cartels and other private arrangements, as well as the abuse of economic power; (2) distortions of competition caused by state subsidies or measures to the same effect; and (3) distortions of competition which are based on differences in the legal or administrative regulations of the various member states (like technical barriers or tax regulations). As von der Groeben

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<sup>16</sup> The negotiators for Euratom received even a higher travel allowance.

<sup>17</sup> Free movement of capital was more limited, under French pressure.

noted: "The co-ordination of individual planning decisions through the market occurs therefore in all member states within the same legally binding framework consisting of far-reaching guarantees of private property, freedom to establish a business, the determination of prices by supply and demand, freedom to exercise a profession, and free access to any market." (von der Groeben, 1979, 497). The French obtained the setting-up of the common agricultural policy and the association of the overseas territories. The social chapter was rather limited. One of the surviving elements of the French demands was the equality of pay for men and women.

The EEC Treaty was rather sketchy on macroeconomic and monetary issues. It left macroeconomic policy-making mainly at the level of the Member States. The responsibilities of the Commission were rather limited, they concerned mainly the orientation and co-ordination of the national macroeconomic policies. Also, the Treaty provided for the creation of the Monetary Committee.

### **3.2. *The organisation of the Commission of the EEC***

The first organigramme of the Commission was of a rather amazing simplicity and reflected very well the structure of the EEC Treaty. The services of the Commission were initially composed of nine directorate-generals (departments), giving a good overview of the activities of the EEC. They were: External Relations, Economic and Financial Affairs (the macroeconomic research department), Internal Market, Competition, Social Affairs, Agriculture, Transport, Overseas Countries and Territories, and Administration. There was also the powerful Secretariat (with responsibility for the co-ordination of activities and the preparation of the meetings of the Commission).

In the attribution of the responsibilities of the members of the Commission and the director-generals (the highest civil servants) one can observe the preoccupations and sensitivities of France and Germany. Louis Armand, a Frenchman, was the first president of the Commission of the EAEC. Walter Hallstein, a German, was the first president of the Commission of the EEC, while the Secretary-General, Noël, was French<sup>18</sup>.

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<sup>18</sup> Naturally, there was also an element of "chance" in these attributions. So was initially foreseen that the Belgian foreign minister P.H. Spaak, one of the driving figures behind the EEC negotiations, would become the first president of the EEC Commission.

**Table 1 - The first Commission of the European Economic Community**

Responsibility	Member of the Commission	Director-General
Presidency (Secretariat - General) Economic and Financial Affairs Competition Internal Market Agriculture Overseas Countries and Territories External Affairs Social Affairs Transport	Hallstein (D) Marjolin <sup>a</sup> (F) von der Groeben (D) Malvestiti <sup>a</sup> (I) Mansholt <sup>a</sup> (N) Lemaigen (F) Rey (B) Petrilli (I) Rasquin (L)	Noël (F) Bobba (I) Verloren van Themaat (N) Ortoli (F) Rabot (F) Allardt (D) Seeliger (D) de Muyinck (B) Renzetti (I)

<sup>a</sup> Vice - President

Sources: Commission, 1958 and Lemaigen, 1964, 65.

There was also a Franco-German balance in economic policy attributions. The French had the lead in macroeconomic policy, as Robert Marjolin became responsible for Economic and Financial Affairs. The Germans had the, for them, crucial portfolio of competition policy, with Hans von der Groeben.

The Germans further secured their presence in external relations with the director-generals for External Relations and Overseas Countries and Territories (Seeliger and Allardt). Moreover, they were pleased with Jean Rey at foreign relations. As von der Groeben (1998, 106) later remarked, "we could more readily expect him, a liberal politician, to have an appreciation of a worldwide and liberal trade policy".

Also the French obtained some key positions in for them sensitive areas. Lemaigen became the member of the Commission responsible for Overseas Countries and Territories, while Ortoli and Rabot became director-general for, respectively, Internal Market and Agriculture. The French were also quite happy with Mansholt as the member of the Commission responsible for agriculture: he had been a Dutch Minister for agriculture for many years, knew perfectly the mechanics of the farm sector and was convinced of the need for a common European agricultural policy (Marjolin, 1986, 313).

## **4. EMU APPEARS ON THE SCENE**

### **4.1. *The Hague summit and the Werner plan***

During the 1960s the common market project, with the abolition of tariffs and quota's, was realised. However, no important new attempts at European integration were undertaken, mainly due to Gaullist resistance. Changes appeared at the end of the 1960s, when the customs union was being completed and the unease with the Bretton-Woods system was growing.

French interest in European monetary integration can, in first instance, be situated in the discussions about the future of the international monetary system (de Lattre, 1999). De Gaulle had always been critical of the central position of the American dollar in the Bretton-Woods system. During the second half of the 1960s, French officials, in order to attain a more equilibrated international monetary system, developed ideas about a "European monetary identity" (Haberer, 1981). However, this concept remained rather vague. Elements were a type of exchange rate mechanism, to keep European currencies closer together, and a common position of the Community in international institutions like, the IMF<sup>19</sup>.

At the end of the 1960s, doubts about the future of the fixed exchange rate system became widespread, especially with the devaluation of the French franc in 1969 and the vulnerable position of the American dollar. The countries of the Community feared that further exchange rate instability would lead to the disintegration of the customs union and the demise of the common agricultural policy. As a response, the European Commission elaborated a Memorandum on the coordination of economic policy and the creation of a Community mechanism for monetary cooperation, also known as the "Barre Plan" (Commission of the EEC, 1969).

A further crucial factor was that new political leaders had come to power. In 1969 de Gaulle resigned and Pompidou was elected in France. He and his finance minister, Giscard d'Estaing, were more pro-European. The other major event was the formation of a new government in Germany by the Social Democrats and the Free Democrats with Willy Brandt as chancellor, a pragmatic but convinced pro-European (Wilkens, 2001). The Brandt government proposed the EMU project. Foreign policy motives were crucial.

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<sup>19</sup> This contrasted with German analyses of the Bretton-Woods system, which focused on the threat that intervention obligations posed for their domestic objective of price stability (Emminger, 1977, 53)

Germany wanted to demonstrate its European credentials, also as a way to counterbalance its new Ostpolitik (recognition of the German Democratic Republic). As with the common market project, the technical experts, were more cautious<sup>20</sup>.

At the Hague Summit of December 1969, the Heads of State and Government agreed on economic and monetary union as an objective of the European Community. A committee, chaired by the Luxembourg Prime Minister Pierre Werner, produced a report for the establishment in stages of an economic and monetary union by 1980 (Council-Commission of the European Communities, 1970, commonly known as the Werner Report)<sup>21</sup>.

The Werner Report first presented a general picture of economic and monetary union. EMU implied that "the principal decisions of economic policy will be taken at Community level and therefore that the necessary powers will be transferred from the national plane to the Community plane" (Werner Report, 26). The Report proposed that two new Community institutions should be created: a centre of decision-making for economic policy and a Community system for the central banks. These transfers of responsibility and the creation of the new Community institutions would entail the progressive development of political cooperation and it appeared that EMU would be "a leaven for the development of political union, which in the long run it will be unable to do without" (Werner Report, 26).

However, the Report did not elaborate very much on the institutional structure of EMU and did not distinguish clearly between a single currency and a system of irrevocably fixed exchange rates (Baer and Padoa-Schioppa, 1988, 54). An important reason herefore were Franco-German divergencies on the conception of economic policy and European integration (Achard, 2002)<sup>22</sup>.

The Report considered that economic and monetary union could be achieved in the next ten years, "provided the political will of the Member States to realize this objective, solemnly declared at the Conference at The Hague, is present" (Werner Report, 14). It proposed a plan to attain EMU in three stages. However, it did not lay down a precise

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<sup>20</sup> This would be a constant element in the history of European monetary integration. The different initiatives came from the heads of state (Brandt-Pompidou, Schmidt-Giscard and Kohl-Mitterrand), and "the schemes got a tough reception among the experts" (Hoffmeyer, 2000, 14).

<sup>21</sup> Belgium played an important role in this process. So went Gaston Eyskens, the Belgian prime minister to the Hague with a concrete plan for EMU. Later on, Belgium played further a pace-setting role in the EMU process, cf. Smets, Michielsen and Maes, 2002.

<sup>22</sup> So could Bernard Clappier, the French member of the Committee, not accept anything on the institutional level (Bloch-Lainé, 2002). However, in practice, he proved to be very independent-minded (Dyson and Featherstone, 1999, 107).

timetable for the different stages. Rather it wanted to maintain a measure of flexibility, while concentrating on the first phase.

It proposed that the first stage should commence on 1 January 1971 and cover a period of three years. The main elements were: (a) reinforcement of procedures for consultation and policy co-ordination; (b) further liberalisation of intra-Community capital movements and steps towards an integrated European capital market; (c) narrowing of exchange rate fluctuations between Community currencies (creation of the "snake").

In the Werner Committee, there were heated discussions about the priorities on the path to EMU. It would lead to the classic description of the debate between the "monetarists" and the "economists". The "economists", led by Germany, emphasised policy co-ordination, while the "monetarists", with France, argued for priority for the narrowing of exchange rate fluctuations (Werner, 1991). The compromise solution was that there had to be "parallel progress" in both areas<sup>23</sup>.

Immediately after its publication, the Werner Report was heavily criticised by the orthodox gaullists in France (Tsoukalis, 1977, 104). Their criticism centred on the supranational elements of the Report. It induced a change in the policy of the French government, contributing to a dilution of the proposals of the Report<sup>24</sup>. In particular, the creation of new Community institutions was dropped.

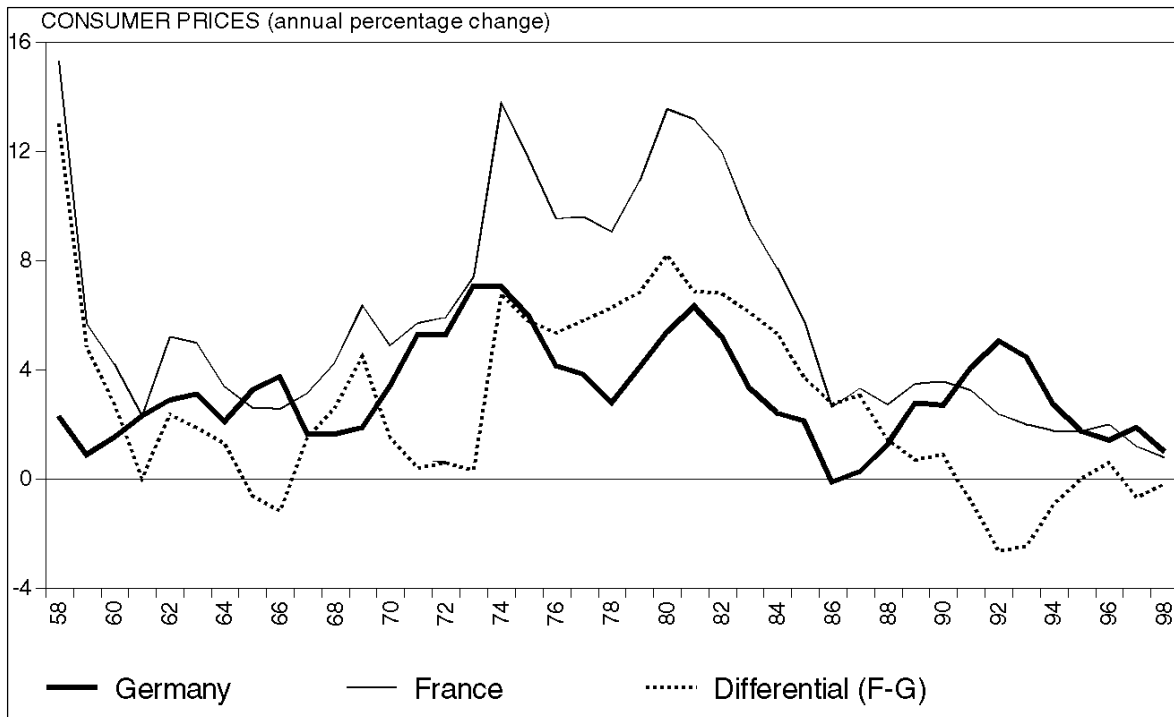
The first attempt at monetary unification was not very successful: the "snake" was quickly reduced to a German mark-zone and policy coordination remained limited. This was not only due to the unstable international environment (the collapse of the Bretton-Woods system and the oil crisis), but also because national governments were still strongly attached to their monetary sovereignty and the pursuit of national economic objectives, herein comforted by the then influential theory of the Phillips curve (Maes, 2002). In Germany, priority was given to the fight against inflation, while in France economic growth was considered a more important objective.

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<sup>23</sup> According to Tietmeyer (1971, 187), who was the German alternate, the principle of "effective parallelism" comprised at least three aspects: (1) between economic policy convergence and closer monetary ties; (2) between currency ties and the transfer of responsibility for economic policy to the Community level; and (3) between the building up of Community authority and an extension of the responsibilities of Community institutions.

<sup>24</sup> For an analysis of the attitude of Pompidou towards EMU, see Bernard, 1999.

**Chart 2 - inflation in France and Germany**



Fundamentally, this first attempt at monetary union failed because of different views in France and Germany, both on Europe, especially a French refusal to transfer sovereignty to supranational European institutions, and regarding economic policy conceptions, more stability-oriented policies in Germany and more activist economic policies in France.

#### **4.2. The European Monetary System**

In the second half of the 1970s, European leaders became increasingly worried about the stagnation of the European integration process and the ensuing risk that the achievements of the past could fall apart. Roy Jenkins, the president of the European Commission, tried to revive the monetary union project, especially in his Florence speech (Jenkins, 1977). The following year, the French president Valéry Giscard d'Estaing and the German Chancellor Helmut Schmidt played a crucial role in the relaunching of the monetary integration process with the creation of the European Monetary System (Ludlow, 1982).

The European Monetary System was launched against considerable scepticism, especially from academic economists but also from monetary experts. However, political leaders succeeded in getting it off the ground: "a victory of political intuition over expert opinion" (Mortensen, 1990, 28).

The European Monetary System was a less ambitious project than the earlier attempt at monetary union. The conclusions of the Bremen Council (July 1978) did not mention economic and monetary union but a "scheme for the creation of closer monetary co-operation leading to a zone of monetary stability in Europe". The more limited objectives of the EMS were also reflected in the legal form of the exchange rate mechanism: an agreement between the central banks of the Community.

Monetary stability, the objective of the EMS, had a double dimension: internal and external. This was a compromise and synthesis between the ideas of the "monetarists", led by France, emphasising the importance of external stability (exchange rate stability) and of the "economists", led by Germany, advocating internal stability (price stability) and the co-ordination of economic policy.

The first years of the European Monetary System were very difficult, characterised by several realignments, a lack of convergence of economic performance and a weak co-ordination of economic policy. Even the European Commission was pessimistic. It noted that the two realignments of 1982 "give serious cause for concern, since the frequency and the size of the adjustments threaten a gradual erosion of the system's credibility" (CEC, 1982, 35).

The year 1983 can be considered a turning point in the European Monetary System, especially in the relationship between the French franc and the German mark.

In May 1981 François Mitterrand became the first socialist president of the Fifth Republic in France. He started with a strong activist economic program, including an expansionary budgetary policy and nationalisations (Sachs and Wyplosz, 1986). This reinforced the divergences in policy preferences between France and Germany. The ensuing loss of competitiveness of the French economy, and capital outflows, repeatedly put strong pressure on the French franc, leading to increases in interest rates and several devaluations.

Faced with renewed heavy pressure on the French franc in March 1983, Mitterrand realised that this could not continue. He opted for staying in the EMS, mainly for European



reasons. This implied that, in order to avoid further devaluations of the French franc, he had to pursue a more orthodox economic policy, the "politique de rigueur"<sup>25</sup>.

### **4.3. A growing consensus on stability oriented policies**

The oil shock of 1973, and the ensuing stagflation, were of fundamental importance to induce changes in the conceptions of French economic policy-makers. They showed very clearly the openness of the French economy and the vulnerability to external developments (Patat, 1992, 8). The oil shock was a, more or less fatal, blow to the French planning experience. French policy-makers became more and more aware that there were limits to activist policies, and that France had to take into account the external constraint.

During the second half of the 1970s, under the prime ministership of Raymond Barre, French economic policies became more stability-oriented (Albert, 1982, 115)<sup>26</sup>. The exchange rate was a crucial element in the strategy to instill discipline on the French economy. Barre also pushed through measures to liberalise prices. This reorientation of French economic policy was an important element why German policy-makers consented to the creation of the EMS. Mitterrand's initial economic policies can then be considered as a last gasp of the traditional French interventionist policies, running against the external constraint.

These changes in economic policy conceptions were also supported by new economic theories. The "Monetarist counter-revolution" had questioned the Keynesian framework. It led to thrilling debates, initially mainly in the academic world. In a first stage, discussions centred on the determination of nominal demand, monetarists emphasising the money supply and not budgetary policy, as the main determinant of effective demand. In a second stage, the attention shifted towards the functioning of the labour market, with the monetarists attacking the Phillips curve (Friedman, 1968). With the rational expectations hypothesis, the possibilities of policy-makers to steer the economy were even more strongly questioned, as economic agents react to changes in policy (Lucas, 1976). The literature on time-inconsistency pointed further to the inflationary bias of a discretionary monetary policy (Barro and Gordon, 1983). To retain flexibility, while dealing with the inflationary bias of a discretionary policy, central bank independence quickly topped the

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<sup>25</sup> So changed the Mauroy government the wage-setting procedures, including the abolishment of automatic wage indexation.

<sup>26</sup> Raymond Barre was originally a prominent academic and scholar (including a knowledge of German ordo-liberalism, cf. Barre, 1952). As a Vice-president of the European Commission, from 1967 to 1972, he got first hand knowledge of differences in the French and German economic policy conceptions (Barre, 2000, 19).

research agenda (Fischer, 1994). Moreover, empirical studies indicated that central bank independence went together with a better economic performance (Grilli, Masciandaro and Tabellini, 1991). Central bank independence became so not only a key theme of German ordo-liberalism, but also an important element of mainstream Anglo-Saxon economics.

The expansion and the growing importance of the financial markets also reinforced the position of the central banks. This was especially so in France, where the Treasury had the final say on monetary policy. However, with the growth of the financial markets, the position of the Banque de France vis-à-vis the Treasury was strengthened, due to its technical expertise and its knowledge and experience of the markets.

Gradually then a consensus developed, moving away from active demand management policies and towards a medium-term orientation, emphasising structural, supply-side oriented policies<sup>27</sup>. A core ingredient of this new strategy was that monetary policy should be geared to price stability, and conducted by an independent central bank.

Multilateral fora, like the European Union, the OECD, the BIS, and the IMF, greatly contributed to the dissemination of these new ideas on stability oriented policies<sup>28</sup>. Senior French and German officials would meet often, not only bilaterally, but also in these international fora. This contributed to a growing consensus, also among French economic policy-makers, on "sound money" policies. An important illustration is Jacques de Larosière, the Governor of the Banque de France from 1987 to 1993, who, previously, had been Managing Director of the IMF.

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<sup>27</sup> With the Thatcher government, a new tendency to privatisation started in Europe. In France, when Mitterrand came to power, he implemented a large scale nationalisation programme. Privatisations began in France during the first "cohabitation", with Balladur as finance minister.

<sup>28</sup> For an overview of the evolution of ideas at the European Commission, see Maes, 1998.

## 5. THE MAASTRICHT TREATY PROCESS

### 5.1. *The relaunching of the monetary union project*

Meanwhile, in 1985, the process of European integration was relaunched with the internal market programme. With the Single European Act of 1987, economic and monetary union was for the first time mentioned in the Treaties.

A crucial element of the internal market programme was the liberalisation of capital movements, for which also Delors had been pushing. This was having consequences in the monetary field, as the liberalisation of capital movements was a crucial German condition for progress on monetary cooperation. Moreover, central bankers and finance ministry officials were more and more confronted with the so-called "impossible triangle", indicating that it is impossible to have free capital movement, fixed exchange rates and an autonomous monetary policy at the same time. During the 1980s and early 1990s capital mobility increased enormously. With stable exchange rates in the EMS, there was no longer much room for an autonomous monetary policy, except in the anchor country. The European Community therefore had to live with the disadvantages of monetary union, while enjoying few of its advantages.

**Table 2 - Cross-border transactions in bonds and equities<sup>1</sup>**

	1975	1980	1985	1990	1995	1998
Germany	5	7	33	57	172	334
France	-	5	21	54	187	415
Italy	1	1	4	27	253	640

Source: BIS.

<sup>1</sup> Gross purchases and sales of securities between residents and non-residents, as a percentage of GDP.

Moreover, also after the decision of March 1983 to opt for the EMS, France remained unhappy with the German dominance in the System. During Franco-German negotiations, Jacques Attali even called the German mark the "force de frappe allemande".

In early 1988, debates about Europe's monetary future accelerated. In a memorandum of January 1988, the French Finance Minister, Edouard Balladur, argued that the exchange

rate mechanism still had some important defects, notably its asymmetry<sup>29</sup>. Balladur criticized the German dominance of the system: "Il faut éviter qu'un seul pays ait, de fait, la responsabilité de fixer les objectifs de politique économique et monétaire de l'ensemble du système" (Balladur, 1988, 19).

Although, the Balladur Memorandum focused on adapting the way in which the EMS functioned, it also argued that it was necessary to reflect on further institutional steps in the monetary construction of Europe. With the liberalisation of capital movements and the internal market, an integrated economic area would be created. It concluded by raising the issue of the creation of a single currency (Balladur, 1988, 20).

Balladur's Memorandum found a perceptive ear in Germany, not at the Bundesbank or the Finance Ministry (see Stoltenberg, 1988), but at the Foreign Ministry. Several factors converged in making economic and monetary union a key theme for Genscher (Smets, Maes and Michielsen, 2000, 67): (1) it fitted in perfectly with Genscher's pro-European convictions. Genscher wanted to strengthen the process of European integration, which he considered as still fragile after the Euro-sclerosis of the first half of the 1980s. Moreover he sensed that, with Gorbachev, things were changing in the East; (2) it was a popular theme among the business community in Germany, a natural constituency of Genscher's liberal democratic party; (3) Genscher was also influenced by French complaints about the German dominance of the EMS and wanted to do something about this<sup>30</sup>. The German Presidency of the Council of Ministers, in the first half of 1988, offered just such an opportunity (Schönfelder & Thiel, 1996, 29). In February 1988, Genscher, in his personal capacity, published a Memorandum wherein he argued strongly for a European Monetary Union and a European Central Bank (Genscher, 1988).

At that time, early in 1987, Helmut Kohl was still quite open to the issue of monetary union. On the one hand, he was sensitive to the arguments of Stoltenberg that EMU was only possible if a sufficient degree of convergence was achieved (coronation theory). On the other hand, he was also sensitive to the arguments of the advocates of EMU (like Genscher), but also Mitterrand, for whom he had a high esteem and who often complained about the asymmetry of the EMS. Moreover, Kohl gradually realised that EMU was

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<sup>29</sup> Asymmetry was probably the most important theme in the Franco-German discussions about the different exchange rate regimes and proposals in the 1970s and 1980s. In essence, it revolved around the issue of which country had to make policy adjustments in order to preserve the stability of the exchange rate. This topic falls however outside the scope of this paper.

<sup>30</sup> Germany was confronted with the issue of the "political sustainability" of the EMS: could the stance of monetary policy be determined by one country, in a Community, where, in principle, decisions are taken together.

unavoidable if he wanted to realise his vision of a "United States of Europe", a recurrent theme in his speeches at that time. Of crucial importance was the Franco-German bilateral summit at Evian, early in June 1988, when Kohl and Mitterrand decided to push ahead with EMU.

Important progress was further made at the Hanover Summit in June 1988. The European Council confirmed the objective of economic and monetary union and decided to entrust to a Committee the task of studying and proposing concrete stages leading towards this union<sup>31</sup>. The Committee was chaired by Jacques Delors, who had the confidence of Kohl and Mitterrand, and, as a former finance minister, the technical expertise. The governors of the central banks - in a personal capacity - were also on the Committee. Delors wanted them to be members, both because of their expertise and because this would bind them to the monetary union project. In a first reaction, Karl-Otto Pöhl, the president of the Bundesbank, even considered refusing to serve on the Committee (Pöhl, 1996, 196). The Committee produced its report for the June 1989 meeting of the European Council (Committee for the Study of Economic and Monetary Union, 1989, hereafter referred to as the Delors Report).

## **5.2. The Delors Report**

The Delors Report would assume a crucial role as a reference and anchor point in further discussions, just as the Werner Report nearly two decades earlier. The Delors Report basically revolved around two issues: first, which economic arrangements are necessary for a monetary union to be successful? Second, which gradual path should be designed to reach economic and monetary union?

Initially, the relation between Delors and Pöhl in the Committee was rather tense. However, the crucial aim of Delors was to get a unanimous Report. So he took a low profile and focused on seeking out consensus in the Committee.

Karl-Otto Pöhl took a "fundamentalist" position and emphasised the new monetary order which had to be created: "Above all agreement must exist that stability of the value of money is the indispensable prerequisite for the achievement of other goals. Particular importance will therefore attach to the principles on which a European monetary order should be based" (Pöhl, 1988, 132). He argued for price stability as the prime objective of

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<sup>31</sup> This was a very shrewd limitation of the mandate of the Committee. It was not asked to analyse whether EMU was desirable or not, only to work out the path to reach EMU.

monetary policy, which had to be conducted by an independent central bank. Pöhl further emphasised the "indivisibility of monetary policy", that decisions should be taken either at the national level or by a common central bank.

The fundamentalist approach would be deeply influential in the Delors Report and inspire a number of principles that would figure prominently in the Maastricht Treaty (Padoa-Schioppa, 1994, 9). The Delors Committee took great care to work out first the view on the final stage of EMU, a major, and very fundamental, contrast to the Werner Committee, which was deeply divided on this issue. The Delors Report proposed, at the institutional level, the creation of an independent "European System of Central Banks", which would be responsible for the single monetary policy, with price stability as the ultimate aim. In the discussions on the independence of the central bank, one of the most delicate issues, Pöhl received valuable support from de Larosière, for whom the Delors Committee presented also an opportunity to increase the independence of the Banque de France (Dyson and Featherstone, 1999, 345)<sup>32</sup>.

The Delors Report also provided a characterisation of economic union (Delors Report, 20): (a) the single market within which persons, goods, services and capital can move freely; (b) competition policy and other measures aimed at strengthening market mechanisms; (c) common policies aimed at structural change and regional development; (d) macroeconomic policy co-ordination, including binding rules for budgetary policies.

To attain economic and monetary union the Delors Committee proposed three stages. However, the Committee underlined the indivisibility of the whole process: "the decision to enter upon the first stage should be a decision to embark on the entire process" (Delors Report, 31). The three stages were, in contrast to the emphasis on the first stage in the Werner Report, all worked out in considerable detail.

One of the most controversial issues in the Committee was the proposal of de Larosière to create a European Reserve Fund (de Larosière, 1988). The idea was that a European Reserve Fund could be a possible initial step on the path to EMU. It would function as a training ground process and as a monetary "think-tank". One of its functions could be interventions in the foreign exchange markets.

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<sup>32</sup> In order to cover himself politically, de Larosière had a meeting with Mitterrand, in which Mitterrand did not object to central bank independence.

This proposal of de Larosière was in line with the classic French ideas of strengthening support mechanisms for weak currency countries. It also reflected the French emphasis on the building of institutions. However, for de Larosière tactical elements, especially his position with regard to the French Treasury, played also a role. It was an issue on which no consensus could be reached (Delors Report, 36). According to Hoffmeyer (2000, 72), it was probably backed by a majority, but it ran counter to the German indivisibility philosophy.

The Delors Report also implied that an agenda had been set which was contrary to the view of Mrs. Thatcher. The British government responded with some rather "belated alternatives": the competing currency and the hard ecu plans (Dyson and Featherstone, 1999, 612). They were both based on a market-led approach. Both sets of proposals failed miserably. A first problem was naturally the perception that the Thatcher government wanted to obstruct the path to EMU. Also, the Delors Committee, with the powerful central bankers, had already rejected the basic principles of the British alternatives and had made a clear choice for a single currency. Moreover, the British alternatives, and the rejection of them by Germany, brought clearly to the foreground, the fundamental difference between the British and the German economic policy paradigms. It showed to French policy-makers, that, for Germany, monetary stability was a political issue of the highest level and not something to be left to the market.

However, there remained important differences between France and Germany. For Kohl, in line with Adenauer, the ultimate goal of European cooperation was political union. He accepted that EMU was a necessary element of political union and might even contribute to it, but it was not an end in itself. For Mitterrand, what mattered was that monetary policy should be a common undertaking.

### **5.3. *The Maastricht Treaty***

The period 1989-1990 was characterised by some of the most dramatic political changes in Europe since the end of the Second World War. With the fall of the Berlin Wall on November 1989, the issue of German unification came suddenly to the forefront. The German government's policy line could almost be summarised in Thomas Mann's dictum: "Wir wollen ein europäisches Deutschland und kein deutsches Europa".

In this context, the EMU process accelerated. At the Strasbourg Summit of December 1989 the date for the IGC was fixed. Furthermore, Mitterrand increasingly turned in favour of greater political integration. In April 1990 Kohl and Mitterrand formulated a common letter, suggesting a parallel IGC on political union.

Both IGC's started in Rome in December 1990. However, the IGC on political union was less well prepared. Moreover, the old German and French conceptions of European integration quickly came to the surface. Germany was in favour of a more supranational European Union, with, especially, a stronger role for the European Parliament. It was also in favour of more European cooperation in the area of foreign and security policy. France preferred an intergovernmental model, with a greater role for the Council.

The Maastricht Treaty created a so-called European Union, based on three pillars. The first pillar had at its core the old Community, but with greatly extended responsibilities, especially economic and monetary union. The second pillar was for foreign and security policy. The third one concerned co-operation on such topics as immigration, asylum and police. These last two pillars were more intergovernmental, with a limited role for the supranational European institutions, like the Commission and the European Parliament. The Treaty also strengthened the powers of the European Parliament.

Economic and monetary union had an asymmetrical structure<sup>33</sup>. Monetary policy was centralised. It was the responsibility of the European System of Central Banks, composed of the European Central Bank and the national central banks, which are all independent. The primary objective of monetary policy is price stability. This part of the Treaty went quite smoothly through the intergovernmental conference. The preparations in the Delors Committee, the Committee of Governors and the Monetary Committee certainly contributed to this<sup>34</sup>. The prominence of the German institutional model was also evident. Several factors contributed to this: the sheer size of Germany and the Deutsche mark; strong theoretical support, based on a blend of German *ordo-liberal* and mainstream Anglo-Saxon ideas; the successful history of German monetary policy; the strong bargaining position of the German authorities and the unique federal structure of the Bundesbank (Rey, 1999).

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<sup>33</sup> The old "economist" versus "monetarist" debates also resurfaced in the discussions on the criteria to be admitted to EMU, with Germany insisting on strict "convergence" criteria.

<sup>34</sup> For an analysis of the role of the Monetary Committee, see Kees, 1994.



The responsibility for other instruments of economic policy, like budgetary policy and structural policies, remained basically decentralised, with the national authorities. However, Member States have to regard their economic policies as a matter of common concern and co-ordinate them accordingly. Important elements in this co-ordination process are the Broad Economic Policy Guidelines, the multilateral surveillance process and the excessive deficit procedure. The different conceptions of monetary union and economic union reflect the limits of the willingness of the member states to give up national sovereignty (Szász, 1999, 154).

The coordination process for budgetary policy and the responsibility for exchange rate policy were the topic of some of the most tense discussions during the intergovernmental conference. The French proposed a "gouvernement économique", whereby the European Council would provide for broad orientations for economic policy, including monetary policy. This provoked a strong clash with the Germans, for whom the independence of the European Central Bank was not negotiable. However, the Germans were also convinced of the necessity of a coordination of other economic policies, especially budgetary policy, as they determine the environment in which monetary policy has to function. The agreement was only reached after intense negotiations, including secret bilateral discussions between the French and the Germans.

These discussions showed that the Franco-German controversies touched on the "meta-beliefs" concerning the organisation of economic policy: centralised or decentralised. They concerned fundamental issues of a constitutional nature and of legitimacy. For Germany, to agree on the establishment of EMU, "the independence of the European Central Bank was *a conditio sine qua non*" (Tietmeyer, 1999, 139, original italics).

## **6. CONCLUSION**

There were significant differences in ideas and economic policy-making in France and Germany in the postwar period. In Germany, the economic order was based on the concept of the social market economy, while in France the government played a greater role in economic life and pursued more activist economic policies. These differences in economic thought were to a large extent based on more fundamental underlying differences in "meta-beliefs". The "tradition républicaine" in France stressed the sovereign nation as the source of legitimacy and, consequently, the political direction of economic

policy. The postwar German federal system stressed decentralisation and a division of power.

These differences in economic ideas between France and Germany contributed to shaping the nature and form of the European Communities. The European Atomic Energy Community, advocated by Monnet, bore the signature of the sectoral approach, typical of French planning. The European Economic Community reflected to a large extent German *ordo-liberal* ideas with its emphasis on the abolition of trade barriers and a strong competition policy.

There were regular recurrences of these Franco-German debates during the last decades. In the beginning the Franco-German debates went to the core of economic policy-making. They concerned the basic mechanisms of economic coordination: planning or the market. Gradually, however, planning, fell into demise. Important factors hereby were the stagflation of the 1970s and the growing openness of the economies. Also activist Keynesian policies lost support, due to the failure of demand management policies, both at the international level, like the coordinated expansion of 1978, and at the national level, like the Mitterrand experiment in France in the early 1980s. Gradually, a consensus developed on "sound money" policies: stability oriented, medium-term, economic policies, with an emphasis on the supply side. The ensuing acceptance of price stability as the ultimate objective of monetary policy was an important factor behind the remarkable convergence of inflation in the 1980s and 1990s, an indispensable condition for the realisation of EMU.

One can discern some interesting parallels between the negotiations for the Rome Treaties and the Maastricht Treaty. The parallels were probably strongest on the German side. In both cases the main technical actor, the Economics Ministry in the 1950s and the Bundesbank in the 1980s and 1990s, was cautious about the move towards European integration. However, in both cases the Chancellor overrode the objections of the "technicians", because of foreign policy motives, whereby the desire to further the process of European integration and to strengthen the Franco-German relationship were important elements.

While the German Chancellor in both cases decided to continue with the process of European integration, he left his negotiators a large room of manoeuvre as regards the kind of European construction to be created. The Economics Ministry and the

Bundesbank were deeply concerned with the new economic order which would be created. So took Pöhl a "fundamentalist" approach in the discussions in the Delors Committee. He argued for price stability as the prime objective of monetary policy, which had to be conducted by an independent central bank. This view would permeate the Delors Report and the Maastricht Treaty, just as the creation of a competitive market permeated the Rome Treaty.

The most difficult discussions during the Maastricht Treaty negotiations concerned the French proposal for a "Gouvernement économique". This went to the core of the French and German meta-beliefs concerning the constitutional architecture of EMU, related to the division of powers between the different authorities, especially the independence of the central bank and the political direction of economic policy. Basically, the German view prevailed, as the transfer of monetary sovereignty to the European Central Bank was only acceptable for Germany if the German model was followed.

To conclude, the convergence of French and German economic policy conceptions was an indispensable condition for the realisation of EMU. However, differences still remain. France typically tends to favour a more discretionary approach, while Germany rather emphasises the importance of rules. The discussions on the creation of the Stability and Growth Pact were a typical example of this.

## **LIST OF PERSONS INTERVIEWED<sup>†</sup>**

### **France**

Pierre Achard, Member of the cabinet of R. Barre (23-01-2002)

Michel Albert\*, Commissioner General, Planning Office (9-11-2000)

Raymond Barre\*, Prime Minister (6-12-2001)

Jean-René Bernard, Advisor to G. Pompidou (2-10-2001)

Jean-Michel Bloch-Lainé, Deputy Director of the Treasury (6-12-2001)

Jacques de Larosière, Director of the Treasury, Governor of the Banque de France (3-10-2001)

André de Lattre, Advisor to Ch. de Gaulle, Deputy Governor of the Banque de France (23-1-2002)

Jacques Delors\*, Finance Minister (13-7-1999)

Hervé Hannoun, Chef de cabinet of P. Bérégovoy (9-2-2000)

Jean-Yves Haberer, Chef de cabinet of M. Debré, Director of the Treasury (3-10-2001)

François-Xavier Ortoli\*, Chef de cabinet of G. Pompidou, Finance Minister (4-12-2001)

Jean-Pierre Patat, Director-General, Research and International Relations, Banque de France (23-3-2001)

Jean-Claude Paye\*, Advisor to R. Barre (23-3-2001)

Jérôme Vignon\*, Advisor to J. Delors (8-3-2001)

### **Germany**

Leonhard Gleske\*, Member of the Board, Deutsche Bundesbank (18-12-2001)

Günter Grosche, Head of the European Currencies Division, Finance Ministry (27-7-2001)

Otmar Issing, Member of the Board, Deutsche Bundesbank (2-5-2001)

Horst Köhler, State Secretary, Finance Ministry (26-10-1999)

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<sup>†</sup> Main functions relating to the topic of the interview and date of the interview. The paper also draws on the working experience and contacts of the author at the National Bank of Belgium (since October 1983), the Commission of the EC (October 1989 - January 1991), the Deutsche Bundesbank (September - October 1993) and in the academic world.

\* Persons which had positions at both the national and European level.

Manfred Lahnstein\*, Finance Minister (13-6-2002)

Bernhard Molitor\*, Head of the Economic Policy Directorate, Economics Ministry (8-3-2001)

Karl-Otto Pöhl, State Secretary, Finance Ministry, President of the Deutsche Bundesbank (23-9-1999)

Wilhelm Schönfelder, Head of the Economics Division, Foreign Ministry (12-11-1999)

Hans Tietmeyer, State Secretary, Finance Ministry, President of the Deutsche Bundesbank (18-12-2001)

### **Luxembourg**

Pierre Werner, Prime Minister (15-5-1999)

### **European Monetary Institute**

Alexandre Lamfalussy (B), President (12-7-1999)

Jean-Jacques Rey (B), Chairman of the Monetary Policy Committee (17-6-1999, 27-2-2002)

### **Commission of the EC**

#### ***a) Members***

Raymond Barre\* (F), Vice-President, Economic and Financial Affairs (6-12-2001)

Jacques Delors\* (F), President (13-7-1999)

François-Xavier Ortoli\* (F), President (4-12-2001)

Hans von der Groeben (D), Member, Competition Policy (23-7-2001)

#### ***b) Officials***

Jean-Paul Abraham (B), Economist, European Coal and Steel Community (6-6-2000)

Michel Albert\* (F), Director DG II (9-11-2000)

Daniel Cardon (B), Chef de cabinet of A. Coppé (15-5-2001)

Roland de Kergorlay (F), Secretary of the Monetary Committee (27-11-2001)

Michael Emerson (UK), Member of the cabinet of R. Jenkins, Director DG II (16-6-1997, 21-5-1999)

Jean Flory (F), Chef de cabinet of R. Marjolin (5-12-2001)

Michele Fratianni (I), Economic Advisor DG II (18-11-1998)

Franz Froschmaier (D), Chef de cabinet of W. Haferkamp (16-7-1997)

Leonhard Gleske\* (D), Director DG II (18-12-2001)

Andreas Kees (D), Secretary of the Monetary Committee (28-11-2001)

Manfred Lahnstein\* (D), Chef de cabinet of W. Haferkamp (13-06-2002)

André Louw (B), Head of Unit DG II (22-8-1997, 24-7-2001)

Jörgen Mortensen (DK), Head of Unit DG II (23-2-1995, 15-1-1998)

Jean-Claude Morel (F), Deputy Director-General DG II, Director-General Forward Looking Studies Unit (17-8-2000, 5-11-2000)

Tommaso Padoa-Schioppa (I), Director-General DG II (18-6-1999)

Jean-Claude Paye\* (F), Chef de cabinet of R. Barre (23-3-2001)

Giovanni Ravasio (I), Director-General DG II (10-4-2002)

Ludwig Schubert (D), Advisor to A. Pfeiffer, Deputy Director-General DG II (25-8-2000, 25-4-2001)

Umberto Stefani (I), Assistant to the Director-General, DG II (31-10-2001)

Robert Toulemon (F), Chef de cabinet of R. Marjolin (23-1-2002)

Paul van den Bempt (B), Director DG II (5-6-1997)

Jérôme Vignon\* (F), Advisor to J. Delors (8-3-2001)

Manfred Wegner (D), Deputy Director-General DG II (2-9-1997)

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