The Community and the Disruption of the World Monetary System*

I

Talk of European monetary union these days involves running a serious risk of being shrugged off by the professional sceptics and so called realists who let the difficulties of the moment blind and paralyze them about the possibilities of the future. In the very short run they are right. For the last three years there has been a series of crises, disappointments and setbacks, and the oil crisis has given rise to new uncertainties, especially for England and Italy. As a result, all governments are loath to tie their hands by the clearcut and binding commitments indispensable to the pursuit of the economic, monetary and political union of the Community.

But we cannot remain indefinitely prisoners of the present. The first stages of the construction of the Community have already yielded results which even the most optimistic among us would not have dared hope for and which, indeed, have no parallel in the long history of Europe. These are:

1. Measured in dollars, intra-Community trade has increased more than tenfold, and extra-Community exports almost fivefold since 1958. If we abstract from the increase in export prices, the former has risen more than sixfold and the latter have more than tripled in fifteen years.

2. The growth of the European capital market is even more impressive. The international bonds placed on the European market have risen from about 350 million dollars in 1963 to over 5,000 million in 1973, and the Eurodollar market from a net of 9 billion dollars in 1964 to 185 billion dollars in mid-1974.

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* Inaugural lecture of the Paul-Henri Spaak Foundation, Brussels, November 5, 1974.

3. Migrations of workers between European countries have also increased several times over,[1] thereby augmenting the income of the poorest, reducing unemployment and underemployment in the countries providing the emigrant labour, and increasing production in the countries to which they have moved.

4. The Community's gross national product, at constant prices, has more than doubled in 15 years, thus making possible an unprecedented expansion in the material prosperity of its people.

5. Lastly and most important, the Community has dispelled the nightmare which had for so long weighted on my generation and those of my parents and grandparents and led to two world wars in twenty years. A war between France and Germany has become inconceivable nowadays.

These achievements should not be endangered. Both history and public opinion would brand as criminals any statesmen who proved incapable of discharging their task, however arduous it may be at the present time. *Our* task is to back them and help them to the fullest extent possible rather than to explain and excuse in advance their possible shortcomings. The economic, monetary and political union solemnly promised by three summit conferences of heads of State and Government must remain the cornerstone and inspiration of future European policy.

The problems which presently assail us, far from excusing new delays and tergiversations, make it essential, on the contrary, to move sooner and faster than previously planned. Europe, it is clear, cannot by herself solve the world problems of energy, inflation and the disruption of the international exchange markets. But her action is indispensable to reach eventual worldwide solution as well as to ward off the worst in the meantime.

I shall confine my remarks to the most anguishing monetary problems that confront us today — the world inflation and international monetary disorder — and I shall try to show how the creation of a European monetary area could both facilitate their solution and thereby be of immense assistance in the final completion of the economic, monetary and political union of Europe. In

[1] At the end of 1973, the Community countries provided work for over 6 million immigrants, of whom 1.8 millions came from member countries (875,000 Italians, 472,000 Irish, etc.) and 4.6 millions from third countries (666,000 Turks, 581,000 Jugo-Slavs, 521,000 Spaniards, 488,000 Portuguese, 456,000 Algerians, 301,000 Greeks, etc.).

my analysis, I shall concentrate on the first steps to be taken in the immediate future. Since, as the French proverb puts it, they are the hardest (« Il n'y a que les premiers pas qui coûtent »), the others will follow. There is no point in dwelling today on the final stages, for two reasons:

1. We will never take the last steps if we do not take the first, and even less if we move backward.

2. They terrify and discourage the sceptics who ought to be convinced by their very scepticism that a European monetary area is more essential than even in a world condemned, probably for a long time to come, to a régime of fluctuating exchange rates.

II

Allow me first of all to brush a broad outline of the main arguments for the rapid implementation of a European Exchange Rate Area which would in no way exclude mutually agreed exchange-rate readjustments, but would focus attention on the intra-Community rates rather than — as was the case until recently — on the dollar.

The Community has repeatedly affirmed its preference for the worldwide restoration of stable and adjustable parities. This preference is shared by most other countries — including those of the developing world — and is once again affirmed in the latest report of the Committee of Twenty (p. 12). The realization of this objective remains nevertheless still remote, for several reasons:

1. Numerous countries envisage this solution as being possible only in the long run, and certain countries — including the United States — seem inclined at the present time to favour a greater degree of flexibility in exchange rates, even as a permanent solution.

2. As long as the dollar — and especially the inconvertible dollar — continues to be used as a reserve and settlements currency, fixed rates of exchange in terms of dollars would automatically transmit to Europe and to the rest of the world any inflationary or deflationary pressures which the United States was unable to control on its own territory.

A certain flexibility — or at the very least, frequent readjustments — of the European rates for the dollar would therefore be

deemed desirable or even necessary in the foreseeable future, both by the United States and by European countries. This ought to imply a radical reorientation of the exchange-rate policies inherited from the past. These policies were anchored to the quasi-universal acceptance of the dollar as the key currency of the international monetary system, and, in consequence, to the acceptance of the dollar as the only currency in relation to which every country sought to define, stabilize, or, when necessary, adjust its own currency's rate of exchange. This policy was understandable as long as the dollar was universally convertible and the United States balance of payments relatively in equilibrium, but it became extremely dangerous in the context of an inconvertible dollar and of violent disequilibria in the United States balance of payments, for it then led in fact to different national reactions to these disequilibria and excessive fluctuations between the currencies of the Community itself. Last July, for example, the Mark had gone up by 15 per cent over the florin, 19 per cent over the Belgo-Luxembourg franc, 25 per cent over the Danish crown, 51 per cent over the French franc, 58 per cent over the pound and 62 per cent over the Italian lira.

Fluctuations on this amplitude between the currencies of the Community may prove necessary in exceptional circumstances such as those which have characterized this period, but it is hard to believe that the customs union could survive for long if each of its members were free to devalue its currency unilaterally, for such a decision is equivalent in practice to the unilateral institution of customs duties on imports and of export subsidies, not to mention its effects on financial contracts.

It would admittedly be premature to demand of the Community countries an irrevocable stability in their intra-Community rates of exchange until considerable progress has been made in harmonizing their internal policies — both fiscal and monetary — and institutionalized by sufficient transfers of jurisdiction from national to Community bodies. An interim but urgently necessary solution would be the creation of a European Exchange Area, focussing the definition and readjustment of the rates of exchange of each country upon the currencies of the Community itself rather than upon the dollar.

In fact, the dollar is far from being the "centre of gravity" of the Community countries' foreign trade. On the average, the

United States absorb only a small (7.5 per cent in 1973) and declining fraction (it was 10 per cent in 1958) of the Community countries' exports, whereas the Community itself absorbs a proportion almost seven times as great (52 per cent in 1973) and growing (it was 35 per cent in 1958) of member countries' exports.

It is extremely probable, moreover, that a large number of other countries would have the same reasons for stabilizing — or adjusting — their exchange rates in relation to a Community area rather than to the dollar. This is particularly evident in the case of the other Western European countries and of Africa and the Middle East. These three regions export from 27 to 58 per cent of their global trade to the Community and only from 4 to 9 per cent to the United States. A monetary area grouping Western Europe, Africa and the Middle East would absorb on the average 75 per cent of member countries' exports, that is, nearly ten times more than their exports to the United States (8 per cent) and almost six times more than their exports to the whole Western hemisphere (13 per cent).

Other countries would tend to gravitate in the same direction, either for economic or for financial and political reasons, especially the Eastern European countries, South Africa, New Zealand and Australia. To avoid cramming you with figures, I would refer you for further details to Table II in Annex. To come back to the Community of Nine, over 83 per cent of its exports in 1972 (and 85 per cent in 1973) went to the countries listed above, and less than 17 per cent (15 per cent in 1973) to the rest of the world, including about 8 per cent to the United States.

The formation of a European monetary area would thus create a framework and a centre of gravity which would be particularly appropriate to these countries' foreign exchange policies. It would facilitate the maintenance of at least a presumptive stability in the foreign exchange rates of certain countries in relation to each other — as is already the case for the members of the Community "snake" — and also the decisions to be taken and negotiated with the United States as regards their dollar rates.

III

I hope that I have convinced you that the creation of a European foreign exchange area is just as essential in order to cope with the immediate problems facing us now as it is a precondition

for further progress towards the economic and monetary union promised by the Summit Conferences. This aim ought, it seems to me, to elicit unanimous agreement if adequate answers can be found to the problems which it raises. I shall therefore devote the rest of this paper to an examination of the five basic questions to which we must find an answer:

1. To avoid as far as possible exchange-rate fluctuations triggered by temporary and reversible disequilibria, and risking unnecessarily to create undesirable and indeed unacceptable disturbances in basic competitive conditions governing trade between participating countries, and to invite reprisals which might lead to the collapse of the common market.

2. To ensure, on the other hand, the readjustments of exchange-rates which are essential if major and persistent disequilibria between national policies are to be corrected.

3. To coordinate foreign exchange interventions in third currencies — that is, essentially in dollars — to the extent necessary to secure the effective maintenance of the intra-Community rates agreed between participating countries.

4. To define a European unit of exchange — and not just a unit of account — accessible to the private sector, capable of being dealt in on the market on the same basis as the dollar, the Euro-dollar and other Euro-currencies, and of being used for interventions by central banks as well as for the repayment of multiple credit operations, both official and private.

5. At some later date — but let us hope, fairly soon — to simplify and facilitate immensely the practical application of these measures by the gradual transformation of the mini-*European Fund for Monetary Co-operation* into a body whose task would be to ensure, not the merging, but the joint management, of the Community countries' national monetary reserves.

Let us now take up, one by one, each of these five problems in order to try and find a concrete solution for them, sufficiently logical and convincing to be negotiable in the present difficult context.

1. *To Avoid Reversible and Disequilibrating Fluctuations*

The solution of the first problem is to be sought above all in the adaptation, expansion and improvement of the agreements at present in force regarding the functioning of the Community "snake" and mutual monetary support arrangements. Countries in deficit should be guaranteed, in case of need, the co-operation indispensable to avoid a devaluation or a depreciation of their currency deemed undesirable — or even unacceptable — by their partners. *Vice versa,* surplus countries should have the right to prefer — even as a lesser evil — the temporary accumulation of reserves or credits on their partners to a revaluation or appreciation of their currency which was also deemed undesirable or unacceptable by them and their partners.

The present short-term monetary support agreements have set up, to that end, a series of credits and so called "rallonges" totalling 4,225 million units of account (about $5 billion) for borrowers and 6,950 million units of account (about $8.3 billion) for lenders.[2] These credit ceilings are clearly insufficient in the present context. It is paradoxical that the countries of the Community grant each other, in support of such ambitious and binding commitments as those of the Treaty of Rome, only a fraction of the credits granted by them to the United States who are not bound by such commitments and with which their trade is only about a seventh ($15.8 million in 1973) of their trade among themselves ($111.2). Leaving aside, in the present climate of mistrust, the most logical and even the most indispensable long-term solution (see point 5 below), the minimum mutual monetary support commitments politically and financially acceptable at present should be at least equal to the bilateral so-called "swap" commitments of the Community countries

[2] The difference between these two totals aims at avoiding the possible exhaustion of lending commitments before borrowing rights are exhausted, should the use of such rights be concentrated on one or two strong surplus countries. Germany's overall lending commitment, for example, totals 2,700 million units of account (a quota of 1,200 million plus a "rallonge" of 1,500 million), whereas the others' borrowing rights amount to 3,625 million (quotas of 2,125 million plus "rallonges" of 1,500 million). The inadequacy of the lending commitments would be greater still if borrowings were concentrated on a country whose lending quota was less than Germany's.

to the United States, i.e., $11.8 billion, or 10 billion units of account.

Subject to later adjustments, these ten billion units could be distributed in accordance with the proportions at present in force, i.e., about 2.2 billion each for Germany, England and France, 1.5 billion for Italy, 750 million for Belgium and Holland, 300 million for Denmark and 100 million for Ireland. The actual or foreseeable exhaustion of a credit or debit quota would automatically lead to consultations between member countries regarding the political choice to be made between the various courses conceivable in that case — increases of the credit ceilings, control of capital movements, adjustments of parities or allowing the rates of exchange to float. I will revert under (2) below to the modalities of consultation likely to render as palatable as possible for all countries concerned the choice, *which will in any case be unavoidable,* between these solutions, all of them unpleasant.

A drastic reform of present repayment provisions is just as important as the raising of existing credit ceilings. It is, to say the least, paradoxical that a substantial part if not the whole of these reimbursements can now be effected in inconvertible dollars, i.e., in fact by a simple substitution of a claim on the United States for a claim on a member country. The creditor countries themselves would have every interest in preferring to such a reimbursement the transfer of bonds, either medium- or long-term, expressed in terms of the Community unit of account — conferring on them an appropriate exchange guarantee — and negotiable on the market, to mop up, if need be, liquidities deemed excessive or inflationary. The adoption of a system on these lines would in addition pave the way for "open market" operations which are indispensable for the future management of the monetary union of the Community. As to the real final reimbursement of the intra-Community credits or bonds, this ought to be effected solely either in the currency of the creditor country, or in truly international assets — i.e., in Special Drawing Rights or other similar reserve assets on the International Monetary Fund — or in gold at a (fluctuating) price to be agreed between debtors and creditors, but doubtless close to the current prices on the free gold market.

2. *To Ensure Indispensable Readjustments*

It would, however, be unrealistic to expect that the measures just suggested will succeed in avoiding all needs for exchange readjustments in the foreseeable future. Different rhythms of inflation — or deflation — between Community countries will continue to make such adjustments imperative if they are not corrected in time.

Of course prevention is better than cure, and our rulers ought to be convinced that it will be infinitely more unpleasant, difficult and dangerous for them to end inflation tomorrow than to avoid it today. Nonetheless, we must be prepared for setbacks, and these, until economic and monetary union is completed, will still involve excessive balance-of-payments disequilibria between the countries of the Community.

The persistence of such disequilibria will inevitably raise serious problems both for surplus and for deficit countries, no matter how they are financed (by loans or settlements). They may impose on the surplus countries an excessive expansion of their monetary issues, and, in consequence, lead to inflationary rises in prices and wages; they may subject the deficit countries to deflationary pressures, and, in addition, to losses of net reserves which cannot conceivably be borne indefinitely.

In these circumstances, it will be impossible for the countries of the Community to avoid the choice between four alternative policies or a combination of these policies:

a) an anti-inflationary or anti-deflationary adjustment of internal policies will, obviously, be most appropriate:

i) for a deficit country whose external deficits coincide with internal rises in prices and wages, since both phenomena reflect the inflationary financing of levels of consumption and investment exceeding the country's productive capacity and its ability to raise loans under acceptable economic and political conditions;

ii) for a surplus country whose external surpluses coincide with internal deflationary pressures, since these two phenomena reflect demand levels insufficient to absorb the country's productive capacity.

b) But internal readjustments will be just as inappropriate and

unacceptable when the surpluses or deficits in the balance of payments are due:

i) to over- or under-competitive levels of prices and costs whose international correction would impose, on the deficit country, prolonged policies of deflation and unemployment, and, on the surplus country, an excessive rise in its prices and wages; an adjustment of the rates of exchange, restoring competitive levels of prices and costs, is distinctly preferable in these cases for all the countries concerned;

ii) to excessive movements of capital which cannot be attributed to overvalued or undervalued exchange rates and for which the most acceptable correction in the countries in question would consist in a concerted adaptation of interest rates or in temporary and jointly applied restrictions on the inflows or outflows of capital which they deem least desirable.

c) Lastly it is still possible that the disadvantages inherent in each of the three policies envisaged above are such that it would seem preferable to seek to avoid, attenuate or spread them over a longer period of time, even at the cost of further financing of the balance-of-payments disequilibria.

In any case, the effectiveness or likelihood of success of the policies adopted would be considerably diminished if they were adopted unilaterally — thereby incurring the risk of provoking protective measures or reprisals on the part of the partner countries — and would on the contrary be powerfully reinforced by the concerted adoption of complementary measures by the debtor and creditor countries.

A procedure ensuring mutual and rapid consultations should therefore be rapidly brought into play in the case of persistent disequilibria. The initiative for such consultations should *normally* come from the country ready to take itself the measures necessary for the elimination or reduction of its surpluses or deficits. An excessive rate (x per cent per month) of increase or decrease in a country's net reserves beyond or below an agreed "fork" around "normal" or "desirable" reserve levels should give that country:

a) the benefit of the doubt regarding the most appropriate measures which it is itself disposed to take in order to deal with the situation;

b) the unconditional right to cease or limit its exchange interventions on the market, thus allowing its currency to fluctuate upwards or downwards, without however accentuating these fluctuations by its own interventions in the market; but solely

c) to the extent that the other alternative measures discussed above were unable to rally the agreement of the partner countries or proved incapable of resolving the problem.

In the case (which, it is to be hoped, would be exceptional) in which a country with an excessive surplus or deficit was too slow in setting in motion the necessary consultations, the other countries should have the right to initiate consultations — which should be as secret as humanly possible — aiming at a readjustment, by the country in question, of its internal policies, its exchange rates and/or its rates of interest and controls of capital movements. Such an initiative would obviously be very delicate and ought not to be invoked except in extreme cases. It might be confined, for example, to a *group* of countries whose *overall* reserve losses or gains exceeded the limits mentioned above and whose *combined* quotas for mutual monetary support exceeded 50 per cent of the total.[3]

The three rules mentioned above regarding the benefit of the doubt and the right to suspend or limit interventions in the exchange market in case of disagreement would be applicable jointly to the countries taking the initiative in calling such consultations.

In either case — but especially in the former case — it would obviously be extremely desirable to apply Articles 148 and 149 of the Treaty of Rome as regards voting rules rather than to require unanimity for the adoption of any agreement deliberated by the Council.

If it still seems utopian at this stage to impose on a country an adjustment of its exchange rates which appears indispensable to the others, the latter ought at least to be released from their obligation to intervene themselves in the exchange market in order to maintain the stability of a currency which is deemed clearly overvalued or undervalued by a qualified majority of the Council.

[3] This would in fact mean that such an initiative could only be taken by at least:
a) the three countries whose quota exceeds 22 per cent of the total (Germany, England and France);
b) or by two of these countries, *plus* Italy *or* Belgium, *or* Holland;
c) or by one of these countries, *plus* Italy, Belgium *and* Holland.

3. *Extra-Community Rates of Exchange*

The application of the rules suggested under (2) above regarding the intra-Community rates of exchange obviously implies a concerted policy by the participating countries in their foreign exchange interventions in currencies other than those of the Community, i.e., practically, in the dollar market.

The simplest and most rational solution would be to declare to the International Monetary Fund the parities at which the countries of the Community pledge themselves to buy or sell their currency to the IMF and to foreign monetary authorities *against Special Drawing Rights or other reserve accounts on the Fund,* but not in dollars as long as the dollar remains inconvertible. They would in the same way abstain from selling or buying on the market any inconvertible currency, including the dollar. This was in fact the policy followed until 1971 by the United States in application of Article IV, Section 4 (b) of the Statutes of the IMF. They were defending the declared parity of the dollar by purchases or sales of *gold* to *foreign monetary authorities,* but abstained from all purchases or sales of *national currencies,* both in the market and from or to the monetary authorities.

This solution, however, cannot be applied completely in the present circumstances, for the following reasons.

The first is that the countries of the Community are legally bound by their "swap" agreements to lend, temporarily, their currency to the United States against dollars for amounts negotiated bilaterally but totalling at present $11.8 billion.

The second reason is that this solution would indefinitely block any use of the dollars and Euro-dollars which now constitute almost the whole of the exchange reserves (over $41 billion last August) accumulated by the countries of the Community under the now defunct régime of the dollar standard, and which they might need tomorrow in order to settle their oil and other deficits. The most logical solution of this problem would obviously be a world agreement on the conversion of these surplus dollars into Special Drawing Rights, as envisaged by the Committee of Twenty in its proposal for a "substitution account". But such an agreement has still to be negotiated.

The third reason is that no country can afford to remain indifferent to the rate of exchange of a currency as important as the dollar and to leave to the United States the power to decide alone and unilaterally on the rate of the other currencies — and in any case of theirs — in relation to the dollar.

For these three reasons, purchases or sales of dollars by the countries of the Community will continue to be indispensable in the future as they have been in the past. The overall limits of these sales and purchases ought however to be subject to concerted decisions, in as close consultation as possible with the United States and the IMF. Failing which, they might be subject to contradictory decisions, or provoke — by way of arbitrage — upward or downward pressures deemed unacceptable by certain other countries of the Community.

These decisions, concerted and revised periodically, might fix the maximum amounts of the interventions deemed necessary in order to moderate excessive fluctuations in exchange rates, or, on the contrary, to promote the exchange-rate readjustments which would appear desirable.

They ought obviously to be taken in the light of the overall balance of payments of the member countries with the rest of the world, and particularly with the United States. The divergences of opinion between member countries regarding the concerted rate of the dollar ought not, however, to make agreement impossible, for two reasons:

a) the fact that the dollar rate affects only a small fraction of their exports to the European area and is therefore of secondary importance compared to their rates vis-à-vis the other currencies of this area;

b) the possibility for any minority country of subordinating its agreement to the revision of its intra-Community rate of exchange, following the procedures suggested under (c) above.

4. *A European Unit of Exchange*

The present functioning of the "snake" is based on the acceptance, at least tacitly, of a Community unit of account. The intervention rates for purchases and sales between any two currencies of the "snake" correspond to the agreed margins of fluctuations

around the "central rates" notified to the IMF in relation to the Special Drawing Rights unit (and no longer to gold or the dollar).

These central rates should be explicitly redefined in terms of a *Europa* unit of account, for three reasons:

a) Because the Special Drawing Rights unit of account is now subject to two different interpretations:

i) a legal definition in gold, incorporated in the Statutes of the Fund, but which has become completely academic;

ii) an "interim" definition in a "basket of currencies" which came into force last July.

b) Because a definition in terms of the *Europa* would express more precisely the reality of a policy which permits a distinct evolution:

i) in any readjustments of a Community currency in terms of the other Community currencies;

ii) in any readjustments (parallel readjustments, however) of the currencies of the Community as a whole in relation to Special Drawing Rights.

c) Because it is urgent to be able to transform the Community *unit of account* into a *unit of exchange,* accessible to the private sector and capable of being dealt in on the market in the same way as the dollar, the Euro-dollar and the other Euro-currencies. Special Drawing Rights seem still to be nowhere near being in a position to play this role.

There remains the question of the most acceptable definition of this *Europa* unit. Three suggestions, at the very least, deserve consideration:

a) The first would be to dodge the question. The exchange value of the *Europa* would simply be defined by its interconvertibility into Community currencies at the exchange parities notified by each country to the Community, and capable — for a time at least — of being readjusted in case of need.

This might provide the simplest and most rational solution, but it will doubtless prove acceptable to public opinion only when it has become sufficiently familiar with a *Europa* which has already acquired an established position in the market. It should be noted that the dollar enjoys widespread acceptance, both abroad and in the United States, although it is no longer defined in terms of anything else, except by freely fluctuating market rates.

b) The second solution would be to retain — but explicitly define — the system at present in force for the "snake" currencies, i.e., to define the *Europa* in terms of the Special Drawing Rights, subject obviously to readjustments of that parity if need be, just as all currencies are liable to do so in accordance — or alas all too often in contradiction — with the Statutes of the IMF.

c) The third solution would be to choose one of the European units of account already used by the market for the issue of international bonds. I would eliminate at once, in this connection, the ECU definition, which is equivalent to a currency option by the creditor, as too risky and unfair to the borrowers; and I shall confine my comments to the European Unit of Account, to the EURCO, and to a possible combination of these two formulae in a new one.

The *European Unit of Account* (UC) has the enormous advantage of already being widely accepted by the market. The bonds subscribed by the public total an amount equivalent to over a billion dollars, and their reimbursement value has obviously increased considerably in relation to dollar bonds, and substantially in relation to the EURCO because of the predominance of devaluations over revaluations. The definition of the UC, initially modelled on that of the *European Payments Union* unit of account, is also very close to that of the agricultural unit of account of the Community. Its basic aim is to preserve the equivalence of the UC with the currencies of reference which prove the most stable in fact (i.e., which revalue or devalue least).

A double difficulty has arisen in this connection:

a) This stability was originally measured, like the parities declared to the IMF, in relation to a certain weight of fine gold (0.88867088 grams). These parities having become academic, it will be measured in the future by reference to any standard (for example, Special Drawing Rights) in which the parities are expressed. This new definition, however, could itself become unacceptable if all the currencies of reference — or even only the most important of them — were one day to cease to maintain such a parity.

b) The parities declared to the Monetary Fund have become completely academic, since an increasing number of currencies — including all the currencies of reference — now fluctuate on the market at rates unconnected with the parities or "central rates" (in Special Drawing Rights or in dollars) notified to the IMF.

The formula of the EURCO is not subject to this double difficulty since it is defined by a weighted basket of participating currencies at their market value. But it raises two objections:

a) the EURCO changes its value every time the exchange value of any currency of reference appreciates or depreciates.

b) In order to make it acceptable to the market, the present formula gives an abnormally high weighting to the currencies which the market thinks are likely to appreciate and an abnormally low weighting to those thought likely to depreciate. This makes the formula difficult to accept politically by the official authorities of those countries whose currency is regarded as weak, and would entail repeated changes of weighting, which would be upsetting for the market, every time speculators change their views regarding the strength or weakness of the currencies of reference.

I shall therefore hazard a new definition of the *Europa* combining the advantages of the UC and the EURCO and avoiding their disadvantages:

a) The reference base in relation to which the future stability of the participating currencies would be measured could be that of the EURCO basket, but with a permanent weighting, based for example on the agreed quotas of participation of the different countries in the mutual monetary support.

b) The *Europa* would not, however, vary every time a single currency appreciated or depreciated. Its current reimbursement value would remain equivalent to that of the currency or currencies whose market value remains stable or shows the least variation in relation to the EURCO package defined under (a).

A *Europa* calculated in this way in mid-1969 — before the great upheavals of recent years — would, if my calculations are correct, have had, on 30 September 1974, a reimbursement value calculated on the Danish crown and reflecting a depreciation of

about 19 per cent in terms of the Mark, 15 per cent toward the Swiss franc, 11 per cent toward the schilling, 9 per cent toward the guilder, 6 per cent toward the Norwegian crown and 4 per cent toward the Belgo-Luxembourg franc, but an appreciation of 1 per cent over the yen, 5 over the Swedish crown, 12 over the Canadian dollar, 17 over the French franc, 23 over the dollar, 26 over the pound sterling, and 29 over the lira.

In the last three months of this period, the *Europa* would have remained relatively stable in relation to almost all the other main currencies, with its value practically unchanged in relation to the guilder and the Swedish and Norwegian crowns, and with a maximum rise of 3 per cent over the yen and a maximum fall of 3 per cent below the French franc. From the end of August to the end of September, it would have remained practically stable in relation to most of the main world currencies including *all* the Community currencies, except for the French franc, whose value in terms of the *Europa* would have appreciated by slightly over 1 per cent.

A *Europa* calculated in this way would, by definition, maintain the maximum stability vis-à-vis the Community currencies as a whole, i.e. the most important currencies by far in the foreign trade and financial relations of the participating countries. It would have the same advantage, as I have just stressed, for the other countries of Europe, Africa and the Middle East.

Do not, however, ask me to conclude this debate at this point, for none of these formulae is exempt from risks, drawbacks and ambiguities.[4] I would far prefer first of all to clarify my own thoughts by begging you for your own opinion and especially those among you whom their experience of the market puts in a far better position than me to express a clear preference for one or the other of these formulae. My main concern is to accelerate such a debate and the conclusion of an agreement between the Community authorities and the private market on the most rapid possible adoption of a Community unit of exchange. The best is the enemy

[4] The last one which I have just examined, for example, ought no doubt to be slightly amended in order to avoid a violent switch from the least depreciated to the least appreciated currency, or *viceversa*, because of a slight fluctuation in relative percentages of depreciation and appreciation which are very close to each other. This could be done by excluding any currency that has depreciated in terms of the average.

of the good, as the French proverb puts it, and even an interim definition — like that of the Special Drawing Rights — would be preferable to prolonged debates on an « ideal » and « definitive » definition, which in any event will remain elusive in the absence of a worldwide agreement on the restoration of an international monetary order.

The adoption of a Community unit of exchange would be particularly opportune at a time when the Community envisages the need to issue, in the coming months or even years, a number of international loans. The possibility of denominating certain of these loans in such a unit would without any doubt facilitate their placement with some, at least, of the subscribers.

This does not, however, in any way mean that a monopoly must be granted to the *Europa* in this respect. The first issue envisaged at this moment is that of dollar bonds, but no formula should be *a priori* ruled out. It is even possible, for example, that issues of bonds indexed to the cost of living or to a « basket » of those raw materials and/or manufactured products which are the most important in international trade, would be so attractive to certain subscribers that they could, in the present circumstances, be placed at nil or quasi-nil interest rates, thus making them attractive to the borrowers also.

A range of borrowing formulae, which is desirable and indeed inevitable in present circumstances, could in fact help to throw light on the final choice of the Community as to the most appropriate definition for settlements between the monetary authorities of the Community and their interventions on the market.

5. *Joint Management of National Monetary Reserves*

I shall abstain from repeating here the arguments, which I have developed *ad nauseam* in numerous publications,[5] for a *joint* management of the *national* monetary reserves of the countries of the Community. This joint management is in any event indispensable to the completion of the economic and monetary union, and would, contrary to a widespread opinion, in no way imply the transfer of national monetary reserves to a Common Fund on

[5] Especially in various reports to Jean Monnet's *Action Committee for the United States of Europe.*

which each country would be free to overdraw. It would simply mean that the countries of the Community would place their reserves with an institution managed jointly by them, thereby reinforcing their negotiating power, instead of placing them directly in Treasury bonds or deposits in foreign banks over whose management they have not the slightest control.

The *European Fund of Monetary Co-operation* constitutes a first step — desperately modest and inadequate, alas — in this direction. Let us hope that the sombre climate which at present paralyzes the chances of success of an ambitious negotiation will be sufficiently dispelled in the coming months to convince the Council to take a stand on the extremely constructive proposals which have already been twice submitted to them by the Commission of the Communities.

Conclusions

To sum up, it appears to me that the urgent adoption of a few agreements — modest, but crucial and perhaps germinal — ought to rally the unanimous support of the sceptics as well as of the enthusiasts, given the worldwide and European crisis with which we are now faced. These agreements would constitute, for the latter an essential step in the direction of economic and monetary union, which has been repeatedly promised by the Summit Conferences. They ought to be, *for all*, a means of influencing and accelerating the negotiation of the world monetary reforms which are indispensable in the long run. In the meantime, they would help to limit and palliate, as far as this is possible, the inevitable repercussions of worldwide inflation and of fluctuating rates of exchange on the economies and on the commercial and financial relations of the countries of the Community, the associated countries and many others whose foreign trade is predominantly with Europe.

1. A revision of the mutual monetary support agreements and of the rules governing the functioning of the Community's « mini-snake » ought to make the latter more attractive and acceptable to all:

a) by facilitating the rapid adoption and the success of the concerted readjustments of exchange rates and other instruments

of internal and external policy that remain in certain cases unavoidable;

b) by permitting countries in difficulty to avoid the adoption and contagion of exchange-rate fluctuations and other measures that might cause unhealthy and unnecessary disturbances in competitive conditions between member countries and reprisals jeopardizing the very survival of the Community.

2. The rapid adoption of a Community *unit of exchange* — and not only of a "unit of account" ought to:

a) greatly facilitate Community loans and borrowings, both external and internal, particularly urgent in the present circumstances;

b) help to broaden, orient and strengthen the Euro-bond and Euro-currency markets;

c) make it possible to replace, at least partially, a dollar which has become inconvertible and fluctuating by a more appropriate unit in a number of official and private contracts, in the interventions of central banks on the exchange market and the repayment of mutual support and other credits between Community countries.

3. This new unit of exchange must obviously be integrated in a world system — and not only a European one — of exchange rates, settlements and reserve management. Its rapid adoption would be particularly useful for preserving a minimum of order, stability and cohesion in the present régime of floating rates. The revision of the interim arrangements — which are alone conceivable at the present time — will no doubt become imperative when, at some distant date, worldwide arrangements are at last negotiated and put into application.

Inaction is doubtless the easiest (but also the most loathsome, not to say criminal) response to the uncertainties which at the present time paralyze Community negotiations.

Is it vain to hope that our Heads of Government will try to prove, at their Summit Conference, that "impossible" is not European any more than it is French?

New Haven

ROBERT TRIFFIN

STATISTICAL APPENDIX

I

TABLE I A

SOURCES AND USES OF INTERNATIONAL RESERVE CREATION: 1950-1973
(in billions of U. S. dollars)

	World	United States	Other Countries		
			Total	Devel.	LDC's
I. *Reserve Assets*	*138.2*	*— 11.6*	*149.8*	*113.8*	*36.0*
II. *Reserve Liabilities*	*123.1*	*89.9*	*33.2*	*29.6*	*3.7*
1. Foreign Exchange	111.9	87.3	24.6	24.6	—
2. SDR Allocations	11.2	2.8	8.5	5.6	2.8
3. IMF Credits	0.1	— 0.2	0.3	—0.5	0.8
4. BIS Credits	—0.2	—	—0.2	—0.2	—
III. *Surpluses or Deficits* (—) (I-II). Total = *World Monetary Gold* [1]	*15.0*	*— 101.5*	*116.4*	*84.3*	*32.3*
1. At $35 an ounce	6.5				
2. Revaluation to $42.22 an ounce	8.5				

Notes:

1. All these estimates are derived from IMF publications and exclude the communist countries, for which reliable estimates are not available.

2. The huge reserve increases of this period — from $46 billion in 1949 to $184 billion in 1973 — can be seen to have resulted overwhelmingly — and indeed exclusively in the last decade, except for SDR allocations — from the accumulation of foreign exchange (primarily dollars) and the revaluation of gold.

3. The net reserve increases of the rest of the world have in effect financed about $90 billion (88 per cent) of the more than $100 billion cumulative deficits of the United States.

TABLE I B

SOURCES, DISTRIBUTION AND USES OF INTERNATIONAL MONETARY RESERVES: 1937-1973
(in millions of current U. S. dollars)

End of Year	World	U. S.	Other Countries		
			Total	Developed	LDC's
1937					
A. *Reserve Assets*	27,655	12,790	14,865	12,568	2,297
B. *Reserve Liabilities*	2,365	430	1,935	1,935	—
1. Foreign Exchange	2,370	430	1,940	1,940	—
2. BIS Credits	— 5	—	— 5	— 5	—
C. *Net Reserves* (A-B)	25,290	12,360	12,930	10,633	2,297
1949					
A. *Reserve Assets*	46,116	26,024	20,092	11,329	8,763
B. *Reserve Liabilities*	11,312	3,361	7,951	7,877	74
1. Foreign Exchange	11,158	3,360	7,798	7,798	—
2. IMF Credits	208	1	207	133	74
3. BIS Credits	— 54	—	— 54	— 54	—
C. *Net Reserves*	34,804	22,663	12,141	3,452	8,689
1959					
A. *Reserve Assets*	57,599	21,505	36,094	26,485	9,609
B. *Reserve Liabilities*	17,382	10,605	6,777	6,453	324
1. Foreign Exchange	16,444	10,120	6,324	6,324	—
2. IMF Credits	844	485	359	35	324
3. BIS & EF Credits	94	—	94	94	—
C. *Net Reserves*	40,217	10,900	29,317	20,032	9,285
1969					
A. *Reserve Assets*	78,265	16,964	61,301	45,676	15,625
B. *Reserve Liabilities*	37,258	21,567	15,691	14,707	984
1. Foreign Exchange	32,415	20,698	11,717	11,717	—
2. IMF Credits	4,415	869	3,546	2,562	984
3. BIS & EF Credits	428	—	428	428	—
C. *Net Reserves*	41,007	— 4,603	45,610	30,969	14,641
1972					
A. *Reserve Assets*	158,720	13,150	145,570	113,435	32,135
B. *Reserve Liabilities*	113,814	79,673	34,141	30,738	3,403
1. Foreign Exchange	103,610	77,371	26,239	26,239	—
2. SDR Allocations	10,113	2,491	7,622	5,073	2,549
3. IMF Credits	354	— 189	543	— 311	854
4. BIS & EF Credits	— 263	—	— 263	— 263	—
C. *Net Reserves*	44,906	— 66,523	111,429	82,697	28,732
1973					
A. *Reserve Assets*	184,275	14,378	169,897	125,177	44,720
B. *Reserve Liabilities*	134,427	93,248	41,179	37,438	3,741
1. Foreign Exchange	123,075	90,685	32,390	32,390	—
2. SDR Allocations	11,237	2,767	8,470	5,635	2,835
3. IMF Credits	350	— 204	554	— 352	906
4. BIS Credits	— 235	—	— 235	— 235	—
C. *Net Reserves*	49,848	— 78,870	128,718	87,739	40,979

EXPLANATION

I. *Purpose*

The purpose of this Table is to recast the "International Reserves" Tables of *International Financial Statistics* in a more integrated (1) and meaningful fashion, highlighting the relationships between the sources, distribution and uses of reserve creation since 1937 and their relationship to the financing of balances of payments.

Sources of Reserve Creation. The "World" column shows gross reserve assets (line A) as the sum of various liabilities used as reserves (foreign exchange, SDR allocations, IMF, BIS, and EF credits, shown on lines B, 1-5) and of world monetary gold stocks (line C).

Distribution and Uses of Reserves. The other four columns distribute between the United States and other major areas (developed and less developed):

a) gross reserve assets (line A);

b) reserve liabilities (line B); and

c) net reserves (line C = A-B), reflecting the cumulative balance-of-payments surplus, or deficit, of each country or area on official settlements.

Further breakdowns by individual countries and years would thus integrate reserves creation and uses with the financing of balance-of-payments surpluses and deficits.

II. *Sources and Technical Notes*

1. All of the estimates used in this Table — with the exception noted under (2) immediately below — are derived from the "International Reserve Tables" of *International Financial Statistics* (August 1974 for the 1969 and 1973 estimates, 1972 Supplement for 1949 and 1959 estimates, and 1963-64 Supplement for 1937 estimates).

2. One of the bottom lines of the *IFS* Table on "Foreign Exchange" records the "*difference*" between reported direct reserve holdings of foreign exchange by national monetary authorities and the reported U. S. and U. K. liabilities to reserve holders. The 1973 *Annual Report* of the IMF, however, identifies (p. 39) a substantial portion of this "difference"

(1) An incidental by-product of such integration is to help spot errors and discrepancies in the *IFS* Tables. For example, the "Foreign Exchange" total for 1972 appears as $103,610 million on p. 23, but as $103,555 million on p. 19, of the August 1974 issue of *IFS*. Using the first of these two contradictory estimates raises "Total Reserves", on p. 19, from $158,665 million to $158,720 million.

as official holdings of Euro-dollars. This identified portion is here included among other U. S. liabilities (on line B, 1) and provisionally estimated at roughly half of the reported " difference " for the year 1973, pending publication of the 1974 IMF *Annual Report.* The remainder, together with sterling holdings, is allotted entirely to other developed countries.

3. IMF credits (lines B, 2) are the difference between " Gold Deposits and Investments " and " Use of Fund Credit " on the one hand and, on the other, the undistributed profits of the IMF (" Surplus " on bottom line of " Source " of " Reserve Positions in the Fund "). For simplicity's sake — to avoid an " unallocated " line — these undistributed profits are attributed here *pro rata* of Fund quotas, *i.e.* 23 per cent to the United States, 49 per cent to other developed countries (of which 9.6 per cent to the United Kingdom) and 28 per cent to the LDC's.

4. All of these estimates are in current dollars. Those for 1972 and 1973 should be divided by 1.0857 and 1.20635 respectively — *i.e.* the ratios of the new official U.S. dollar gold parities ($38.00 and $42.22 per ounce) to its previous parity ($35.00 per ounce) — in order to obtain estimates in " constant " (?) dollars or SDR's officially valued throughout at $35.00 per ounce.

5. World monetary gold stocks (= world net reserves on line C) are calculated at the official gold price for each year. Their physical increase since 1969 is insignificant (about $300 million), most of the apparent increase being due to the officially registered increase in the gold price from $35 to $38 an ounce in 1972 and $42.22 in 1973.

At current market prices (about $150 an ounce) world monetary gold stocks would be valued at about $177,000 million.

6. Note finally that all of these estimates exclude the monetary reserves of the communist countries, for which reliable estimates are unavailable.

II

Table II A

THE IMPACT OF INTERNATIONAL RESERVE ACCUMULATION ON MONETARY EXPANSION AND PRICE AND WAGE INCREASES IN INDUSTRIAL COUNTRIES OTHER THAN THE UNITED STATES: 1970-1973

	In billions of U. S. dollars			Increase in % of 1969			
	1970-73 Increases of			Reserve money		Money	Av. of Consumer Prices & Wages
	Int'l Rsves	Reserve Money	Money	Int'l Rsves	Reserve Money	Money	
I. *European Community* . .	*43.99*	*44.17*	*101.69*	*69*	*69*	*70*	
A. *Founding Members* .	*38.83*	*36.81*	*88.59*	*74*	*71*	*74*	
Germany	26.02	12.50	9.83	187	90	42	43
France	4.70	10.60	24 39	28	63	57	57
Italy	1.39	11.45	47.35	9	76	121	69
Netherlands . . .	4.02	0.73	3.27	146	27	51	54
Belgium-Lxbg . .	2.71	1.53	3.75	74	41	49	52
B. *New Members* . . .	*5.16*	*7.36*	*13.11*	*43*	*62*	*51*	
United Kingdom .	3.95	6.97	10.78	39	69	51	56
Ireland	0.33	0.40	0.44	53	63	47	72
Denmark	0.88	— 0.01	1.89	78	—1	50	54
II. *Other Industrial Europe* .	*7.69*	*4.38*	*7.93*	*77*	*44*	*46*	
Norway	0.86	0.32	1.47	77	28	69	48
Sweden	1.83	0.91	1.30	78	39	41	45
Switzerland . . .	3.65	2.40	3.57	78	51	37	37
Austria	1.34	0.75	1.59	72	40	63	50
III. *Other Industrial Countries*	*11.25*	*22.31*	*55.69*	*58*	*115*	*89*	
Japan	8.59	19.39	45.12	58	131	89	71
Canada	2.66	2.92	10.56	57	63	91	35
IV. *Total*	*62.94*	*70.86*	*165.30*	*67*	*76*	*73*	
A. Foreign Exchange	51.55(=82% of total)						
B. Reserve Positions in IMF	1.61						
C. Special Drawing Rights	5.85						
D. Gold, at official $ price	3.96						

TABLE II B

COMPARATIVE STATISTICS OF GROSS INTERNATIONAL RESERVES RESERVE MONEY AND MONEY IN INDUSTRIAL COUNTRIES OTHER THAN THE UNITED STATES: END OF 1969 AND 1973

	1969 Dollar Rate	End of year, in billions of U.S. dollars					
		Int'l Reserves		Reserve Money		Money	
		1969	1973	1969	1973	1969	1973
I. *European Community*		*24.59*	*68.58*	*64.16*	*108.33*	*145.43*	*247.12*
A. *Founding Members*		*20.92*	*59.76*	*52.28*	*89.09*	*119.59*	*208.18*
Germany . . .	4.00	7.13	33.15	13.95	26.45	23.40	33.23
France	4.93706	3.83	8.53	16.75	27.35	42.90	67.29
Italy	625.00	5.05	6.34	15.14	26.59	39.16	86.51
Netherlands . .	3.62	2.53	6.55	2.75	3.48	6.41	9.68
Belgium-Lxbg .	50.00	2.39	5.10	3.69	5.22	7.73	11.47
B. *New Members* . .		*3.66*	*8.83*	*11.88*	*19.24*	*25.84*	*38.95*
United Kingdom	0.41667	2.53	6.48	10.13	17.10	21.15	31.93
Ireland	(0.41667)	0.69	1.03	0.63	1.03	0.93	1.37
Denmark . . .	7.50	0.45	1.32	1.12	1.11	3.76	5.65
II. *Other Industrial Europe*		*7.36*	*15.05*	*10.00*	*14.38*	*17.36*	*25.29*
Norway	7.14286	0.71	1.58	1.12	1.43	2.14	3.61
Sweden	5.17321	0.70	2.53	2.35	3.26	3.15	4.44
Switzerland . .	4.318	4.43	8.08	4.67	7.08	9.54	13.11
Austria	26.00	1.53	2.87	1.86	2.61	2.54	4.13
III. *Other Industrial Countries*		*6.76*	*18.01*	*19.39*	*41.69*	*62.37*	*118.06*
Japan	360.00	3.65	12.25	14.76	34.14	50.78	95.91
Canada	1.08108	3.11	5.77	4.63	7.55	11.59	22.15
IV. *Total*		*38.71*	*101.65*	*93.55*	*164.40*	*225.17*	*390.47*
A. Foreign Exchange .		15.12	66.67				
B. Reserve Positions in IMF		3.28	4.89				
C. Special Drawing Rights		—	5.85				
D. Gold, at official $ price		20.32	24.27				

(The rate 0.41667 is bracketed for both United Kingdom and Ireland.)

Table IIA: Footnotes, Sources and Brief Comments

Footnotes and Sources:

1. More decimals than shown in columns 1-3 were used in the per cent calculations of columns 4-6.

2. The percentages in columns 5-6 were calculated directly from the *IFS* national currency estimates rather than from the $ estimates in columns 2-3. The latter are based *throughout* on the *1969* dollar conversion rates in order to:

a) be consistent with the per cent calculations in columns 5-6;

b) to permit comparison between the *potential* impact of reserve accumulation (columns 1 and 4) in the absence of exchange-rate readjustments and other actions and its *actual* impact (columns 2-3 and 5-6) after such readjustments and other actions;

c) to avoid complex calculations requiring ideally the use of non-readily available data, such as actual — and changing — conversion rates, revaluation profits and losses, etc.

3. See also following Table and footnotes.

Brief Comments:

1. Reserves Accumulation (82 per cent of which from foreign exchange — primarily dollars — accumulation) accounts for most of the enormous increases in reserve money (76 per cent) and money (73 per cent) over this short space of four years.

2. Eight central banks offset through domestic credit contraction and other actions a substantial portion of the *potential* impact of reserve accumulation (column 4) upon the *actual* expansion of their reserve-money liabilities (column 5). Domestic credit expansion increased further the expansion of reserve money in six countries, particularly Italy, France and Japan.

3. The average of consumer prices and wages increases (last column) shows a surprisingly close correlation with overall money increases (column 6), but with a lesser dispersion reflecting probably the influence of direct price competition between countries.

Table IIB: Footnotes and Source

Footnotes:

1. Conversions from national currencies into dollars (in columns 4-7) are carried at the rates shown in column 1, *i.e.* the official parities (or exchange rate in the case of Switzerland) in 1969 (*before* the August and October readjustments of the French and German parities). They show the number of national currency units per U. S. dollar.

2. Note that the 1969 rates are used also in the 1973 columns, for the reasons given in footnote 2 of the preceding Table.

Source: International Financial Statistics, August 1974: 1. for International Reserves: line 1 of country Tables; 2. for Reserve Money: line 14 of country Tables; 3. for Money: line 34 of country Tables; 4. for Consumer Prices and Wages: lines 64 and 65 of country Tables.

III

A European Monetary Area in World Trade

I *The Need for Policy Coordination*

Article 104 of the Rome Treaty defines as follows the broad objectives of member countries' economic policy: "Each member country practices the economic policy necessary in order to ensure the equilibrium of its global balance of payments and to maintain confidence in its currency, while aiming to ensure a high degree of employment and the stability of the price level." And Article 105 continues: "In order to facilitate the realization of the objectives enounced in Article 104, the member States coordinate their economic policies. They institute to this effect a collaboration between the competent services of their administrations and between their central banks."

All countries would probably agree with the objectives defined in Article 104, but the degree of dependence of each country's GNP on its foreign trade inevitably entails:

1. A significant difference of emphasis on the order of priorities to be assigned to these objectives. Countries with a low ratio of foreign trade to GNP would understandably put their primary emphasis on high employment and price stability rather than on balance-of-payments equilibrium, especially if the international monetary system facilitates — as it traditionally did for reserve-currency countries like the United States — the financing of their deficits.

2. A lesser need, and therefore willingness, to coordinate their economic policies with those of other States, as accepted by the countries of the Community in Article 105.

Table I illustrates this asymmetry: Foreign exports sustain only 4 per cent of total GNP for the United States, but 13 per cent to 43 per cent for the countries of the Community, taken separately (column 1). The *Economic and Monetary Union* of the Community would reduce these percentages significantly, to levels ranging from about 6 per cent to 12 per cent (column 3). The emergence of a *European Monetary Area* (see below) would reduce them further to about 3 per cent to 6 per cent (column 5), averaging for the Community as a whole 4.4 per cent, *i.e.* just about the same ratio as for the United States.

The coordination of economic and monetary policies is thus indispensable to the Community countries to give their national policies a degree of effectiveness comparable to that enjoyed by the United States.

It may also entail, quite rationally, a different attitude toward the degree of exchange-rate flexibility or stability that would best serve their

interests in a reformed international monetary system, as well as in the years which are still all too likely to elapse until agreement is reached on the reforms under discussion for more than a decade already.

II *A European Monetary Area*

It is widely recognized that the national currency area of each of the countries of the Community is far short of the "optimum currency area" necessary to the effectiveness of national policies. Tables II and III are designed to determine the likely scope of an optimum and feasible currency area for the countries of the Community.

The first column of Table III shows that exports to the Community countries account for more than 50 per cent — and up to 77 per cent — of the foreign trade of each Community country, except the United Kingdom (30 per cent), Denmark (42 per cent), and Germany (47 per cent). It also shows that the Community absorbs, on the average, 47 per cent of the exports of the other countries of Western Europe, with only two countries (Iceland and Yugoslavia) with ratios below 43 per cent. There is little doubt that all — or nearly all — of these countries would in fact gravitate toward a European Monetary Area if the countries of the Community succeed in implementing the economic and monetary union to which they have repeatedly committed themselves.

Such a monetary area would encompass more than two thirds of most European countries' exports, and less than half of them (49.4 per cent) for only one country, Yugoslavia (see column 2 of Table III).

Some other countries and areas, moreover, would also be drawn into the same orbit. The African countries — other than South Africa — export two thirds of their total exports toward Western Europe, the countries of the Middle East 57 per cent, the Soviet Area 64 per cent and South Africa 51 per cent (column 2 of Table II). A conservative estimate of a *de facto* European Monetary Area would include in it — because of traditional political as well as economic links — the countries of Africa and the Middle East, and encompass (see column 3 of Table III) about three fourths of the exports of each area, except the Middle East (63 per cent).

I have placed into a separate group (line II of Table II) other areas whose attraction toward Western Europe is more questionable, although still strong either for trade reasons (the Soviet Area and South Africa) or because of their financial and political links (South Africa, New Zealand, Australia, and a motley of small "other countries", including dependent territories, such as Gibraltar and other predominantly British, French and Australian territories, for which the *Direction of Trade* statistics are too incomplete for separate listing). Column 4 of Table II includes them in the group of countries primarily oriented toward Western Europe. Comparison with column 6 shows that such a group would absorb as a minimum from 2½ (Australia) to 6 (Western Europe) and even 8 (Middle East) and 13 (Soviet Area) times more of their exports

than the Western Hemisphere as a whole, and 3 (Australia) to 10 (Western Europe), 15 (Middle East) and 26 (Soviet Area) times more than the United States.

III *Other Regional Groups*

Other regional groups are more difficult to define.

The most obvious of them would be a Western Hemisphere group accounting for 50 per cent, on the average, of its members' foreign trade, but as much as 70 per cent for Canada (column 6 of Table II). Such a group would obviously center primarily on the United States which accounts alone for nearly 67 per cent of Canada's trade (see line IV, column 7). This very fact would elicit, however, some political resistance on the part of Canada.

The worldwide interests of the United States are reflected in the fact that its trade with Europe-oriented areas and with Asia (42 per cent and 19 per cent, respectively, or 60 per cent in all) exceeds its regional trade with the Western Hemisphere (40 per cent) (see line IV, 1 of Table II).

Intra-Asia trade centers mostly on Japan and averages 28 per cent for the area as a whole. In this case also the worldwide interests of Japan are evidenced by the fact that its exports to Europe-oriented areas and to the Western Hemisphere (36 per cent and 42 per cent respectively, or 78 per cent in all, of which 31 per cent with the United States alone) far exceed its trade with Asia (22 per cent). (See line III, 1 of Table II).

A Western Hemisphere and an Asian group would economically tend to be pulled together, and encompass about twice as much of their members' trade as their trade with the Europe-oriented areas.

Political — rather than economic — considerations are the main explanation of the emergence of a Soviet group, a Latin American group, of the Central American and Andean sub-groups, and of other sub-continental groupings in Asia and Africa. It might be noted, however, that the existing trade patterns of many of these less developed countries are not exclusively the reflection of Adam Smith's "invisible hand". They are very much influenced by a technical and financial infrastructure imported from the major capital markets of Europe and the United States and aiming at developing a few raw materials and agricultural products for export to them, rather than at developing local manufactures and intra-regional trade. The adoption of uniform protectionist policies toward the rest of the world further reinforced the trade links with the developed countries and weakened those with other less developed countries, by erecting the *same* barriers against the "infant industries" of neighboring countries as against the "adult industries" of Europe and the U.S.

Regional economic plans may be justified, even on purely economic grounds, as an effort to correct the distortions inherited from this history and to help diversify the LDCs' pattern of trade and production. The bulk of their exports — whether it be oil, coffee, meat, grains, etc. — will continue to flow outward, but regional preferences could be justified — on the "infant industry" argument — as the only way to develop sufficient markets for their non-staple manufactures.

In the monetary and financial fields, regional development banks, and payments unions — such as already created or discussed in Latin America and ECAFE (United Nations Economic Commission for Asia and the Far East) — may be necessary to support regional trade liberalization commitments, just as the European Payments Union contributed powerfully to European trade liberalization in the early postwar years.

IV *Concluding Remarks*

The development of a Community Economic and Monetary Union and of a European Monetary Area would help preserve among their member countries the maximum degree of economic and monetary stability achievable under current conditions. It should minimize the recourse to beggar-my-neighbor trade and exchange-rate policies.

While irrevocable exchange-rate stability could be achieved only on the final stage of the ambitious program for the economic and monetary union of the Community, unnecessary and damaging exchange-rate fluctuations within the Community could be avoided by the accelerated development of the *Fund for European Monetary Cooperation.* This would be sufficient to protect 3/4 to 4/5, or more, of their foreign trade. It

TABLE 1

1972 EXPORTS IN PER CENT OF GNP

Exports to → from ↓	World	European Community	Rest of World	European Monetary Area	Rest of World
European Community	18.7	9.7	9.0	14.3	4.4
France	13.4	7.5	5.9	10.9	2.6
Germany	18.1	8.5	9.6	13.5	4.6
Italy	15.6	7.9	7.8	11.8	3.8
Netherlands	36.3	26.7	9.6	31.5	4.8
Belgium	43.2	32.0	11.1	37.3	5.8
United Kingdom	16.9	5.0	11.8	10.0	6.8
Ireland	30.8	23.1	7.7	25.0	5.8
Denmark	20.8	8.5	12.3	16.5	4.2
United States	4.3				

Source: Calculated from export estimates of *Direction of Trade, Annual 1968-72* and GNP and exchange-rates estimates of *International Financial Statistics.*

TABLE II

REGIONAL DISTRIBUTION OF EXPORT MARKETS, 1972
(in % of total exports)

Exports to → from ↓	Eur. Comm.	West. Eur.	Eur. Mon. Area	Total I + II	Total III + IV	Western Hemisphere			Asia
						Total	U.S.	Other	
I. *European Monetary Area:*	*51.4*	*67.5*	*74.6*	*81.8*	*18.2*	*13.0*	*8.0*	*4.9*	*5.2*
A. *Western Europe* .	*51.1*	*68.5*	*75.7*	*83.3*	*16.7*	*13.3*	*8.2*	*5.1*	*3.4*
1. Eur. Comm..	52.0	68.7	76.2	83.2	16.8	13.3	8.2	5.1	3.5
2. Other . . .	47.1	67.6	73.5	83.5	16.5	13.4	8.4	5.0	3.1
B. *Africa & Middle East*	*52.8*	*63.4*	*67.8*	*73.1*	*26.9*	*10.8*	*6.7*	*4.2*	*16.1*
1. Africa . . .	57.9	66.6	73.3	80.0	20.0	14.0	9.4	4.6	6.0
2. Middle East .	48.7	57.1	63.3	67.4	32.6	8.2	4.5	3.7	24.3
II. *Other Europe-oriented Areas*	*34.0*	*44.8*	*53.2*	*60.9*	*39.1*	*13.6*	*6.0*	*7.6*	*25.5*
A. *Soviet Area* . . .	*41.9*	*63.8*	*73.5*	*74.1*	*26.0*	*5.5*	*2.8*	*2.7*	*20.5*
B. *S. Afr., N.Z. & Australia*	*30.7*	*33.8*	*40.0*	*53.6*	*36.4*	*16.2*	*11.9*	*4.3*	*30.2*
1. S. Africa . .	45.8	51.4	67.2	72.9	27.1	10.6	7.4	3.1	16.6
2. New Zealand	43.0	43.3	43.3	66.1	33.9	22.3	16.7	5.6	11.6
3. Australia . .	20.8	23.3	27.3	42.7	57.3	17.5	12.9	4.6	39.8
III. *Asia*	*13.9*	*18.0*	*23.6*	*35.1*	*64.9*	*36.9*	*29.5*	*7.5*	*28.0*
1. Japan . . .	11.5	16.7	22.7	36.4	63.6	41.5	31.3	10.2	22.1
2. Other . . .	17.3	19.9	24.8	33.2	66.8	30.1	26.6	3.4	36.8
IV. *Western Hemisphere* .	*21.2*	*27.0*	*30.6*	*36.7*	*63.3*	*50.2*	*23.2*	*27.0*	*13.1*
1. United States	23.9	30.9	36.6	41.7	58.3	39.6	x	39.6	18.8
2. Canada . .	11.8	13.8	14.9	23.8	76.2	70.2	66.9	3.3	6.1
3. Latin America and Other	24.5	31.1	32.4	37.7	62.3	55.8	35.1	20.8	6.4
V. *World*	*38.6*	*50.6*	*56.7*	*64.2*	*35.8*	*24.6*	*14.2*	*10.4*	*11.2*

Source: Calculated from Summary and Country Tables of *Direction of Trade, Annual 1968-72*. See p. 374 for listing of countries in each group.

Notes:

1. "Africa" refers to African countries other than the Middle East and South Africa, and "Asia" to Asian countries other than the Middle East.
2. Australia and a motley group of small "Other Countries" (including dependent territories) have been listed under Group II in the above table, in view of their major political and financial links, even though their exports to Asia and the Western Hemisphere slightly exceed their exports to the rest of the world.
3. See Table III for estimates of separate countries listed under Western Europe.

would also make far less damaging and more acceptable the exchange-rate fluctuations or readjustments that may prove desirable, or unavoidable, with other countries, and particularly with the dollar area.

Finally, it would enhance the ability of the Community and of other major powers to participate effectively, and on a more equal and manageable basis, in the consultations aiming at desirable exchange-rate readjustments and at the reconstruction of a viable world monetary order.

TABLE III

WESTERN EUROPE: REGIONAL DISTRIBUTION OF *COUNTRIES'* EXPORTS, 1972

(in % of total exports)

Exports to → from ↓	Eur. Comm.	West. Eur.	Eur. Mon. Area	Eur.-oriented Areas	Total	Western Hemisphere			Asia
						Total	U. S.	Other	
I. *Eur. Comm.*	*52.0*	*68.7*	*76.2*	*83.2*	*16.8*	*13.3*	*8.2*	*5.1*	*3.5*
France	55.7	69.1	81.4	87.8	12.2	9.9	5.3	4.6	2.4
Germany	46.9	69.8	74.6	82.0	18.0	14.3	9.3	5.1	3.7
Italy	50.3	66.5	75.5	82.8	17.2	15.0	9.8	5.2	2.2
Netherlands . . .	73.7	82.4	86.7	91.0	9.1	7.0	3.8	3.1	2.1
Belg.-Lux.	74.0	82.3	86.6	89.6	10.4	8.4	6.1	2.4	2.0
U. K.	30.1	48.0	59.4	71.2	28.8	21.4	12.5	8.9	7.4
Ireland	77.0	80.4	81.4	87.1	12.9	11.9	9.4	2.4	1.1
Denmark	41.8	73.9	78.9	84.5	15.5	12.9	8.0	4.9	2.6
II. *Other Western Europe*	*47.1*	*67.6*	*73.5*	*83.5*	*16.5*	*13.4*	*8.4*	*5.0*	*3.1*
Austria	48.8	73.3	77.1	90.6	9.4	7.4	4.5	2.9	2.0
Switzerland . . .	46.5	64.5	70.3	77.5	22.6	15.7	8.8	6.9	6.9
Sweden	50.3	74.8	79.1	85.2	14.8	12.1	7.1	5.0	2.7
Norway	50.2	76.6	82.1	86.6	13.4	11.1	7.2	3.9	2.3
Finland	43.7	71.2	73.7	90.8	9.2	7.7	4.8	2.9	1.5
Iceland	32.4	53.2	54.3	67.1	32.8	32.0	30.7	1.3	0.8
Spain	45.2	55.0	64.8	70.9	29.2	27.1	16.4	10.7	2.1
Portugal	47.0	64.4	80.7	83.5	16.6	14.8	10.7	4.1	1.8
Greece	52.5	62.3	72.2	86.7	13.2	10.9	9.8	1.1	2.3
Turkey	45.7	61.1	73.4	85.8	14.2	12.0	11.7	0.3	2.2
Yugoslavia	36.1	49.4	53.6	89.7	10.2	8.9	6.7	2.2	1.3
III. *Western Europe* . .	*51.1*	*68.5*	*75.7*	*83.3*	*16.7*	*13.3*	*8.2*	*5.1*	*3.4*

Source: *Direction of Trade, Annual 1968-72* and July 1973.

R. T.