"Europe and the Money Muddle" Revisited

Introduction

Events have — alas! — confirmed the grim forecast which I ventured more than 20 years ago in "*Europe and the Money Muddle*"[1] and, in 1959, in two articles of this Review.[2] The inability of our governments to negotiate the long overdue reform of an anachronistic international monetary system finally brought about its total collapse, and the "new economic policy" launched in 1971 by the Nixon Administration has certainly failed so far to remedy either the world inflation or the world recession and unemployment. What saddens me in the present situation is not merely the "unholy alliance" of inflation and unemployment rates of 6% or more in most countries, nor the enormous balance-of-payments deficits encurred by even the richest countries in the world — some $ 50 billion last year, of which $ 18 billion by the United States alone[3] — nor even the humanly repugnant and intolerable income inequalities that condemn nearly 60% of the world population to survive (or starve) on the equivalent of about 60 US *cents* per day, on the average, as against the 17 *dollars* per day available to the most opulent 10%.[4] What distresses me even more is the fact that economists as well as statesmen are becoming increasingly resigned to such an intolerable state of affairs and hardly dare venture any credible promise of a new and more tolerable world order. The new

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[1] Yale University Press, New Haven, 1957.

[2] "The Return to Convertibility: 1926-1931 and 1958-? or Convertibility and the Morning After" (March 1959, pp. 3-57) and "Tomorrow's Convertibility: Aims and Means of International Monetary Policy" (June 1959, pp. 131-200), reprinted with minor changes in *Gold and the Dollar Crisis* (Yale University Press, New Haven, 1960, revised in 1961).

[3] OECD, *Economic Outlook*, December 1977, p. 65.

[4] *World Bank Atlas 1976*, pp. 5-6.

international monetary policies of inconvertibility and floating exchange rates have now been with us for five years or more already, but have brought no improvement so far — on the contrary! — to world inflation, unemployment, balance-of-payments disequilibria, and excessive income inequalities. A recent report of the United States Congress is significantly entitled *not* "How to Stop Inflation", but "How to Live with Inflation".

Equally discouraging is the fact that the short-term palliatives rallying the most agreement today run exactly *counter* to the long run goals toward which we should move. To quote only one example, the current so-called "locomotive" prescription urges three of the richest countries (the United States, Germany and Japan) to reduce sharply their external surpluses, or even — in the case of the United States — to keep on with large deficits in their external transactions. This is the very opposite of the piously reiterated resolutions of the United Nations urging the richer countries to devote at least 1% of their Gross National Product to the real financing of economic development in the poorer, less capitalized countries.

The only ray of hope that I can perceive is that our officials are notoriously poor forecasters. In the international monetary field they confidently promised, only a few years ago, that they would actively explore all and any reforms needed to improve the functioning of an anachronistic and shaky international monetary system, but that its two permanent pillars would remain the stability of exchange rates and of the price of gold, at $ 35 per ounce. I hardly need point out that the only major reforms of the system so far have been exactly the opposite: wild and erratic exchange-rate and gold-price fluctuations, with no end in sight.

In looking at what might, and *should*, be done to get us out of the present mess, I shall be guided in this paper by two deep convictions, apparently contradictory but in fact complementary and inseparable. The first is that we must do the opposite of what we are doing now. We must keep in mind the broad directions in which we should move, and reject any complacent resignation to short-term palliatives directly contrary to the imprescriptible long-term goals of a viable world order, fair and acceptable to all the countries, rich and poor, of our shrinking planet. The second is that, while keeping that long-run perspective well in mind, we should eschew detailed, but distant, blueprints on which opinion is still deeply divided at

present, and focus attention instead on concrete measures susceptible of being negotiated and implemented right away. As Mr. Krustchev used to say, and as emphasized before him by Professor — now Ambassador — Richard Gardner,[5] the long run can only emerge from actual short-term steps. We shall never reach the end of the road if we do not start moving. Among the various alternative measures immediately feasible, however, we should give priority to those which I would call "seminal" or "germinal", i.e. those most able to trigger an evolutionary momentum of their own toward the longer-term reforms that still elude us today.

I. How did we get here?

Before discussing where we should go and how, let us try first to agree on how we got into the mess from which we must now extricate ourselves.

1. *Stagflation or Inflession?* — Permit me to start with a semantic quarrel. The widely used term "stagflation" seems to me a misleading summary of a situation in which stagnation did not precede and cause inflation, but in which recession, or even depression — rather than mere stagnation — followed and was largely triggered by the previous surge of world inflation and the inescapable, even if often half-hearted, attempts to slow it down in order to ward off the very real danger of hyperinflation. I suggest the term "*inflession*" or "*infession*" as more descriptive and suggestive than "*stagflation*".

2. *Non-Monetary Causes.* — The root causes of the world inflation that now engulfs us lie far deeper, of course, than the "permissive" monetary policies which have accomodated — and financed — it. They derive primarily from the growing scarcities of real resources eloquently denouced by the Club of Rome. While obviously controversial in their detailed projections, the main themes of the Club of Rome seem to me incontrovertible in their broad

[5] In his brilliant book on *Sterling-Dollar Diplomacy* (revised edition, McGraw-Hill, 1969). My own conviction in this respect is derived from my successive experiences with the *International Monetary Fund* in 1946-1949, and with the *European Payments Union* in 1949-1951.

sweep and conclusions. Future historians will probably describe as a unique parenthesis in world history the spectacular increase of material production and consumption of the last two hundred years. It began with the so-called "*industrial revolution*" which helped meet real, basic needs for food, shelter, clothing, health, transportation etc... It was increasingly sustained later by what might be called the "*advertising revolution*" which sought outlets for growing productive capacity in the creation and propagation of new wishes or whims not perceived previously as real needs. It was accelerated further, after World War II, by the very success of Keynesian policies in avoiding the cyclical recessions which had, up to then, periodically slowed down this continuing process of economic growth. Last but not least, it is now compounded by the explosion of the most inflationary type of expenditures by far, military expenditures, to an incredibly wasteful level of about $ 350 billion a year, just about equal to the total GNP on which nearly 30% of the world population has to survive today: a meager 36 US cents a day per capita.[6]

Outside of its polluting impact on our atmosphere and environment, this enormous surge of material production and consumption has brought within our horizon increasing prospective scarcities of essential resources. Most of these scarcities may be overcome in time, but only at sharply rising costs, particularly if suppliers are encouraged by permissive monetary policies to "charge all that the traffic will bear" and to base their expectations and claims on persistent price flexibility upward only, rather than on prices fluctuating around traditional norms embedded in approximate overall stability in the long run. Price and wage rises then tend to feed on each other indefinitely and to spread from the scarce sectors to the rest of the economy.

3. *National Monetary Permissiveness.* — This brings us to the role of monetary policies and institutions in this inflationary process. This role has long been, in most if not all countries, to finance and underwrite price and cost pushes whenever resolutely anti-inflationary policies would run too great a risk of unemployment, strikes, and social unrest, not to speak of dismissal of responsible officials and overthrow of political leaders. Legal restraints, such as

6 *World Bank Atlas*, 1976, p. 6.

public debt ceilings and minimum gold cover requirements, were invariably ignored, relaxed, and eventually abolished whenever their enforcement would have shackled the authorities.

Yet, until about 1969, inflation tended, on the whole, to remain a national rather than a world phenomenon. The countries which inflated faster than others became more and more uncompetitive in world trade, ran increasing foreign deficits, compounded eventually by capital outflows, and were forced sooner or later by the depletion of their international reserves and borrowing capacity to devalue their currency, or to let it depreciate on the exchange markets, vis-à-vis the currencies of the less inflationary countries. World export and import prices, measured in US dollars, remained relatively stable, increasing by less than 1% a year, on the average, throughout the decade of the 1960's. This annual rate of increase, however, rose abruptly to an average of 10% over the following four years, reaching more than 30% in the 12 months that preceded the explosion of oil prices at the end of 1973.

4. *International Monetary Institutions and Policies.* — This was made possible by international monetary institutions and policies that extended monetary accomodation and permissiveness from the national to the international scale. The so-called "gold-exchange standard", or rather "gold-convertible dollar standard" of the postwar years relieved in fact — even though not in law — the United States from the adjustment pressures which external deficits imposed upon all other countries. Only a minor fraction of huge and persistent US deficits — triggered initially by the Vietnam war — were financed by US reserve losses. Most of them were financed by foreign central banks' acceptance of US banks and Treasury debts as international reserves, doubling these over the years 1970-1972, i.e. increasing them as much over this brief spell of three years as over all previous years and centuries. This world reserve flood frustrated the famed process of balance-of-payments adjustment for all other countries as well. Practically all countries of the world — except the United States — shared in these reserve increases, enabling some of them to pursue inflationary policies of their own without the usual sanction and restraint of reserve depletion, and making it next to impossible for others, more averse to inflation, to offset fully through domestic credit contraction the inflationary impact of their foreign exchange purchases.

A third major defect of this dollar-anchored system of reserve creation is that it led nearly automatically to their investment in the United States and a few other rich countries, rather than in the countries most in need of foreign capital. Less than 5% of the huge reserve increases of the early 1970's were invested in the less developed countries, well over 95% being placed in the more developed countries. In the area that is — or should be — most amenable to their influence and control, national and international monetary authorities do exactly the opposite of what they preach: they foster capital investments, *not* in the poorer countries most in need of capital, but in the richest, most capitalized countries.

5. *The Abortion of International Monetary Reform.* — These obvious shortcomings of the gold-exchange standard led to its predictable — and widely predicted — collapse on August 15, 1971, 40 years nearly to the day after its previous downfall on September 21, 1931. After 10 years of marathon debates and negotiations, this second collapse elicited at long last a near consensus of official as well as of private experts on the broad features of the reforms most essential to the reconstruction of a viable world monetary order. The most authoritative expression of this consensus may be found in the last report of the " Committee on Reform of the International Monetary System and Related Issues " (Committee of Twenty).[7] [May I add, immodestly, that they bear an uncanny resemblance to my own proposals to the Joint Economic Committee of the United States Congress, 15 years earlier, on October 28, 1959.]

Incredible as it is, the reforms finally incorporated in the second Amendment to the Articles of Agreement of the International Monetary Fund practically ignore the diagnosis and prescription painfully worked out over more than 12 years of continuous consultations among the participating countries. All that is proposed in effect is to recognize the collapse of the Bretton Woods system, and to legalize the general — and still illegal — repudiation of the convertibility and exchange-rate commitments inscribed in the Bretton Woods Treaty. The attention of most commentators has centered primarily on the proposed new Article IV of the IMF Agreement, misleadingly titled " Obligations regarding Exchange Arrangements," but which in fact

7 See the " Outline of Reform " on pp. 7-48, and particularly p. 8 of *International Monetary Reform. Documents of the Committe of Twenty* (International Monetary Fund, Washington, D.C., 1974).

leaves every member free to adopt any exchange arrangements it chooses, except only the one still imposed on all countries by the present IMF agreement, but universally disregarded by them, i.e. " the maintenance by a member of a value for its currency in terms of... gold." (Article IV, Section 2, b)

I shall abstain from discussing further these new exchange-rate arrangements. They are probably unavoidable for now, but do not change the realities of the previous system as radically as is usually thought. Exchange rates were far from stable under the Bretton Woods system,[8] and most currencies remain pegged today, as precariously as yesterday, to the US dollar, or to some other major currency or batch of currencies. The main difference is that the US dollar is no longer the unquestioned benchmark for such pegging and more or less frequent readjustments. It is now subject to wide and reversible daily fluctuations vis-à-vis other major currencies, downward as well as upward, instead of appreciating repeatedly and continually, as before 1970, in terms of practically all currencies. Far more significant — and devastating, in my opinion — is the abdication of all attempts to reform an absurd, inflationary, and unfair system of world reserve creation whose unanimously diagnosed shortcomings are at the root of the Bretton Woods collapse and are bound to plague and frustrate the new floating rates system as well as the previous pegged rates system.

6. *The Abdication of Responsibility to the Private Market.* — This abdication is further compounded by the increasing unloading of balance-of-payments financing responsibilities on the private market. International bond issues have quadrupled over the last four years, rising from $ 8 billion a year in 1973 to $ 32 billion in 1977[9] and the foreign assets of major countries' commercial banks (including their foreign branches), net of inter-bank lending, are estimated to have increased by $ 230 billion from the end of 1972 ($ 110 billion) through June 1977 ($ 340 billion), i.e. nearly 2 ½ times the growth of central banks' foreign exchange reserves

8 Between 1948 and 1965, only ten countries had maintained exchange rate stability, while 94 had depreciated their rate, many of them repeatedly, and 80 of them by 30.5 per cent or more.

9 *World Financial Markets* (Morgan Guaranty Trust Company of New York), December 1977, p. 13.

($ 98 billion) and more than 14 times the growth of IMF loans ($ 16 billion).[10]

Particularly striking is the role of foreign branches of US banks in this process. Their claims on foreigners (net of those to other branches of the parent bank) are now more than twice those of head offices in the United States ($ 169 billion, as against $ 83 billion, at the end of June 1977), having more than decupled since the end of 1969 ($ 16.6 billion).[11] About $ 60 billion of these loans are from branches in the Bahamas and Cayman islands whose fantastic mushrooming may well be explained by the need to meet the competition of other countries " offshore " banks, but has bizarrely elicited so far no serious attempt to reach international agreement on proper restraints and controls.

II. How do we get out?

But enough of this grim historical record and diagnosis! Let us look to the future and try to see how we could possibly " cure " our diseases (inflation, unemployment, intolerable balance-of-payments disequilibria and income disparities) rather than " live with them "!

1. *International Monetary Reform.* — I shall not insist on commonsense suggestions regarding the basic, non-monetary, causes of our problem, particularly the conservation and development of scarce resources. Coming to the problem of international monetary reform, more familiar to me, I would stress the following points.

a) First of all, the need to regain control over the excessive rates of reserve creation and private international lending which play such a large role in the present world inflation. As suggested by the Committee of XX, this would require the substitution of *international* reserves under IMF control (broadly similar to the barbarously named SDR's) for foreign exchange as well as for gold, and an overall rate of reserve creation that does not facilitate and invite further inflationary excesses. Balances in *national* currencies

[10] *Id.*, p. 12 and *International Financial Statistics*, November 1977, pp. 22 and 24 (SDR estimates converted into US dollars).

[11] *Federal Reserve Bulletin*, October 1977, pp. A 60-62, and corresponding Tables in former issues.

might have to be retained in a transitional phase, to finance daily interventions in the exchange market, but they should be limited to agreed ceilings beyond which they would have to be redeposited into reserve accounts with the IMF.

b) Such a reformed system is indispensable to enable the IMF to cure the other shortcomings of the present system diagnosed above. It would enable it to " recycle " the surpluses of any country (including those of the OPEC) for purposes collectively agreed and commanding the highest priority, such as the offsetting of purely speculative and disequilibrating capital movements and the financing — mostly through the World Bank, its affiliates and regional banks — of feasible development in the poorest and least capitalized countries of the Third World.

The acceptance of IMF reserve accounts in settlement by the surpluses countries might require more attractive exchange guarantees and other provisions than those now attached to SDR accounts. If, and as long as, some major surplus countries refused nevertheless to accept IMF accounts in settlement, the " recycling " task would have to depend in part on the participation and mutual committments of the recipient " reserve-center " countries (benefiting from the investment of such surplus funds) to reshufflle among each other speculative switches of such investments from one currency to another, with of course adequate liquidity, solvency and exchange guarantees.

c) This proposed strengthening of the IMF may be particularly necessary and urgent to solve or ward off the liquidity and confidence crises that might be triggered by the overexposure of commercial banks, defaults on some of their huge lending of recent years, or even merely too abrupt a curtailment of such loans in the foreseeable future.

2. *Exchange Rate Interventions.* — Let me admit that I am not confident about the chances of any prompt agreement on the reforms that I have just outlined.

a) Relatively rich and developed countries which should *contribute* real resources to the rest of the world are now running huge current account deficits *absorbing* instead real resources from other countries, including of course the OPEC countries.

b) The correction of these deficits, obviously intolerable in the long run, will not be easy. The whole infrastructure of the U.S. and many other countries was built on cheap energy and cannot be changed overnight.

c) The few countries still in surplus (primarily some of the OPEC countries, Japan, Switzerland, Germany, the Benelux countries and, since last year, the United Kingdom and Italy) will have to show patience and understanding, and cannot avoid financing the deficits that are the counterpart of their surpluses. One of their main concerns at the moment is the sharp and excessive depreciation of the dollar vis-à-vis their own currencies, since this risks to curtail their exports, boost their imports, and worsen further their unemployment problem. Public opinion in the United States, on the other hand, is understandably averse to measures that might stop the dollar depreciation, but only at the risk of aggravating the U.S. recession and unemployment, all the more so as the domestic inflationary impact of currency depreciation is far smaller, and less perceived by the public in the relatively closed U.S. economy than in the wide open economies of most other countries.

A continuation of the present trend could hardly fail to stimulate a disastrous relapse into protectionism and/or exchange controls by countries complaining of the growing undervaluation of the dollar. As suggested recently by Mr. Roosa, former Under-Secretary of the U.S. Treasury, a concerted effort by the major financial countries to agree on desirable or unavoidable exchange-rate adaptations, and to participate in the market interventions necessary to guide them, would be a major and necessary step to ward off such a disaster.

III. A Challenge to the European Community

The European Economic Community has been desperately slow in reacting constructively to the problems and challenge forced upon it by the collapse of the world monetary system under which it had thrived, and whose very shortcomings had indeed hidden some of its own problems (as suggested on p. 53 above).

1. *Monetary Union? or Pre-Union?* — I shall refrain from discussing here the fundamental policy changes and institutional

reforms indispensable to transform into reality the dream of full economic union which I share with the courageous and forward-looking President of the Community, Mr. Roy Jenkins. Economic and monetary union is as essential as ever — or more — to enable Europe to play a constructive role in the worldwide reforms necessary to fight inflation, underemployment and speculative exchange crises and disequilibria in Europe as well as in the rest of the world. It should be an essential plank of the parties that will soon vie for the first direct election of the European Parliament.

I shall concentrate instead (for the reasons suggested in my introductory remarks) on the measures that could — and *should* — prove feasible in the immediate future: first, to shelter the Community, to the extent possible, against the external shocks that have played such a large role in the failure of the Werner plan for monetary union; secondly, to participate more effectively in the worldwide arrangements that must be negotiated urgently, particularly with the United States; and third to initiate at the same time the evolutionary momentum required for eventual economic and monetary union.

I would suggest for this purpose only a few immediate, modest, but " seminal " measures aiming at creating a " European Exchange Area ", rather than full monetary union (or to use the slogan of President Werner,[12] to begin with a state of " pre-union "). They would leave intact the use of national currencies in domestic transactions, but would offer an alternative to the foreign currencies, Euro-dollars, and other Euro-currencies widely used already in transnational contracts which cannot, by definition, be simultaneously denominated in the national currency of each participant.

2. *The " Europa " as a " Parallel Currency ".* — This alternative should be the adoption of a so-called " parallel currency " which I shall denominate for short " *Europa* ", in order to distinguish it from the multiple " Units of Account " now in existence, to symbolize the ultimate aim of European Union, and — very practically — to dispense with the need of translation into the various languages of Europe and of the world. The availability of such a parallel currency for international capital investments should help attract

[12] Pierre Werner, *L'Europe Monétaire Reconsidérée*, Centre de Recherches Européennes, Lausanne, 1977.

such investments from the stronger currency countries rather than merely from the weaker, as tends to be the case at present. It should reduce speculative capital movements aggravating balance-of-payments disequilibria, exchange rate fluctuations, and inflationary pressures in the weaker currency countries (i.e., " the vicious spiral ".)

The first initiative might come, as has most often been the case in the major monetary reforms of the past — such as the displacement of gold and silver moneys by bank currency and deposits — from the private sectors of the economy rather than from national bureaucracies and governments. Commercial banks and other financial intermediaries might use the " Europa " denomination not only for the flotation of Euro-bonds, but also for the opening of deposit accounts and bank loans for which the use of foreign and Euro-currency denominations is already prevalent and legally permitted.[13] This would give their customers a valuable alternative to the use of parallel *national* currencies — such as the pound sterling in older days, and the dollar and the mark today — whose huge fluctuations in terms of one another as well as of other Community currencies make them a less and less satisfactory instrument in this respect.

3. *Alternative Initial Definitions.* — The main requirement of a satisfactory definition of the Europa should be to make it sufficiently fair both to the lenders and to the borrowers to attract a large volume of operations in both directions. Some of the alternative definitions reviewed below obviously meet this requirement better than others, but the market itself should be the test, and determine which definition is most acceptable to it.

a) One of the obvious candidates from this point of view might be deemed to be the " Unit of Account " adopted in the early 1960's by the *Kredietbank* of Luxembourg, and in which various banking syndicates have floated numerous Euro-bond issues, totalling the equivalent of more than $ 1 ½ billion today, i.e. considerably more than corresponding issues in all other units of account taken together. This unit was initially modelled upon that which the *European Payments Union* used to general satisfaction throughout its

[13] About $329 billion (86%) last September, of the foreign assets of banks in the eight countries reporting to the BIS ($383 billion) of which $310 billion in dollars (73%), in marks (16%) and in Swiss francs (6%).

eight years of existence; the basic intention was to identify the unit of account with the exchange value of whichever member currency would retain in fact the greatest degree of stability. But stability in terms of what?

The legal definition initially took as benchmark gold, in which all IMF par values were then defined. The gradual disintegration of the Bretton Woods system has unfortunately forced successive and unexpected switches: from gold at first to IMF parities no longer related to gold, then to the Smithsonian " central rates ", and finally to the few currencies maintaining effectively agreed margins of fluctuations vis-à-vis one another, i.e. the currencies of the " snake ". If the snake itself were to disappear, the unit of account would remain equivalent to the last currency to leave it, and would become in effect a national currency. The system of floating exchange-rates generalized in March 1973, and which the Second IMF Amendment proposes to legalize, excludes any *common denaminator* in terms of which stability could be defined. The foreign exchange world has become a world of general relativity, an Einsteinian world rather than a Newtonian world. When an exchange rate changes, one cannot tell any more whether one currency has appreciated or the other depreciated.

b) The strongest and most ambitious definition of a different " Europa " would be that recently suggested and powerfully argued by a number of economists:[14] a constant purchasing power, measured by a weighted average of national cost-of-living indices. Such a radical proposal would meet strong official opposition, however, unless it became a last desperate solution in the unlikely event of generalised hyperinflation and flight from all national currencies. It would also be unlikely to attract sufficient borrowings, unless at extremely low, or even negative, interest rates raising a host of difficult problems. Finally, it would require complex calculations and invite endless controversies regarding the honesty and reliability of the national indices entering these calculations.

c) The simplest formula of all would be an exchange option for the creditor, equating in fact the Europa with whichever member currency remains strongest — rather than stablest — in the market.

[14] See the " All Saints' Day Manifesto for European Monetary Union " in *The Economist* of November 1, 1975, and the carefully articulated proposals of JACQUES RIBOUD, notably in *Une Monnaie pour l'Europe: l'Euro-stable*, Paris, 1977.

This would dispense with " weighted basket " calculations and should also be more attractive to prospective lenders than any national currency. I would not rule it out firmly as a possibility since the U.S. dollar succeeded for many years in attracting willing borrowers at a time when it was unanimously regarded as the strongest currency in the world, equal to, or even better than gold.

d) The definition most susceptible of rallying the broadest agreement in the near future, however, is probably the *European Unit of Account* (EUA in English, and UCE in French) officially adopted by the Community in 1974, and progressively extended to more and more of its operations (notably, those of the European Development Fund, the Coal and Steel Community and, more recently, medium-term monetary support credits and the budget of the Community). A growing number of such operations are now channelled through bank accounts denominated in EUA rather than in national or foreign currencies. This EUA denomination should be as, or more, attractive to the lenders than the dollar, or Euro-dollar, denomination still prevalent today in international transactions, official and private. An EUA claim would have appreciated vis-à-vis the dollar as of the end of 1977, by 20% since the end of 1969, and nearly 9% in the last year alone.

The main drawback of the EUA is that it is exposed to depreciate in terms of the stronger member currencies because of the downward pull exerted upon it by any depreciation of the weaker currencies, such as the pound and the lira until recently. This might call for a stronger Europa definition, excluding from the weighted basket calculations any currency depreciating in relation to the EUA by, let us say, more than 5% a year. This would, however, create difficulties for financial intermediaries insofar as they could not protect themselves as easily and fully on the market against exchange risks on daily imbalances between their borrowing and lending transactions. One might hope, however, that the worst period of exchange disturbances among member currencies is now past, and that the major currencies with heavy ponderation in the EUA basket will be able — as they must in the end — to preserve a far better approximation to stability vis-à-vis one another than has been the case from 1969 until about the end of 1976. Moderate interest-rate differentials should suffice, in that case, to make the EUA as attractive as any national currency for lenders as well as for borrowers.

4. *From a Parallel Europa Currency to Full Monetary Union.* — If and when the drive toward monetary union can be resumed, the Europa would provide a far more realistic path toward it than the *sudden* and *simultaneous* switch from all national currencies to a common currency envisaged in the Werner Plan for the end of the process only.

a) Long before that, the development of a private market in short, medium and long term Europa obligations would help, and be helped by, official transactions in Europa. First of all, the Europa would provide the authorities of the Community, of national governments, local authorities, and other official organizations — within and even outside the Community — with a currency unit alternative to those now in use (primarily the U.S. dollar) for the denomination of their borrowing and lending operations and investments. It would provide, in particular, a most logical form of exchange-rate guarantee for the " new instrument of Community borrowings and loans " envisaged in the decisions of the European Council of the 5th and 6th of December 1977. Secondly, it could become a far more appropriate instrument than a widely fluctuating dollar for central banks' interventions and for agreed monetary support operations in the foreign exchange market. It is ludicrous to note that such support operations in exchange-guaranteed Community currencies are now labelled " *credit operations* " and " *repaid* " (?) for the most part by credit claims on the United States, denominated in an inconvertible, fluctuating and unguaranteed foreign currency. It is high time that central banks revise a terminology that may have been adequate in former days, but is certainly absurd and misleading today.

A parallel Europa currency, properly defined and guaranteed, should become in time the main — or, at least, an alternative — means of foreign exchange interventions and settlements between the countries of the Community, and even play an increasing role in transactions and settlements with other countries, including the OPEC countries.

b) It should also provide a more logical *common denominator* for member countries' exchange rates and a *benchmark* for the exchange-rate readjustments that will still prove necessary in the medium term, as well as for their eventual, hoped for, stabilization in the longer term. Trade, services and capital transactions among

member countries are probably today more than 10 times larger than their transactions with the United States, and several times larger also than their transactions with other countries whose currency is precariously pegged to the dollar. A European foreign exchange unit would provide a far more logical " center of gravity " than the dollar for the definition and occasional readjustments of member countries' exchange rates. Yet, in the absence of such a unit, the dollar remains in fact the only common denominator in which their currencies are quoted by the market to the man in the street.

c) Admittedly, a *Europa* parallel currency and exchange area would leave unsolved the major obstacles to full monetary union and the actual merger of the national currencies into a single common currency for the Community. I shall not dwell here on the multiple and difficult policy *and institutional* reforms that will be necessary to make such a goal realistic and possible. I am confining myself now to what seems most urgent and feasible, rather than on the policy and institutional problems that still divide deeply academic and business circles as well as responsible policy makers and their advisers.

The proposals outlined above would be valuable for their own sake, and constitute in any case a prerequisite step toward more ambitious objectives. If and when sufficient progress has been achieved to make monetary union conceivable as a practical policy goal, the proposed *Europa* would provide a far more realistic transition than the Werner Plan to the eventual switch from national currencies to a single European currency.

Rather than the *abrupt* and *simultaneous* jump envisaged in the Werner Plan, it would *permit each country to move at its own pace*, enlarging gradually the use of the " Europa " from the external transactions legally admitted at the start — for operations now conducted already in Euro-dollars and Euro-currencies — to more and more internal transactions as well. Even the most skeptical or jingoist opponents of monetary union should be enthusiastic supporters of the Europa as an urgently needed shelter against foreign shocks repeatedly unleashed by past, present, and foreseeable exchange crises in the disorderly monetary system inherited from the collapse of Bretton Woods.

IV. Shall We Start?

Is there any chance that we can start moving? In the paralyzing political atmosphere in which we are bogged-down, many may be temped to say " No! " and to quote to the old saying: " Politics is the art of the possible."

I have long learned, however, from the most constructive mind of the postwar era, Jean Monnet, that it is also " the art of making possible tomorrow what still seems impossible today."

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