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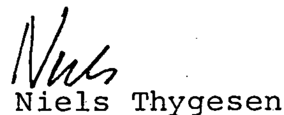
Dear Günther.

In agreement with Tommaso I forward the note I had promised to do for the November meeting for circulation through you to the members together with the notes prepared by MM. Godeaux and De Larosière and, possibly, a conceptual issues paper. If you have any queries please call me. I shall be travelling in the Netherlands and Belgium Thursday-Friday, but I can be reached at my office Monday or during the weekend at 45-2-850085. Any comments you may have would be appreciated.

Best personal regards,



Niels Thygesen

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A EUROPEAN CENTRAL BANKING SYSTEM
- SOME INSTITUTIONAL CONSIDERATIONS

Niels Thygesen

Summary:

The note asks how central banking functions could be exercised in a framework of fixed exchange rates and high capital mobility which imply the need for essentially one monetary policy. It raises four main issues:

(1) What policy decisions need to be taken jointly ?

(2) Is there a need for a central authority with an oporational capacity or could a central banking system be run entirely through national central banks ?

(3) How would the governing bodies of the system be composed ?

(4) How would the system be positioned in the EC framework and how could it be made autonomous and accountable at the same time ?

The note ends with some brief reflections about the timetable.

INTRODUCTION

The present note, prepared at the request of President Delors for the November meeting of the Committee, raises some institutional issues relevant for the exercise of central banking functions in an advanced stage of monetary integration. It is assumed that participants in this process towards full Economic and Monetary Union have (1) implemented the decisions to liberalize capital movements already taken, and (2) invested substantial efforts and credibility in making fixed nominal exchange rates among the participants sustainable.

Such an advanced stage of monetary integration would still fall short of full Monetary Union, characterized by near-perfect substitutability of participating national monies and an important role for a parallel, common currency. In the present vision national currencies exist, they have retained most of their present functions unimpeded, and no explicit role is outlined for an emerging common currency. The basic issues of designing an institutional framework for an advanced stage of monetary integration arise even in the absence of a common currency, though many would see both economic and political-symbolic benefits in giving such a currency important functions from the start of a more institutionalized stage. However, the Committee has decided to discuss the issue of a parallel, or ultimately a common, currency at its December meeting. Conclusions from that discussion could then be merged with those that arise out of the November meeting on the institutional framework. Writing about the central bank without reference to a common currency is obviously con- straining.

The present note is addressed to the medium-term future, sufficiently far ahead to consider the full implications of operating essentially one monetary policy, as required by assumptions (1) and (2) above. In that sense it has approximately the same time perspective as President Pöhl's paper "The Further Development of the EMS", circulated with his letter of Sept. 14, and including seven principles of a "European Monetary Order" (pp. 12-14).

The advanced stage of monetary integration here foreseen with respect to institutionalization at the European level incorporates several specific transfers of authority which may be regarded as some of the concrete steps towards EMU which the Committee has been asked to study. Governor de Larosière's paper on those concrete steps that seem the most urgent adds an order of priorities within this set of reforms.

My interpretation of the Committee's mandate: that it is desirable to have a comprehensive view of institutional reforms, even though not all of these could be argued to be necessary to proceed towards EMU, is based on two considerations: (1) a clear vision of the principles of a European Monetary Order is necessary to give direction to the immediate steps; (2) the difficulties of advancing monetary integration through institutional steps - following adoption of the European Single Act, such changes require a revision of the Rome Treaty (Art. 236) - suggest that a package of reforms, rather than individual components of it, be submitted for political approval in the form of Treaty revision and national parliamentary ratification. The individual components would then be available, but their activation would be subject to a unanimous decision among those participating fully in the EMS or its successor central banking system. The framework would be decided by all EC member states, but the implementation of individual reforms would not have to await the readiness of all to take part fully.

In asking how central banking functions could be exercised in a framework of fixed exchange rates and high capital mobility, implying a need for essentially one monetary policy, the note raises four main issues in the following sections:

(1) What policy decisions need to be taken jointly?

(2) Is there a need for a central authority with an operational capacity or could a central banking system be run entirely through national central banks?

(3) How would the governing bodies of the system be composed?

(4) How would the system be positioned in the EC framework and how could it be made autonomous and accountable at the same time?

The note ends with some brief reflections about the timetable.

JOINT DECISIONS ON WHAT ?

Any international or regional monetary system has to come to grips with two issues: (1) the methods of relative adjustment, and (2) the overall nominal thrust of the sum total of participants' monetary policies. International agreements, including the Bretton Woods system and the EMS, have typically been more explicit on (1) than on (2). The use of exchange-rate adjustments was intended to be circumscribed by the IMF Articles of Agreement and by joint decision-making in the EMS.

The latter has elaborate rules for interventions and their financing, essentially aimed at ensuring maximum defensive capability and hence credibility for the exchange-rate commitment. The EMS has also developed procedures for relative adjustments in the case of tensions that go beyond interventions to interest-rate adjustments. Here decision-making is less joint, though clearly moving in this direction as exemplified by the Basle/Nyborg Agreements of September 1987 and subsequently tested by the coordinated interest-rate responses later in 1987, as a weak dollar required a differentiated, but coordinated response.

Attention to (2) is more implicit. It is well known that a group of countries with fixed exchange rates between them and increasing capital mobility will have room for only one monetary policy. The Bretton Woods system and the early EMS did not have to face up to this issue directly, because they were both protected by a mixture of capital controls for the short-term and some scope for changing the exchange rate in the longer-term. The recent EMS has not been able to avoid the issue. In the absence of an explicit monetary rule for the participants as a whole, the combination of efforts to defend fixed exchange rates and to impose most of the burden of short-term adjustment on the weaker currencies has led to an implicit rule: monetary policy for the EMS participants as a whole tends to be determined by that of its largest and least-inflationary participant. Defending fixed exchange rates provides rules for managing the relativities of the system and promotes convergence of inflation; the implication of the practice that reserves used for intervention in defending a weak currency have to be reconstituted within the span of a few months is that convergence - provided that exchange rates do remain fixed - will be towards the low inflation in the FRG and not towards some average as would be the case if intervention credits were a more permanent safety net.

By using the degree of freedom for monetary policy to orient convergence increasingly in this direction, the EMS has succeeded to an unexpected degree in becoming "a zone of monetary stability" in the double sense of promoting both exchange-rate and price stability. The very success of the system has made possible the ambition to study how one could achieve the transition from the present EMS to a central banking system appropriate for an advanced stage of monetary integration.

The challenge is to design a new system which can deal still more

efficiently than has the EMS with the relative adjustments required of national monetary policies within an overall mandate to continue to promote medium-term price stability, while moving towards a irrevocably fixed set of exchange rates among the participants. When that final step has been taken, the need for the central banking system to preoccupy itself with relativities will by definition disappear, since interest rates, including those set by national central banks, will have to move very closely together (while growth rates of money and credit aggregates, if they are still measured, may differ between regions/ nations). This note is concerned with the stage where relativities are still important, but where guidance in their adjustment is based on more explicit collective decisions than the present, more implicit rules of the EMS.

The motivation for putting an institutionally more structered system in place can hardly be found in outright dissatisfaction with past performance but rather in two considerations about the nearer-term future. The first is operational, the second conceptual.

The reliability of a domestic monetary aggregate in the FRG as the intermediate objective for German, and indirectly EMS, monetary policy is weakening as capital mobility increases and is extended to short-term instruments. This process affects not only the size of potential flows in countries that undertake liberalization, principally France and Italy, but also the ability of the Bundesbank to keep its preferred monetary aggregate as close to targets as has been the case on average over the past 14 years. Financial integration increases the risk of policy errors and hence the incentive for all participants to modify the present paradigm. But the evolution is gradual and there is no need to try to discard the present system before its successor is well-defined in terms of a jointly accepted inflation objective.

The more conceptual consideration is that if this medium-term objective is as generally accepted among EMS-participants as appears to be the case, the low-inflation credibility which the EMS has so far derived from the performance of the Bundesbank could be transferable to a European central banking system operating under the explicit mandate of pursuing "medium-term price stability". Such a mandate is at the same time necessary to make further monetary integration appealing also to the most stability-oriented EMS-participants, to whom the intended future should not in this respect look inferior to what has already been largely achieved.

Could the objective be made more specific by pointing out in

terms of what price index stability is to be achieved or by prescribing one or more intermediate targets ? The FRG or other countries which have emphasized this ultimate objective have not been as specific in this respect. One could think in terms of an average index for the participants of traded-goods prices, leaving the precise formulation and the selection of one or more aggregate monetary targets-credit targets would be identical, if the participants were to float freely and jointly vis-à-vis third currencies - to those who are to implement policy within that mandate. Research into the stability of the money-income relationship for groups of European countries and into rules for assigning domestic credit targets to individual countries within such groups under fixed exchange rates is at an early stage, though promising; it would be premature to be specific. The statutes of an eventual European central banking system need only contain a listing of its ultimate objective(s) and of the policy instruments that are assigned to it (in addition to the functions, composition and relative competence of its governing bodies and their relationship to other European authorities, briefly discussed in the following sections).

Three types of decisions on monetary and intervention policy might be placed at the collective European level[1]:

(1) adjustment of short-term interest differentials;
(2) intervention policy vis-à-vis third currencies; and
(3) changes in reserve requirements.

The first two relate to the smooth functioning of the fixed exchange rate system, while the third can modify the overall thrust of policy. The first two can be given a simpler, more operational content once the role of a parallel currency has been discussed in the Committee; such a currency and the short-term financial markets trading in assets denominated in that currency would clearly play a major role in the operations envisaged under (1) and (2). But the need for joint decisions on these issues would arise irrespective of the existence of a parallel currency.

The adjustment of relative short-term interest rates is the central instrument in managing the present EMS, and a relatively high degree of coordination and occasionally de facto joint, or at least bilateral, decisions have been observed. With the Basle/Nyborg Agreements of September 1987, participants have developped a flexible set

of instruments for containing incipient exchange-market tensions: intramarginal intervention, flexibility within the band, and changes in short-term interest differentials. The combination has proved robust in periods of tension, notably early November 1987, less so more recently. The risk remains of repeating the experience of earlier periods of tension in which public criticism and mutual recrimination between Ministers of Finance surrounded short-term monetary management. By making such decisions subject to arbitration and joint authority within a European central banking framework governments could step back from the limelight of involving themselves directly in ways that are more likely to provoke than to prevent the occurrence of exchange-market crises. It is a more technical issue whether the joint authority could be exercised simply through interest rates administered by the national central banks or whether an intervention capacity in national money markets would be required as well.

Tensions among EMS-currencies have often in the past had their origin in financial disturbances from third currencies, notably movements in the dollar, to which the European currencies were seen by the markets as being sensitive in different degrees. These perceived - in some cases real - differences have in turn had their origins in capital controls and in expectations of divergent policy reactions to the external financial disturbances. Both factors are of diminishing importance, as the international competitiveness of financial markets of France, Italy and the smaller EMS-countries improves in step with the removal of capital controls, and as basic economic convergence strengthens. Yet a visible capacity to intervene jointly in third currencies and to do so in ways that are conducive to the cohesion of the European currencies would be important. Without a presence in the major exchange markets it is also difficult to see how a European central banking system could be taken seriously as a partner in the international monetary system. This would require some permanent though possibly limited, pooling of reserves through a successor to the European Monetary Cooperation Fund.

The third instrument is the ability to vary required reserves held with the European central banking system. Requirements would be based on a domestic monetary aggregate, possibly the monetary base, and it would be met by depositing dollars, gold and currencies of other participants, or ECU. This instrument would permit an influence on the total rate of monetary or credit expansion in the area. As such it would also have an indirect, longer-term impact on the value of the

participating currencies in terms of third currencies.

The three instruments proposed would all be major examples of shifts towards the European level of decision-making authority which is to-day fully national, though their active use is in practice constrained by habits of informal cooperation and, more important, by the self-interest of participants in avoiding inefficiencies which would result from a more competitive use of the instruments of monetary and exchange-rate policy. It remains to consider how the one decision in the EMS which is to-day subject to de facto joint decision-making, viz. realignments of central rates, could be handled in the situation where a European central banking system exists, but exchange rates within the area are not yet irrevocably fixed. Would there be a case for vesting authority in this respect with the new institution rather than leaving it with the ECOFIN Council ?

There are arguments for and against such a transfer. A major purpose of having a European institutional framework for monetary policy before full Monetary Union and a common currency is to constrain and gradually eliminate realignments; and, in particular, to assure that their residual uses, if regarded as necessary to prevent longer-run tensions, will be sufficiently small to preserve continuity of market exchange rates surrounding realignments. This has been an important feature in the containment of speculative pressures in the recent EMS experience. If private markets would interpret a transfer of authority for making the residual small realignments to the participating central bankers as part of their task of collective monetary management as a signal of an intended tightening of the EMS, such a transfer would be stabilizing and desirable.

Putting the question in this way, however, suggests the counter-arrangement, viz. that governments might not succeed in conveying such a signal. They might instead feel relief at not having to bear the political burden of visibly initiating a realignment - and without a new, more hidden, discipline inherent in belonging to a Monetary Union of irrevocably fixed exchange rates. The collective body of central bankers might be faced with fait accompli situations where only a realignment would ease tensions, and with national policy-makers blaming either private speculators or the central bankers themselves for the outcome. This would imply a deterioration relative to the recent performance of the EMS.

On balance, these arguments suggest that the decisive considerations in assigning the authority to undertake realignments are how

close participants have come to meeting the prerequisites for Monetary Union. It would be dangerous, if feasible, to shift that authority to the central banking system at a time of remaining major divergence of performance, partiularly with respect to the sustainability of external imbalance. It would be desirable to shift it, if the need for realignments was generally accepted as residual and the monetary instruments for a European central banking system to underpin fixed rates had been made available along the lines proposed above. A tentative conclusion would be that within the time perspective of the reforms here suggested the authority to decide on realignments could become part of the mandate of a European central bank; but it should not be one of the first tasks.

DECENTRALIZATION OF OPERATIONS ?

On the basis of the discussion in the previous section of the general mandate for a European central bank and of the policy instruments available to it the question arises as to the degree of institution-building required. There are essentially three conceivable models for the system, but the two extremes seem unlikely to meet the requirements.

A fully decentralized system in which there is no operational capacity at the centre, and all execution of policy is left to the individual national central banks, is intuitively appealing. The central banks have most of the experience required, including extensive cooperation in the EMS. There are no technical reasons why policy implementation could not be delegated to them, each of them undertaking interventions or other operations concerning their own curency. Changes in central bank interest rates or in reserve requirements would in any case have to be administered through the central banks. Responsibility for interventions in third currencies could be delegated to the major reserve currency or financial centre within the system, i.e. to the Bundesbank. Such a practice would have the virtue of building on existing foundations. Other specific aspects of European central banking functions could be assigned to other individual banks with particular expertise in an area. Some tasks might rotate among participants with the chairmanship in the Committee of Governors, as is the practice in other contexts in the EC. Why create a new and potentially rival structure ?

The decentralized model apperars too loose to be operational. It

could create conflicts of interest for the individual central bank to undertake operations on both its own account and in a European role in the same market. It would be very difficult for the new institution to develop any distinct profile. Finally, and most important, there will be a need for some continuing authority at the centre of the system to be responsible for preserving a view of the common interest and to interpret the policy guidelines adopted by the governing body. Since an important part of the instruments are designed to correct relativities between participating countries, their use is likely to be politically sensitive and to be more safely vested outside a national or bilateral framework.

The opposite extreme of a centralized model is more obviously unsuitable, though it might fit late stages of monetary integration when a common currency is well advanced. Indeed, a recent report[2)] sees as a distinguishing criterion for allocating instruments to the centre that they are conducted in the parallel, ultimately common, currency. That criterion is neat, but too restrictive when the role of a parallel or common currency is not yet outlined. If there is to be a centre with an operational capacity to conduct foreign-exchange and other interventions to make its presence felt, it has to have enough to do to win professionel respect from central banks and the market. Some central banks may have started with too few instruments and too little influence at the centre. This seems to have been the case for the Federal Reserve Board for the first two decades after the adoption of the Federal Reserve Act of 1913; apart from analytical and secretarial functions for a new Board, its tasks were to coordinate discount rate changes proposed by the regional banks and to modify reserve requirements. This was hardly enough to assure a minimal authority vis à vis the 12 regional Federal Reserve Banks who did most of operational tasks, in particular open market operations. Lack of first-hand contact with financial markets was, until at least the restructuring of the Fed in the 1930's, a handicap for the Board.

An intermediate Federal structure in which the operational tasks are divided between a centre and the participating central banks recommends itself. Centralization can be kept to a minimum, but it can not be avoided as a matter of principle. A shared work experience at the centre for central bankers who are used to cooperating only over the telephone or by attending meetings could prove valuable.

COMPOSITION OF GOVERNING BODIES

Could a centre with an operational capacity, run by a small staff appointed on their professional merit, act only on the instructions emerging from the monthly meeting of the Committee of Central Bank Governors as the sole governing body ? Like the fully decentralized model one could not exclude its feasibility, but it would leave major tasks for the national central bank governors who would continue to have the full-time responsibility for running their own banks, while taking on the tasks of monitoring the operations of the new centre and explaining the actions to governments, the European political authorities and the public. It may be preferable, as has been the case in large Federal banking systems, to have some European-appointed members of the governing body, along with the governors of the participating central banks. Such a structure was put in place in the US by the Federal Reserve Act of 1913 and by the establishment in the FRG in 1948 of Bank Deutscher Länder, and nine years later its successor, Deutsche Bundesbank. In both institutions the ambition was to have a bank centralized enough to be eficient, but open to influence through regionally appointed officials (Reserve Bank Presidents, respectively Landeszentralbankpräsidenten). The influence of the nationally/ centrally appointed officials was then allowed to grow with time.

In analogy with the US experience one would try to define the relative competences of a Board, nominated at the European level, possibly by the European Council itself, and with long terms of office, say eight years, and the Committee of Central Bank Governors composed as today. The Board would be placed at the seat of the centre; it would prepare the monthly meetings with the Committee of Governors and represent the new institution vis à vis the European political authorities and in international monetary discussions, notably at G7/5 meetings. It would oversee the operations at the centre and have responsibility for one or two policy instruments, as was the case initially with the Federal Reserve Board.

The main policy-making body would be the combination of members of the Board and of the Governors' Committee. Two specific, but not dissimilar, solutions have been proposed in recent publications[3]. They envisage the nomination by the European Council (or Council of Ministers) of 6-7 members for the Board and 5-6 governors of national central banks serving on a rotating basis, again on the model of the

Federal Reserve. In the latter's (since 1935) central policy-making body, the Federal Open Market Committee, the seven Presidentially-appointed members of the Board serve with five of the Reserve Bank Presidents. The President of the New York Fed has a permanent seat while the remaining four seats rotate among the remaining eleven Presidents, with some allowance for the relative size of their district. All twelve Presidents, however, participate actively in the meeting every 6-8 weeks. A literal translation of these provisions could imply, if all present EC-members were to participate, that the President of the Bundesbank had a permanent vote, the Governors of the four next largest central banks a vote every other year and the governors of the six smaller central banks a vote every third year. The procedure may appear undesirably discriminatory, even when it is recognized that all governors will be present at the meetings. It is an alternative to the introduction of weighted voting according to the procedures followed in the Council of Ministres (and proposed by Mr. Pöhl). Some form of recognition to the difference in size of countries will have to be made, once the new institution has genuine decision-making powers. The present proposal has the advantage that it would permit the participation of European-nominated members of the Board along with the national central bank governors in one collegiate body, a situation difficult to reconcile with weighted voting as practised in purely intergovernmental cooperation.

The balance between European-appointed and national members of the Open Market Committee would have to be carefully considered. In the proposals referred to, the European-appointed members would hold a slight majority of the votes. This may be more appropriate to the later stages of operation than initially. The Bundesbank Council presents a different model; there the eleven Presidents of the Land central banks outnumber the seven members of the Direktorium. This regional majority was even stronger in the governing body of Bank Deutscher Länder which preceded the Bundesbank; in that period (1948-57) there were only two Federally-appointed members of the Direktorium. A similar gradual shift in the relative size of the two components in the governing body might be envisaged for the European central banking system in an initial phase.

AUTONOMY AND ACCOUNTABILITY

The preceding sections have discussed what monetary policy deci-

sions need to be taken jointly, the division of responsibility for implementation between European and national levels and the composition of the governing bodies of European central banking system. The position of such a system within the EC framework has to be clarified.

Achievement of an advanced stage of monetary integration through major legal and institutional steps prior to full political unification, and before joint authority over an important part of budgetary powers has been established, would be an experience without historical precedent. In national states the formation of a central bank has followed, rather than led, political unification, also when de facto currency unification preceded the latter. Reversing the usual order will require careful specification of the interaction of a European central banking institution with the political authorities at the national and European levels.

This subject is usually raised by those who insist that an eventual central banking system should be given a degree of autonomy at least comparable to those national central banks which have the highest degree of autonomy within national policy-making; the status of the Bundesbank is often referred to. This perspective alone is incomplete; inevitably a European central banking system would, in the early part of its existence, have a higher degree of autonomy than existing national central banks which operate in continuous consultation with their respective governments, serving as financial agent and adviser to them and coordinating actions with the budgetary authorities. There will be no analogy to this close, almost symbiotic, relationship at the European level prior to, and for a time after, political unification. Various methods are conceivable for organizing a constructive dialogue between the new central banking system and the political authorities during a phase when monetary integration has a more visible profile than joint policies in other areas:

(1) The Board could be asked to report at regular intervals, say every six months, to the ECOFIN Council on the implementation of past policies and the formulation of objectives for the coming period. Reports would be similar in nature to those submitted by the Chairman of the Board of Governors of the Federal Reserve System to the competent Committees in the US Congress. The Board would also in such sessions, at the request of the Council or on its own initiative, give its view on the feasibility of taking additional steps in monetary integration. This is an extension of present practice in which the

Council at more irregular intervals receives reports from the Committee of Central Bank Governors and the EC Monetary Committee.

(2) The Monetary Committee would monitor the actions of the new institution and inject views of national Treasuries and of the EC Commission. The Committee would prepare sessions of the ECOFIN Concil at which reports from the new institution are presented.

(3) Following practice in the FRG, leading policy-makers outside the monetary area could be given a right to be present at the monthly meetings of the Open Market Committee without the right to vote. This would apply to the acting President of the ECOFIN Council and to the President of the EC Commission, personally or through a Deputy. Conversely, the Chairman of the Board could be invited to take part in all meetings of the ECOFIN Council at which monetary subjects are under discussion.

(4) The Board would be asked to report to the European Parliament through its Monetary Affairs Committee every six months. This would provide an occasion for public debate.

These mechanisms for consultations could ensure that the new institution is obliged to explain its formulation and implementation of monetary policy without subjecting it to major restrictions of its autonomy. The Council would have no powers to issue directives to the new institution or to dismiss members of its governing body, but political and public criticism of it would have a natural focus. The presence of national central bank governors in the Open Market Committee would provide input of the respective national opinions into the decisions of the new institution, making unlikely the risk of remoteness from and unresponsiveness to national and Community policies in the non-monetary area.

The above discussion has assumed that the new system wil be part of a familiar EC framework. Within that the modifications of form relative to present practice are not dramatic. In substance, the role of the new system would develop not so much at the expense of than as a complement to those of existing bodies in the EC system. The main impact would be at the national level where political influence over monetary policy would be visibly reduced. For the EC Commission the

evolution of a central banking system, assumed to take collective decisions and prepare common positions would also imply competition as to who was speaking to represent an EC monetary viewpoint, and some redirection of effort as parts of the analytical and secretarial functions, presently spread between the EC Commission (General Directorates for Economic and Financial Affairs and for Financial Services, II and XV), the Secretariat of the Council of Ministers (for the EC Monetary Committee) and the Bank for International Settlements (as agent for the Committee of Central Bank Governors and the Board of EMCF), could be merged into the new system.

If a new central banking system were to come into existence without being part of an EC framework, having the participation of only part of the EC membership, the suggestions (1) to (3) above, though not necessarily (4), could be left inoperative, or replicated within the smaller group of EC-countries which cooperate fully. It would hardly be acceptable, at a time when, say eight or nine member states are participating in the new system and have begun to take genuinely joint decisions, that an acting President of the Council from one of the other EC-members take part in the system's policy meetings. Relations with those member states would inevitably become more bilateral. Their view would need to be sought more jointly only at the time when the fully participating states were considering, by a unanimous vote, to extend the scope of the system by taking an additional step within the package made possible according to a revised Treaty. Before taking steps that would move them further ahead of those who have felt constrained to a slower path towards EMU, consultations among all member states who have accepted that final objective are essential.

A TIMETABLE

Some elements in the package of reforms which would jointly establish a European central banking system have more urgency than others. Assuming the stategy is to seek approvel for the whole package, does the likely time sequence of challenges to European monetary integration suggest an order of priority for activating the individual elements ?

At least four challenges and corresponding stages of activation may be identified:

(1) Management of relations with third currencies. Resumption of

the decline of the dollar could soon (1989 ?) reraise the issue of a more joint, less improvised, response than in 1987. Some reserve pooling is an early priority.

(2) As - or if - several EC-countries remove remaining capital controls on short-term transactions fully by mid-1990 that would provide a natural target date for giving an embryonic central banking system (or reserve fund) visible authority to manage relative interest rates to avoid interest-rate escalation and conflicts in short-term monetary management. Hence power to intervene in national money markets and to assure that relative interest-rate changes do underpin the exchange rate could become a high priority by 1990.

(3) Coinciding with the implementation of most of the Internal Market programme by 1992-93 a move to underline the growing emphasis on exchange-rate fixity would be appropriate. If central rates can not at that time be irrevocably fixed - and that maybe regarded by some as unlikely - the date would provide an occasion for transferring the authority to make narrowly circumscribed central-rate changes to the central banking system. At the same time, and depending on the degree of fixity of exchange rates, moves to encourage a parallel currency and to give it legal tender status in the participating countries could be made.

(4) By approximately that same time the new central bank should have had sufficient time to develop joint policies and to monitor effectively money creation in the participating countries to change from the present implicit working of the EMS to an explicit emphasis on a joint monetary target to reach a joint nominal objective, and to conduct its policy increasingly in terms of a common currency.

FOOTNOTES

1) In terms of Governor Hoffmeyer´s summary table this would imply moving the particular instruments from presently national decision-making, subject possibly to mutual ex-ante information or ex-port consultation, to prior coordination or outright collective decision-making (the two columns at the right of the table).

2) Comité pour l´Union Monétaire de l´ Europe, Un Programme Pour l´Action (Rapport Giscard-Schmidt), Paris 1988, pp. 24 ss.

3) "Rapport Giscard-Schmidt", pp. 19 ss. and D. Gros and Niels Thygesen, The EMS: Achievements, Current Issues and Directions for the Future, CEPS Paper No. 35, Centre for European Policy Studies, Bruxelles, 1988.