ON THE ORIGINS OF THE FRANCO-GERMAN EMU CONTROVERSIES

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1. INTRODUCTION

EMU implied a fundamental change in the economic constitution of the European Union. It was, to a large extent, a culmination of a process of Franco-German reconciliation and understanding. However, in the post-war period, there were significant differences in ideas and economic policy-making in Germany and France. These led to recurring debates between French and German policy-makers, which still continue today, although to a much lesser degree.

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

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

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

Moreover, it is important to keep in mind that crucial stimuli for European monetary integration originated from Franco-German political initiatives at the highest level: at the Hague Summit with Brandt and Pompidou, the European Monetary System by Giscard and Schmidt, and the Maastricht treaty process with Kohl and Mitterand.

EMU was naturally a collective, multilateral, achievement, in which all the countries of the European Union played a role. However, the dominating role of France and Germany in the EMU process, and the, initially, fundamental differences in thought and economic policy-making, warrant an analysis of the Franco-German EMU debates and their origins.

The paper starts with a presentation of the main lines of thought and economic policy-making in France and Germany. Thereafter, the focus is on three important stages in the development of the European Union: the Rome Treaties, the Werner Report and the Maastricht treaty.

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1 For an analysis of the Belgian and Italian contributions, see Maes and Quaglia, 2002.
2. MAIN LINES OF THOUGHT AND ECONOMIC POLICY-MAKING IN GERMANY AND FRANCE

In the post-war period, there were some significant differences in economic ideas among policymakers in Germany and France. These were based on fundamental characteristics of their history and society. This paper focuses on three levels, which are strongly interrelated: (1) meta-cultural beliefs, (2) views on economic policy-making, and (3) views on European integration.

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

France is one of the oldest nation-states in Europe. As remarked by Rosanvallon (1992, 64), the "State" preceded the nation in France, and gave France a coherence and an identity. The Revolution of 1789 abolished the monarchy and reduced the role of religion, placing "Reason" at the center of French society. This further reinforced the role of the state. It gave birth to "la tradition républicaine", focused on the "one and indivisible" republic, a view which would permeate France. Fundamental to the republican state was the primacy attached to the sovereign nation as the source of legitimacy. The task of the state was to ensure the unity of public power in the service of the nation.

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

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2 So is the French civil law system rather designed to be an instrument of power of the state. This contrasts with the Anglo-Saxon civil law system where the protection of the citizens against the government is at the core.

3 It went together with a French emphasis on institutions. This was also very typical of Monnet's approach to European integration: "Rien n'est possible sans les hommes, rien n'est durable sans les institutions" (Monnet, 1976, 412).

4 In an article of 1992, Christian Noyer, then at the French Treasury, wrote about central bank independance as "l'exception au principe démocratique" (Noyer, 1992, 17).
There was further a long tradition of state intervention in economic life in France, famous with Colbertism and the establishment of the “manufactures royales”. This came to the foreground in the powerful role of the Finance Ministry, the role of the state in industrial policy (like already in Colbertism) and the importance of planning in the post-war period.

In France “Le Plan” and the Planning Office would play an important role in the post-war reconstruction. In essence, the plan was a strategy around a medium-term framework, which provided an orientation to the economic actors, in order to reduce uncertainty. It aimed at creating coherence, introducing "un élément souhaitable de rationalité" (Marjolin, 1963, 18), a key concept of the Republican tradition. Important was further the sectoral approach, which aimed at identifying sectors where bottlenecks would occur, which could then be eliminated. The Plan was so at the heart of the French industrial strategy. French programmation was also "voluntarist" (Massé, 1963, 45). It aimed both at a somewhat higher expansion than would be realised by the spontaneous working of market forces, and at correcting certain imbalances of the market mechanism.

Planning was in line with the engineering tradition in economic thought in France. This tradition was especially strong among the graduates of the “Grandes Ecoles”, civil servants and top managers (Schmidt, 2000, 129). Moreover, there was a relatively strong influence of Keynesian economics at the French Planning Office. A special example was Robert Marjolin, the Deputy Commissioner of the Plan and one of France’s first prominent Keynesians (Arena and Schmidt, 1999)\textsuperscript{5}. However, the Plan had much less influence at the powerful Finance Ministry, which had a more pragmatic attitude.

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

\textsuperscript{5} In the post-war period left-wing ideas, partly Marxian inspired, were quite influential in France.
of policies at different moments of time. However, in French macroeconomic and monetary thought and policy, the exchange rate had a central place\(^6\).

Chart 1 - Exchange rate of the French franc against the German mark (number of FF for 1 DM)

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

\(^6\) Which contrasts with the German focus on domestic price stability.
Traditionally, this line was more supported by liberal, free market oriented economists. This "orthodox" line was, generally, also the more pro-European line. The control of inflation in the 1960s made it possible for France to participate in the creation of the common market\(^7\). The European Monetary System was created during the Barre prime ministership. European motives were crucial for Mitterrand to stay in the EMS. Generally speaking, the European constraint was influential in pushing through more orthodox economic policies, while a strong franc (with sound fundamentals) was important to be a strong and solid partner in the European debate\(^8\).

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

### 2.2 Germany: a federalist approach with a division of power\(^9\)

In Germany, the nation-state had not such deep roots. Moreover, Nazism and the Second World War marked a fundamental break with the past. Nazism showed the dangers of a centralisation of power. This centralisation was also evident in the economic field. National socialism had, step by step, introduced a centrally administered economy. The central bank became known as the "specialised printing office" of the government.

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

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\(^7\) During the Rome treaty negotiations, the French negotiators were very concerned about France's competitiveness and insisted on safeguard clauses. However, for de Gaulle, the European Community and the competition which it entailed, was important to push for the modernisation of France's economy.

\(^8\) During the 1960s, currency issues were mainly international monetary issues. For De Gaulle a strong French franc was very much a symbol of a strong France.

\(^9\) The word "federalism" is here used in a "continental" sense (especially application of the subsidiarity principle) and not a "British" one (transferring power to Europe).
Decentralisation not only applied to the political organisation of the country, such as the federal structure of the state. It was also a basic principle of the organisation of economic policy. So was the central bank responsible for monetary policy, but not for banking supervision. The market economy itself is a decentralised structure, which goes easily along with Germany's federal state.

Germany's economic system in the postwar period can best be characterised as a "social market economy", combining the principle of freedom in the market with that of social balance. In contrast to "laissez-faire" capitalism, the concept of the social market economy requires above all a clear legal and political regulatory framework, or "Ordnungsrahmen" (Tietmeyer, 1999, 6). Ordo-liberal economists emphasise the interdependence between the economic order and all other forms of order (i.e. legal, social and political).

During the war, "ordo-liberal" ideas were developed by a number of economists known as the Freiburg School under the leadership of Walter Eucken. In its emphasis on historical and institutional aspects of economic problems, the ordo-liberal approach drew to a significant extent on the ideas and approach of the historical school (Hutchison, 1979, 435). They became very influential in the post-war period. Ludwig Erhard, the first Economics minister, and an economics professor himself, was very much influenced by them. Ordo-liberal ideas inspired the economic reforms of June 1948, which restored the market economy.

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

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11 However, there were also more direct American influences, especially for the currency reform of June 1948, of which Gerhard Colm, a social democrat who emigrated from Nazi Germany in 1933, was the main architect.
According to the advocates of the social market economy, a strong state is necessary, but one with limited functions. The fundamental task of the state is "rule-setting": to set the rules for economic processes, monitor compliance with them, and punish infringements. The aim of these rules is to set a framework that permits the highest possible degree of freedom and ensures lasting maintenance of effective competition. Important elements are clearly defined property rights and an active competition policy.

A constitutive element of the social market economy is monetary stability (Tietmeyer, 1999, 138). Monetary stability is important for economic reasons, as inflation damages the steering function of the price mechanism and creates uncertainty, which hurts investment. It is also important for social reasons, as inflation causes a redistribution of income, to the disadvantage of the weaker groups who cannot protect themselves. Memories of this were still vivid in Germany, with the hyperinflation of the 1920s. The task of ensuring monetary stability became the responsibility of the, independent, Bundesbank. However, there is also an affinity with the German "federalist" approach of preferring decentralised and compartmentalised structures (Tietmeyer, 1999, 165.)

The more Keynesian tendency in Germany, with Karl Schiller as an important representative, put more emphasis on active government policies. Schiller's ideal of economic policy was to combine the market economy (the "Freiburg imperative") with active macroeconomic policies (the "Keynesian message"). This tendency was influential at the end of the 1960s and the early 1970s, when the social democrats participated in the government, with Willy Brandt as their leader and with Schiller as economics minister.

The federalist German philosophy went along with a positive view towards European integration and the transfer of sovereignty to supranational European institutions. Moreover, policy was dominated by the belief that European security and Franco-German reconciliation were the most vital of all interests for Germany.

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12 During the discussions on the Bundesbank law of 1957, Erhard supported the independence of the Bundesbank, while Adenauer was more reserved (Marsh, 1992, 167). See also Bibow, 2002.
3. THE CREATION OF THE COMMUNITIES

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

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

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

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

France was living through the Fourth Republic, characterised by mostly short-lived coalition governments, political instability and a vulnerable economy. The French government was divided on the issue of European integration. However, the prime minister, Guy Mollet, and the minister for foreign affairs, Christian Pineau, were in favour. An important reason was that, in their opinion, European integration could preserve France's political leadership. Among French pro-European policy-makers, Monnet was very influential. He lobbyed for a further push towards European integration along sectoral lines, focusing on transport and energy (Monnet, 1976). However, it was clearly in France that resistance against new initiatives at European integration was the strongest. This was both for political reasons (the aversion against supranational institutions, especially, but not only, among the Gaullists) and for economic reasons (fear, both from businessmen and trade unionists, for German competition, which could endanger France's industry and the "acquis social").

During the negotiations, the French government was in first instance concerned about the Euratom treaty. France also favoured a greater role for the State in economic life and proposed the idea of planning on a European scale (Marjolin, 1986, 287). Moreover, the French government was very concerned that France was not in a position to engage in competition on equal terms. It was therefore in favour of harmonisation of legislation which affected the competitive position, especially social legislation. The French argued further that agriculture had to be included in the common market and that France had extra costs, due to her responsibilities in her overseas territories.

Looking then at the Rome Treaties from an economic thought and constitutional perspective, the European Atomic Energy Community, bears a heavier French imprint, with its sectoral approach, while the European Economic Community, with the abolition of barriers which hindered the free movement of goods, services, labour and capital in the common market and strong emphasis on
competition policy, has a stronger German sounding\textsuperscript{13}. The chapter on competition policy was very comprehensive. The French obtained the setting-up of the common agricultural policy and the association of the overseas territories. The social dimension was rather limited, as Germany was concerned that it could hinder the functioning of the market economy.

\textsuperscript{13} Free movement of capital was more limited, under French pressure. For an analysis of the Rome treaty, see also Streit & Mussler, 1998.
4. **EMU APPEARS ON THE SCENE**

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

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

French interest in European monetary integration should be situated in the discussions about the international monetary system. De Gaulle had always been critical of the central position of the American dollar in the Bretton-Woods system. During the second half of the 1960s, French officials, in order to attain a more equilibrated international monetary system, developed ideas about a "European monetary identity" (Haberer, 1981). A key element was a type of exchange rate mechanism, to keep European currencies closer together\(^\text{14}\).

At the end of the 1960s, doubts about the future of the fixed exchange rate system became widespread, especially with the devaluation of the French franc in 1969 and the vulnerable position of the American dollar. The countries of the Community feared that further exchange rate instability would lead to the disintegration of the customs union and the demise of the common agricultural policy. Moreover, new political leaders had come to power. In 1969 de Gaulle resigned and Pompidou was elected in France. He and his finance minister, Giscard d'Estaing, were more pro-European. In Germany, a new government was formed by the Social Democrats and the Free Democrats with Willy Brandt as chancellor, a pragmatic but convinced pro-European. The Brandt government proposed the EMU project. Foreign policy motives were crucial. Germany wanted to demonstrate its European credentials, also as a way to counterbalance its new Ostpolitik (recognition of the German Democratic Republic). As with the common market project, the technical experts, were more cautious\(^\text{15}\).

\(^{14}\) This contrasted with German analyses of the Bretton-Woods system, which focused on the threat that intervention obligations posed for price stability (Emminger, 1977, 53).

\(^{15}\) This would be a constant element in the history of European monetary integration. The different initiatives came from the heads of state, and “got a tough reception among the experts” (Hoffmeyer, 2000, 14).
At the Hague Summit of December 1969, the Heads of State and Government agreed on economic and monetary union as an objective of the European Community. The Werner Committee produced a report for the establishment of EMU by 1980 (Council-Commission of the European Communities, 1970, commonly known as the Werner Report).

The Werner Report first presented a general picture of economic and monetary union. EMU implied that "the principal decisions of economic policy will be taken at Community level and therefore that the necessary powers will be transferred from the national plane to the Community plane" (Werner Report, 26). The Report proposed that two new Community institutions should be created: a centre of decision-making for economic policy and a Community system for the central banks. However, the Report did not elaborate very much on the institutional structure of EMU and did not distinguish clearly between a single currency and a system of irrevocably fixed exchange rates (Baer and Padoa-Schioppa, 1988, 54). An important reason herefore were Franco-German divergencies on the conception of economic policy and of European integration. So could Clappier, the French member of the Committee, not accept anything on the institutional level. However, in practice, he proved to be rather independent-minded (Dyson and Featherstone, 1999, 107).

The Report proposed to attain EMU in three stages. However, it did not lay down a precise timetable for the different stages. Rather it wanted to maintain a measure of flexibility, while concentrating on the first phase. There were heated discussions about the priorities on the path to EMU. It would lead to the classic description of the debate between the "monetarists" and the "economists". The "economists", led by Germany, emphasised policy co-ordination, while the "monetarists", with France, argued for priority for the narrowing of exchange rate fluctuations (Werner, 1991). The compromise solution was that there had to be "parallel progress" in both areas.

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

Chart 2 - Inflation in France and Germany

![Chart showing inflation in France and Germany](image)

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

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

At the end of the 1970s, European monetary integration came again on the agenda with the creation of the European Monetary System. The EMS was a less ambitious project than the earlier attempt at monetary union. The conclusions of the Bremen Council (July 1978) did not mention economic and monetary union but a "scheme for the creation of closer monetary co-operation leading to a zone of monetary stability in Europe".

The original Giscard-Schmidt plan foresaw a rather symmetrical system, one of the fundamental French aims. It comprised, amongst other things, the partial pooling of official reserves and an expanded use of the ECU, both as a means of settlement between central banks and, in due course, as a new reserve asset (Ludlow, 1982, 82). The Bundesbank manoeuvred to avoid a system with unlimited intervention obligations, which threatened its monetary policy autonomy. It managed to ensure the imposition of limits on credit facilities in the EMS and also the repayment of credits in hard currencies and not only in ECUs\textsuperscript{16}.

The first years of the EMS were difficult, characterised by several realignments, a lack of convergence and a weak co-ordination of economic policy. Moreover, in May 1981, François Mitterrand became the first socialist president of the Fifth Republic in France. He started with a strong activist economic program, including an expansionary budgetary policy and nationalisations. This reinforced policy divergencies between France and Germany. The ensuing loss of competitiveness of the French economy, and capital outflows, repeatedly put strong pressure on the French franc, leading to currency crises.

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

\textsuperscript{16} German dominance of the ERM was an important topic of academic research. The results hereof were somewhat less equivocal. So argue Gros and Thygesen (1998, 177) that Germany had a strong influence on the other countries, but there was also a weak influence the other way around. See also Fratianni and von Hagen (1992).
convictions. It implied that, in order to avoid further devaluations, he had to pursue a more orthodox economic policy, the "polilique de rigueur".

4.3 A growing consensus on stability oriented policies

The oil shock of 1973, and the ensuing stagflation, were of fundamental importance to induce changes in the conceptions of French economic policy-makers. They showed very clearly the openness of the French economy and the vulnerability to external developments (Patat, 1992, 8).

The oil shock was a, more or less fatal, blow to the French planning experience. French policy-makers became more and more aware that there were limits to activist policies, and that France had to take into account the external constraint.

During the second half of the 1970s, under the prime ministership of Raymond Barre, French economic policies became more stability-oriented. The exchange rate was a crucial element in the strategy to instill discipline on the French economy. Barre also pushed through measures to liberalise prices. This reorientation of French economic policy was an important element why German policy-makers consented to the creation of the EMS. The EMS can then be considered as a case of "parallel progress", towards exchange rate stability and stability-oriented policies, as requested in the Werner Report. In this respect then can Mitterrand's initial economic policies be regarded as a last gasp of the traditional French interventionist policies, running against the external constraint.

These changes in economic policy conceptions were supported by new economic theories. The "Monetarist counter-revolution" had questioned the Keynesian framework. It led to thrilling debates, initially mainly in the academic world. In a first stage, discussions centred on the determination of nominal demand, monetarists emphasising the money supply and not budgetary policy, as the main determinant of effective demand. In a second stage, the attention shifted

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17 See Saunier (2002) for an analysis of the early years of the Mitterrand presidency, based on the Archives of the Presidency. Mitterrand clearly asked for the alternative scenario, with the imposition of tariffs, to be investigated.

18 So changed the Mauroy government the wage-setting procedures, including the abolishment of automatic wage indexation.
towards the functioning of the labour market, with the monetarists attacking the Phillips curve (Friedman, 1968). With the rational expectations hypothesis, the possibilities of policy-makers to steer the economy were even more strongly questioned, as the behaviour of economic agents may change in response to a change in policy regime (Lucas, 1976). The literature on time-inconsistency pointed further to the inflationary bias of a discretionary monetary policy (Barro and Gordon, 1983). To retain flexibility, while dealing with the inflationary bias of a discretionary policy, central bank independence quickly topped the research agenda (Fischer, 1994). Moreover, empirical studies indicated that central bank independence went together with a better inflation performance (Grilli, Masciandaro and Tabellini, 1991). Central bank independence became so not only a key theme of German ordo-liberalism, but also an important element of mainstream Anglo-Saxon economics.

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

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

Multilateral fora, like the European Union, the OECD, the BIS, and the IMF, greatly contributed to the dissemination of these new ideas on stability oriented policies. Senior French and German officials would meet often, not only bilaterally, but also in these international fora. This contributed to a growing consensus, also among French economic policy-makers, on "sound money" policies.

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19 With the Thatcher government, privatisations started in Europe. In France, when Mitterrand came to power, he implemented a large scale nationalisation programme. Privatisations began in France during the first "cohabitation", with Balladur as finance minister.

20 For an overview of the evolution of ideas at the European Commission, see Maes, 1998.
An important illustration is Jacques de Larosière, the Governor of the Banque de France from 1987 to 1993, who, previously, had been Managing Director of the IMF.

The emergence of this consensus on stability-oriented policies took also the heat out of the old "monetarist" - "economist" debate about the sequencing of the monetary integration process: whether priority should be given to exchange rate stability or policy coordination. Parallel progress, as requested in the Werner Report, became natural. Policy-makers in both Germany and France followed stability-oriented policies\textsuperscript{21}. For French policy-makers the exchange rate, the "franc fort", became an important anchor for their economic policies.

\textsuperscript{21} During most of the 1990s, inflation was even higher in Germany than in France (see graph 2), something which was naturally also related to German unification.
5. THE MAASTRICHT TREATY PROCESS

5.1 The relaunching of the monetary union project

While French policy-makers where convinced of the importance of stability-oriented policies, they remained unhappy with the German dominance in the EMS. During Franco-German negotiations, Jacques Attali even called the German mark the "force de frappe allemande".

French policymakers developed then, more or less simultaneously, different strategies to cope with the asymmetry in the EMS: (1) adapting the rules of the ERM. This culminated in the Basle-Nyborg agreement of September 1987, which, however, left power relations in the ERM basically unchanged; (2) bilateral Franco-German initiatives. In the fall of 1987 a plan was launched to elevate the Franco-German Economic Council to ministerial level, with also the central bank presidents participating. However, under Bundesbank insistence, it remained a consultative organ; (3) EMU. After the débâcle of his initial socialist policies, Mitterrand gradually turned to European integration as the key theme of his presidency. In this context, senior French policy-makers, especially pro-European socialists, started manoeuvring towards EMU. Delors, already in early 1985, as part of the internal market program, pushed for the liberalisation of capital movements, a crucial German condition for EMU. The Fabius government accepted this. Delors, in November 1985, supported by France and Belgium, also obtained a, limited, chapter on EMU in the Single European Act.

In early 1988, debates about Europe's monetary future accelerated. In a memorandum of January 1988, the French Finance Minister, Edouard Balladur, argued that the exchange rate mechanism still had some important defects, notably its asymmetry. Although, the Balladur Memorandum focused on adapting the way in which the EMS functioned, it also argued that it was

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22 To the great surprise of senior French Commission officials, for whom this was a complete change of direction. Delors was certainly aware of the implications. One of his close confidants, Padoa-Schioppa, was the father of the "inconsistent quartet".
necessary to reflect on further institutional steps in the monetary construction of Europe. At the end, it also raised the issue of the creation of a single currency (Balladur, 1988, 20).

Balladur’s Memorandum found a perceptive ear in Germany, not at the Bundesbank or the Finance Ministry, but at the Foreign Ministry. Several factors converged in making economic and monetary union a key theme for Genscher (Smets, Maes and Michielsen, 2000, 67): (1) it fitted in perfectly with Genscher’s pro-European convictions. Genscher wanted to strengthen the process of European integration, which he considered as still fragile after the Euro-sclerosis of the first half of the 1980s. Moreover, he sensed that, with Gorbachev, things were changing in the East; (2) it was a popular theme among the business community in Germany, a natural constituency of Genscher’s liberal democratic party; (3) Genscher was also influenced by French complaints about the German dominance of the EMS. As such, Genscher was confronted with the issue of the “political sustainability” of the EMS: could the stance of monetary policy be determined by one country in a Community where, in principle, decisions are taken together. In February 1988, Genscher, in his personal capacity, published a Memorandum wherein he argued strongly for a European Monetary Union and a European Central Bank (Schönfelder & Thiel, 1996, 29).

At that time, early in 1988, Helmut Kohl was still quite open to the issue of monetary union. On the one hand, he was sensitive to the arguments of Stoltenberg that EMU was only possible if a sufficient degree of convergence was achieved (coronation theory). On the other hand, he was also sensitive to the arguments of the advocates of EMU, like Genscher, but also Mitterrand, for whom he had a high esteem and who often complained about the asymmetry of the EMS. Moreover, Kohl gradually realised that EMU was unavoidable if he wanted to realise his vision of a "United States of Europe", a recurrent theme in his speeches at that time. Of crucial importance was the Franco-German bilateral summit at Evian, early in June 1988, when Kohl and Mitterrand decided to push ahead with EMU.

Further progress was made at the Hanover Summit. The European Council confirmed the objective of economic and monetary union and decided to entrust to a Committee the task of studying and proposing "concrete stages leading towards this union", a very shrewd limitation of
the mandate of the Committee, as it was not asked to analyse whether EMU was desirable or not. The Committee was chaired by Jacques Delors, who had the confidence of Kohl and Mitterrand, and, as a former finance minister, the technical expertise. The governors of the central banks - in a personal capacity - were also on the Committee. Delors wanted them to be members, both because of their expertise and because this would bind them to the monetary union project. In a first reaction, Karl-Otto Pöhl, the president of the Bundesbank, even considered refusing to serve on the Committee.

5.2 The Delors Report

The Delors Report (Committee for the Study of Economic and Monetary Union, 1989, hereafter referred to as the Delors Report) would assume a crucial role as a reference and anchor point in further discussions, just as the Werner Report nearly two decades earlier. The Delors Report basically revolved around two issues: first, which economic arrangements are necessary for a monetary union to be successful? Second, which gradual path should be designed to reach economic and monetary union?

Initially, the relation between Delors and Pöhl in the Committee was rather tense. However, the crucial aim of Delors was to get a unanimous Report. So he took a low profile and focused on seeking out a consensus in the Committee. Pöhl took a "fundamentalist" position and emphasised the new monetary order which had to be created: "Above all agreement must exist that stability of the value of money is the indispensable prerequisite for the achievement of other goals. Particular importance will therefore attach to the principles on which a European monetary order should be based" (Pöhl, 1988, 132). He argued for price stability as the prime objective of monetary policy, which had to be conducted by an independent central bank. Pöhl further emphasised the "indivisibility of monetary policy", that decisions should be taken either at the national level or by a common central bank.

The fundamentalist approach would be deeply influential in the Delors Report and inspire a number of principles that would also figure prominently in the Maastricht treaty (Padoa-Schioppa, 1994, 9).
The Delors Committee took great care to work out first its view on the final stage of EMU. This was a major and very fundamental contrast with the Werner Committee, which was deeply divided on this issue. The Delors Report proposed, at the institutional level, the creation of an independent "European System of Central Banks", to be responsible for the single monetary policy, with price stability as the ultimate aim. In the discussions on the independence of the central bank, Pöhl received valuable support from de Larosière, for whom the Delors Committee presented an opportunity to increase the independence of the Banque de France (Dyson and Featherstone, 2000, 345).

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

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

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23 In order to cover himself politically, de Larosière had a meeting with Mitterrand, in which Mitterrand did not object to central bank independence.
5.3 The Maastricht Treaty

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

The Franco-German debates on EMU centered on two issues: the transition towards "Stage Three" of EMU and the constitutional structure of EMU. As for the start of Stage Three, two dates are mentioned in the Treaty: 1997 if a majority of countries fulfilled the criteria and 1999 as an ultimate date. In order to participate, the Member States had to fulfil certain conditions, especially central bank independence and the achievement of a high degree of sustainable convergence. Of special importance in these assessments were four "convergence" criteria:

- **Price stability.** The Member State should have an inflation rate no more than 1.5 p.c. above the average of the three EC countries with the lowest inflation rates.

- **Sustainability of public finance.** National budget deficits must be less than 3 p.c. of GDP. The public debt ratio must not exceed 60 p.c. of GDP, or be declining at a sufficient rate.

- **Currency stability.** A national currency must not have been devalued in the previous two years and must have remained within the normal fluctuations margins of the exchange-rate mechanism.

- **Interest rates.** Long-term interest rates should be within two percentage points of the average of the three countries with the lowest inflation rates.

These conditions for the start of monetary union, namely a fixed date and the satisfaction of the convergence criteria, were naturally the outcome of a debate. The monetarists, especially France and Italy, insisted on a fixed date to ensure the start of monetary union, while the economists, in particular Germany, insisted on economic criteria so that only countries which were "fit" could
participate in the monetary union. The combination of the convergence criteria with a fixed date proved to be a very powerful stimulus for the convergence process.

There were also major Franco-German debates on the constitutional structure of EMU. Economic and monetary union became asymmetrical. Monetary policy was centralised. It was the responsibility of the independent European System of Central Banks, with price stability as its primary objective. This part of the treaty went quite smoothly through the intergovernmental conference. The preparations in the Delors Committee, the Committee of Governors and the Monetary Committee certainly contributed to this. The prominence of the German institutional model was also evident. Several factors contributed to this: the sheer size of Germany and the Deutsche mark; strong theoretical support, based on a blend of German ordo-liberal and mainstream Anglo-Saxon ideas; the successful history of German monetary policy; the strong bargaining position of the German authorities and the unique federal structure of the Bundesbank. However, with the anchoring of price stability and central bank independence in a treaty, it went further than the German situation, giving these principles a constitutional status, "a pre-eminence unparalleled in legal history" (Herdegen, 1998, 14). The responsibility for other instruments of economic policy, like budgetary policy and structural policies, remained basically with the national authorities, subject to a coordination process. The different conceptions of monetary union and economic union reflected the limits of the willingness of the member states to give up national sovereignty.

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

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24 As Bordo and Jonung (2000, 35) observe, EMU is quite unique in history, being a monetary union while countries retain political independence.
has to function\textsuperscript{25}. Agreement was only reached after intense negotiations, including secret bilateral discussions between the French and the Germans.

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

\textsuperscript{25} Senior German policy-makers admit that there was a kind of contradiction in the German negotiation position, with Germany being against a "gouvernement économique" but in favour of restraints on national budgetary policies. Waigel's political problems in Bavaria were mentioned as an explanatory factor.
6. CONCLUSION

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

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

There were regular recurrences of these Franco-German debates. In the beginning the Franco-German debates went to the core of economic policy-making. They concerned the basic mechanisms of economic coordination: planning or the market. Gradually, however, planning, fell into demise. Important factors hereby were the stagflation of the 1970s and the growing openness of the economies. Also, activist Keynesian policies lost support, due to the failure of demand management policies, both at the international level, like the coordinated expansion of 1978, and at the national level, like the Mitterrand experiment in France in the early 1980s. Gradually, a consensus developed on "sound money" policies: stability oriented, medium-term, economic policies. Moreover, with this consensus, "parallel progress" towards exchange rate stability and policy coordination, as requested in the Werner Report, became natural. It took the heat out of the traditional "monetarist" - "economist" debate on the sequence of events leading to monetary unification.
One can discern some interesting parallels between the negotiations for the Rome Treaties and the Maastricht treaty. The parallels were probably strongest on the German side. In both cases the main technical actor, the Economics Ministry in the 1950s and the Bundesbank in the 1980s and 1990s, was cautious about the move towards European integration. However, in both cases the Chancellor overrode the objections of the "technicians", because of foreign policy motives, whereby the desire to further the process of European integration and to strengthen the Franco-German relationship were important elements.

While the German Chancellor in both cases decided to push for European integration, he left his negotiators a large room of manoeuvre as regards the kind of European economic constitution to be created. So took Pöhl a "fundamentalist" approach in the discussions in the Delors Committee. He argued for price stability as the prime objective of monetary policy, which had to be conducted by an independent central bank. This view would permeate the Delors Report and the Maastricht treaty, just as the creation and functioning of a competitive market permeated the Rome treaty.

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

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