THE EUROPEAN COUNCIL

BRUSSELS
4-5 DECEMBER 1978

Documents in the dossier include:

Conclusions
Session of the European Council
Reproduced from *The European Council*
Dossier of the Group of the European People's Party
Luxembourg 1990

The European Council in Brussels—Outcome and follow-up
Reproduced from the Bulletin of the European Communities, No. 12/1978

European Council Agrees to Establish Monetary System
European Community News No. 32/1978
European Community Information Service
Washington DC

Economic Policy: European Monetary System
Mr. James Callaghan, Prime Minister, in the House of Commons on December 6, 1878
British Information Service
New York NY

Session of the European Council

Brussels, 4 and 5 December 1978

Conclusions

The European Council agreed, on the basis of the preparatory work of the Council (Economics and Finance Ministers) and of the Monetary Committee and the Committee of the Governors of the Central Banks to set up a European Monetary System as from 1 January 1979. This agreement is enclosed as an Annex.

The purpose of the European Monetary System is to establish a greater measure of monetary stability in the Community. It should be seen as a fundamental component of a more comprehensive strategy aimed at lasting growth with stability, a progressive return to full employment, the harmonization of living standards and the lessening of regional disparities in the Community. The Monetary System will facilitate the convergence of economic development and give fresh impetus to the process of European Union. The Council expects the European Monetary System to have a stabilizing effect on international economic and monetary relations. It will therefore certainly be in the interests of the industrial and the developing countries alike.

- A -

The European Monetary System

1. Introduction

1.1 In Bremen we discussed a 'scheme for the creation of closer monetary cooperation leading to a zone of monetary stability in Europe'. We regarded such a zone 'as a highly desirable objective' and envisaged 'a durable and effective scheme'.

1.2 Today, after careful examination of the preparatory work done by the Council and other Community bodies, we are agreed as follows:

A European Monetary System (EMS) will be set up on 1 January 1979.

1.3 We are firmly resolved to ensure the lasting success of the EMS by policies conducive to greater stability at home and abroad for both deficit and surplus countries.

1.4 The following chapters deal primarily with the initial phase of the EMS.

We remain firmly resolved to consolidate, not later than two years after the start of the scheme, into a final system the provisions and procedures thus created. This system will entail the creation of the European Monetary Fund as announced in the conclusions of the European Council meeting at Bremen on 6 and 7 July 1918, as well as the full utilization of the ECU as a reserve asset and a means of settlement. It will be based on adequate legislation at the Community as well as the national level.

2. The ECU and its functions

2.1 A European Currency Unit (ECU) will be at the centre of the EMS. The value and the composition of the ECU will be identical with the value of the EUA at the outset of the system.

2.2 The ECU will be used:

(a) as the denominator (numéraire) for the exchange rate mechanism;

(b) as the basis for a divergence indicator;

(c) as the denominator for operations in both the intervention and the credit mechanism;

(d) as a means of settlement between monetary authorities of the EC.

2.3 The weights of currencies in the ECU will be reexamined and if necessary revised within six months of the entry into force of the system and thereafter every five years or, on request, if the weight of any currency has changed by 25%.

Revisions have to be mutually accepted; they will, by themselves, not modify the external value of the ECU. They will be made in line with underlying economic criteria.

3. The exchange rate and the intervention mechanism

3.1 Each currency will have an ECU-related central rate. These central rates will be used to establish a grid of bilateral exchange rates.

Around these exchange rates fluctuation margins of 2,25% will be established. EC countries with presently floating currencies may opt for wider margins up to 6% at the outset of EMS; these margins should be gradually reduced as soon as economic conditions permit to do so.

A Member State which does not participate in the exchange rate mechanism at the outset may participate at a later date.

3.2 Adjustments of central rates will be subject to mutual agreement by a common procedure which will comprise all countries participating in the exchange rate mechanism and the Commission. There will be reciprocal consultation in the Community framework about important decisions concerning exchange rate policy between countries participating and any country not participating in the system.

3.3 In principle, interventions will be made in participating currencies.

3.4 Intervention in participating currencies is compulsory when the intervention points defined by the fluctuation margins are reached.

3.5 An ECU basket formula will be used as an indicator to detect divergences between Community currencies. A 'threshold of divergence' will be fixed at 75% of the maximum spread of divergence for each currency. It will be calculated in such a way as to eliminate the influence of weight on the probability to reach the threshold.

3.6 When a currency crosses its 'threshold of divergence', this results in a presumption that the authorities concerned will correct this situation by adequate measures, namely:

(a) diversified intervention;

(b) measures of domestic monetary policy;

(c) changes in central rates;

(d) other measures of economic policy.

In case such measures, on account of special circumstances, are not taken, the reasons for this shall be given to the other authorities, especially in the 'concertation between central banks'.

Consultations will, if necessary, then take place in the appropriate Community bodies, including the Council of Ministers.

After six months these provisions shall be reviewed in the light of experience. At that date the questions regarding imbalances accumulated by divergent creditor or debtor countries will be studied as well.

3.7 A very short-term facility of an unlimited amount will be established. Settlements will be made 45 days after the end of the month of intervention with the possibility of prolongation for another three months for amounts limited to the size of debtor quotas in the short-term monetary support.

3.8 To serve as a means of settlement, an initial supply of ECUs will be provided by FECOM against the deposit of 20% of gold and 20% of dollar reserves currently held by central banks.

This operation will take the form of specified, revolving swap arrangements. By periodical review and by an appropriate procedure it will be ensured that each central bank will maintain a deposit of at least 20% of these reserves with FECOM. A Member State not participating in the exchange rate mechanism may participate in this initial operation on the basis described above.

4. The credit mechanisms

4.1 The existing credit mechanisms with their present rules of application will be maintained for the initial phase of the EMS. They will be consolidated into a single fund in the final phase of the EMS.

4.2 The credit mechanisms will be extended to an amount of 25 000 million ECU of effectively available credit. The distribution of this amount will be as follows:

- Short-term monetary support = 14 000 million ECU
- Medium-term financial assistance = 11 000 million ECU

4.3 The duration of the short-term monetary support will be extended for another three months on the same conditions as the first extension.

4.4 The increase of the medium-term financial assistance will be completed by 30 June 1979. In the meantime, countries which still need national legislation are expected to make their extended medium-term quotas available by an interim financing agreement of the central banks concerned.

5. Third countries and international organizations

5.1 The durability of EMS and its international implications require coordination of exchange rate policies vis-à-vis third countries and, as far as possible, a concertation with the monetary authorities of those countries.

5.2 European countries with particularly close economic and financial ties with the European Communities may participate in the exchange rate and intervention mechanism.

Participation will be based upon agreements between central banks; these agreements will be communicated to the Council and the Commission of the EC.

5.3 EMS is and will remain fully compatible with the relevant Articles of the IMF Agreement.

6. Further procedure

6.1 To implement the decisions taken under chapter A, the European Council requests the Council to consider and to take a decision on 18 December 1978 on the following proposals of the Commission:

(a) Council Regulation modifying the unit of account used by the European Fund of Monetary Cooperation, which introduces the ECU in the operations of the EMCF and defines its composition;

(b) Council Regulation permitting the EMCF to receive monetary reserves and to issue ECUs to the monetary authorities of the Member States which may use them as a means of settlement;

(c) Council Regulation on the impact of the European Monetary System on the common agricultural policy. The European Council considers that the introduction of the EMS should not of itself result in any change in the situation obtaining prior to 1 January 1979 regarding the expression in national currencies of agricultural prices, monetary compensatory amounts and all other amounts fixed for the purposes of the common agricultural policy.

The European Council stresses the importance of henceforth avoiding the creation of permanent MCAs and progressively reducing present MCAs in order to re-establish the unity of prices of the common agricultural policy, giving also due consideration to price policy.

6.2 It requests the Commission to submit in good time a proposal to amend the Council Decision of 22 March 1971 on the introduction of a mechanism for the medium-term financial support to enable the Council of Economics and Finance Ministers to take a decision on such proposal at their session of 18 December 1978.

6.3 It requests the central banks of Member States to modify their Agreement of 10 April 1972 on the reduction of margins of fluctuation between the currencies of Member States in accordance with the rules set forth above (see paragraph 3).

6.4 It requests the central banks of Member States to modify as follows the rules on short-term monetary support by 1 January 1979 at the latest:

(a) The total of debtor quotas available for drawings by the central banks of Member States shall be increased to an aggregate amount of 7,9 billion ECU.

(b) The total of creditor quotas made available by the central banks of Member States for financing the debtor quotas shall be increased to an aggregate amount of 15,8 billion ECU.

(c) The total of the additional creditor amount as well as the total of the additional debtor amount may not exceed 8,8 billion ECU.

(d) The duration of credit under the extended short-term monetary support may be prolonged twice for a period of three months.

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Measures designed to strengthen the economies of the less prosperous Member States of the European Monetary System:

1. We stress that, within the context of a broadly-based strategy aimed at improving the prospects of economic development and based on symmetrical rights and obligations of all participants, the most important concern should be to enhance the convergence of economic policies towards greater stability. We request the Council (Economic and Finance Ministers) to strengthen its procedures for coordination in order to improve that convergence.

2. We are aware that the convergence of economic policies and of economic performance will not be easy to achieve. Therefore, steps must be taken to strengthen the economic potential of the less prosperous countries of the Community. This is primarily the responsibility of the Member States concerned. Community measures can and should serve a supporting role.

3. The European Council agrees that in the context of the European Monetary System, the following measures in favour of the less prosperous Member States ef-

fectively and fully participating in the exchange rate and intervention mechanisms will be taken:

3.1 The European Council requests the Community institutions by the utilization of the new financial instrument and the European Investment Bank to make available for a period of 5 years loans of up to 1 000 million EUA per year to these countries on special conditions.

3.2 The European Council requests the Commission to submit a proposal to provide interest rate subsidies of 3% for these loans, with the following elements:

The total cost of this measure, divided into annual tranches of 200 million EUA each over a period of five years shall not exceed 1 000 million EUA.

3.3 Any less prosperous Member State which subsequently effectively and fully participates in the mechanisms would have the right of access to this facility within the financial limits mentioned above. Member States not participating effectively and fully in the mechanisms will not contribute to the financing of the scheme.

3.4 The funds thus provided are to be concentrated on the financing of selected infrastructure projects and programmes, with the understanding that any direct or indirect distortion of the competitive position of specific industries within Member States will have to be avoided.

3.5 The European Council requests the Council (Economics and Finance Ministers) to take a decision on the abovementioned proposals in time so that the relevant measures can become effective on 1 April 1979 at the latest. There should be a review at the end of the initial phase of the EMS.

4. The European Council requests the Commission to study the relationship between greater convergence in economic performance of the Member States and the utilization of Community instruments, in particular the Funds which aim at reducing structural imbalances. The results of these studies will be discussed at the next European Council.

Economic and social situation

The European Council has reviewed the economic and social situation in the Member States of the Community. It notes with satisfaction that since its meeting in Bremen the conditions for strengthening the process of economic growth in Europe have improved.

The Heads of State and Government have reported on the measures they have introduced. The European Council deems it imperative, particularly in view of the disturbing employment situation, to ensure the further rapid implementation of these measures. It reaffirms its view that only a common coordinated approach by all Member States can lead to greater convergence of economic development in the European Communities. The efforts of all Member States to reduce inflation must therefore be intensified in order to ensure the durability of the European Monetary System.

The European Council asked the Commission to provide for its second meeting in 1979 a study of structural development prospects until 1990. This study should assess the consequences of structural changes for the economic and social situation in the Community.

The European Council welcomed the decision of the Labour and Social Affairs Council to extend the Social Fund to assist recruitment and job creation schemes for young people. In view of its continuing concern about youth unemployment the European Council asked the Labour and Social Affairs Ministers to keep the working of the new aid under review.

Tripartite Conference

The European Council has noted the results of the last tripartite Conference and calls upon the Governments of the Member States to take them into consideration in their economic and social policy decision-making.

The European Council holds the view that the dialogue between the social partners, the Governments of the Member States and the Commission of the European Communities promotes mutual understanding for economic and social policy exigencies and is therefore important for overcoming the problems of growth, stability and employment. The European Council therefore expresses the hope that the contacts between the social partners at European level will be continued.

The President of the European Council has informed the Council that the European Trade Union Confederation is elaborating proposals with a view to improving the methods of work of the tripartite Conference. The Council (Ministers of Economic Affairs and Finance and Ministers of Labour and Social Affairs) is requested to examine these proposals so that further action can be agreed with the social partners.

Terms of reference for the 'Committee of Wise Men'

In accordance with the proposal made by the President of the French Republic, the European Council agreed at its meeting in Brussels on 4 and 5 December to call upon a number of eminent persons with special knowledge of European affairs to give thought to such affairs.

The members of the Committee will be: Mr Barend Biesheuvel, Mr Edmund Dell and Mr Robert Marjolin.

The European Council invited the Committee to consider the adjustments to the machinery and procedures of the institutions which are required for the proper operation of the Communities on the basis of and in compliance with the Treaties, including their institutional arrangements, and for progress towards European Union. It emphasized the interest it attaches to having available specific proposals in this connection which may be implemented swiftly and which take into account experience to date and the prospective enlargement to Twelve.

The European Council requested the Committee to report back on its conclusions when the Council meets in October 1979.

Report on European Union

At the same meeting the European Council noted the reports by the Foreign Ministers and by the Commission on progress achieved in the past year towards European Union. The European Council confirmed the importance of the first direct elections to the European Parliament scheduled for 7 to 10 June 1979 and reaffirmed its determination to proceed further along the road to an ever closer union among the peoples of Europe. This, too, was the purpose of its decisions with regard to the European Monetary System and the setting up of a Committee of Wise Men.

The European Council reaffirmed the usefulness of reports on European Union and decided that, as in 1977, they would be published in an appropriate form.

1. European Monetary System

The European Council in Brussels — Outcome and follow-up

1.1.1 By the end of the year of European Council in Brussels had settled the details of a European Monetary System intended to create a zone of monetary stability in Europe. But this decision, which developed from Commission initiatives of recent years and from the European Council meeting in Bremen last July, immediately ran into difficulties.

The entry into force of the EMS, at first with only six countries, later eight (Italy and Ireland having finally agreed to join), foundered at the end of December over the adoption of the implementing regulations, following a reservation entered by France pending agreement on how monetary compensatory amounts were to be treated within the common agricultural policy. The European Monetary System (EMS) did not therefore start operating on 1 January 1979 as planned.

From the European Council in Bremen to the setbacks in December

1.1.2. Following informal preliminary talks on 6 and 7 July last the Bremen European Council discussed a scheme put forward by several delegations aimed at—to quote the Presidency's statement—'the creation of closer monetary cooperation (European Monetary System) leading to a zone of monetary stability in Europe'.[1]

1.1.3. Five months later, the European Council in Brussels on 4 and 5 December took a further step in this direction by formally adopting a Resolution 'on the establishment of the European Monetary System (EMS) and related matters'.[2] Three Members States however adopted a 'wait and see' attitude—'time for reflection' in the case of Ireland and Italy, and a more definite reservation in the case of the United Kingdom—before committing themselves to full participation in the system.

The next day the Commission confirmed that the EMS had been set up as a Community instrument, and that it would be fully involved in operating the new scheme. The Commission expressed a keen desire to see Ireland and Italy becoming members, and also hoped that the United Kingdom would join as soon as possible. Close contact was maintained with all three countries and a series of implementing measures were drafted in preparation for the Council meeting on Economic and Financial Affairs scheduled for 18 December in Brussels.

1.1.4. The auspices were favourable for the Council's discussions, since both Italy (on 12 December) and Ireland (on 15 December) had by then decided to join the EMS. These decisions were formally announced at the Council meeting. The United Kingdom Delegation stated that it was ready to play its part in all aspects of the EMS and that it would follow Community policies on exchange rates in a spirit of sympathetic cooperation, so as to be able to modify its position should the fears of the British Government prove unfounded.

The Council proceeded to discuss a number of matters relating to the introduction and operation of the European Monetary System. It reached a decision in principle on two Regulations: the first would introduce the ECU in the operations of the European Monetary Cooperation Fund (EMCF) with effect from 1 January; the second would permit the

[1] Bull. EC 6-1978, point 1.5.2.
[2] Point 1.1.11.

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EMCF to receive monetary reserves from the Member States and to issue ECUs in exchange for these reserves.

However the Council was unable to adopt these Regulations formally at the end of the meeting, since the French Delegation had entered a provisional reservation pending the outcome of the Agriculture Ministers' discussions on the impact of the EMS on the common agricultural policy (the problem of monetary compensatory amounts).

1.1.5. The final setback occurred on 29 December when an official communiqué was released in Paris stating that the French Government considered that the necessary conditions for introducing the EMS had not been met in full and would therefore maintain its reservation, until the Council had found a solution for both problems—the EMS and the monetary compensatory amounts.

For this reason it was not possible to launch the EMS on 1 January 1979 as originally planned.

The creation of the European Monetary System

The idea of a European monetary system

1.1.6. The idea of a European monetary system is not new. An initial attempt to organize European monetary relations was made as early as 1970 following the Summit in The Hague in December 1969, at which a decision had been taken in favour of the establishment by stages of economic and monetary union. With this aim in mind, various measures were agreed in 1971 and 1972. In the monetary field, a system of joint floating was set up that subsequently underwent a number of changes in form and membership. In the end, this system (the 'snake') embraced only a reduced number of countries (Federal Republic of Germany, Netherlands, Belgium, Luxembourg, Denmark).

The EMS is being created for reasons of both international monetary policy and Community economic policy. Prominent among these is the need to tackle exchange rate instability, with its unmistakable adverse impact on both the fight against inflation and growth. A greater measure of exchange rate stability, notably within the EEC, would be an important factor in any policy to overcome the present crisis since it would have a favourable effect on the production and investment decisions of firms whose views were increasingly influenced by the unforeseeable nature of exchange rate relationships.

The EMS: mechanisms and operation

1.1.7. The EMS was designed to be established with eight Member States as full members, viz. the countries belonging to the 'snake' plus France, Italy and Ireland, the United Kingdom having decided to delay joining the system.

The EMS is based on a new European monetary unit, the ECU, the composition of which—to be reviewed periodically— will be identical at the outset with that of the European unit of account (EUA), namely: DM 0.828 + UKL 0.0885 + FF 1.15 + LIT 109.0 + HFL 0.286 + BFR 3.66 + LFR 0.140 + DKR 0.217 + IRL 0.00759.

This new instrument, the pillar of the system, will be used as: a denominator (*numéraire*) in the exchange rate mechanism; a basis for establishing a divergence indicator; a denominator for transactions under the intervention and credit mechanisms; a means of settlement between monetary authorities in the European Community.

As part of the EMS, it is planned to set up various mechanisms governing intervention, credit and settlement operations.

Intervention mechanism — Like the snake, the new system is to feature an intervention mechanism which is based on a parity grid (adjustable by joint agreement)

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and which permits a maximum margin of fluctuation at any one time of 2.25%; when this margin is reached, there will be automatic intervention with no limit as to amount, normally in the currencies of the participating countries. Wider margins (6%) have been envisaged for Member States whose currencies are at present floating independently and who might opt for such margins, Italy being a case in point. In addition, a 'divergence indicator' based on the ECU would be introduced. The purpose of the indicator will be to identify any currency that reaches a threshold equal to 75% of its maximum margin of fluctuation against the ECU. Once this treshold has been crossed, there is a presumption that the authorities responsible for the currency in question will take steps to alleviate or indeed eliminate the strain within the system and, where possible, to present the emergence of a situation in which the maximum margin of fluctuation is reached, thereby making intervention compulsory. These steps might take the form of diversified intervention, monetary policy measures or, where appropriate, changes in central rates or any other economic policy measures.

Credit mechanism — Existing intra-Community credit mechanisms would be strengthened in order to provide the EMS with sufficient financial means. The period for which very short-term monetary support is available will be extended from 30 to 45 days after the end of the month of intervention, and the total amount of short-term and medium-term credits will be increased substantially. At present, the amount 'effectively available' under the two mechanisms is about 10 000 million ECU. The Resolution of the European Council provided for it to be increased to 25 000 million ECU. The periods for repayment of short-term credits would also be extended.

Settlement — As soon as the EMS is launched, ECU will be created against the deposit, in the form of resolving swap arrangements, of 20% of the gold and dollar reserves held by the Central Banks. They will be used for settling transactions carried out under the system. A European Monetary Fund embracing the new arrangements and the existing institutions will be set up by 1 January 1981 at the latest, according to the terms of the Resolution of the European Council in December.

1.1.8. The EMS, which is to replace the existing 'Community exchange rate scheme' (the snake), would involve a number of important innovations. For instance the divergence indicator should make for improved symmetry between participants' rights and obligations; and the scale and duration of credits would enable participants to withstand speculative pressure and to cope with temporary balance of payments difficulties. Measures are envisaged to strengthen the economies of the less prosperous member countries participating in the EMS with a view to achieving closer convergence between the different Member States in the Community. The key role played by the ECU and the establishment of an initial fund bear witness to the Community nature of the undertaking. Lastly, the EMS shows a balanced mix between the elements of flexibility (wider margins, changes in central rates, credits) and rigidity (defence of margins, policy coordination) in addition to consistency between the strictly monetary aspects and the economic aspects of the system.

Documents and statements

1.1.9. Following several months of preparatory discussions it was the European Council, meeting in Brussels on 4 and 5 December, which gave the go-ahead to the European Monetary System. The 'conclusions of the Presidency' give the decision and stress its political significance, while the 'Resolution' adopted by the European Council describes the mechanisms of the new system.

Conclusions of the Presidency

1.1.10. The 'Conclusions of the Presidency' released at the end of the meeting of the European Council included the following passage on the EMS:

'The European Council agreed, on the basis of the preparatory work of the Council (Economics and Finance Ministers) and of the Monetary Committee and the Committee of the Governors of the Central Banks to set up a European Monetary System as from 1 January 1979. This agreement is enclosed as an Annex.

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employment, the harmonization of living standards and the lessening of regional disparities in the Community. The Monetary System will facilitate the convergence of economic development and give fresh impetus to the process of European Union. The Council expects the European Monetary System to have a stabilizing effect on international economic and monetary relations. It will therefore certainly be in the interests of the industrial and the developing countries alike.'

Text of the Resolution

1.1.11. The text adopted by the European Council on 5 December is set out below:

'Resolution of the European Council of 5 December 1978

on the establishment of the European Monetary System (EMS) and related matters

A

The European Monetary System

1. **Introduction**

1.1 In Bremen we discussed a "scheme for the creation of closer monetary cooperation leading to a zone of monetary stability in Europe". We regarded such a zone "as a highly desirable objective" and envisaged "a durable and effective scheme".

1.2 Today, after careful examination of the preparatory work done by the Council and other Community bodies, we are agreed as follows:

A European Monetary System (EMS) will be set up on 1 January 1979

1.3 We are firmly resolved to ensure the lasting success of the EMS by policies conducive to greater stability at home and abroad for both deficit and surplus countries.

1.4 The following chapters deal primarily with the initial phase of the EMS.

We remain firmly resolved to consolidate, not later than two years after the start of the scheme, into a final system the provisions and procedures thus created. This system will entail the creation of the European Monetary Fund as announced in the conclusions of the European Council meeting at Bremen on 6 and 7 July 1978, as well as the full utilization of the ECU as a reserve asset and a means of settlement. It will be based on adequate legislation at the Community as well as the national level.

2. **The ECU and its functions**

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gradually reduced as soon as economic conditions permit to do so.

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The European Council stresses the importance of henceforth avoiding the creation of permanent MCAs and progressively reducing present MCAs in order to re-establish the unity of prices of the common agricultural policy, giving also due consideration to price policy.

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— to modify their Agreement of 10 April 1972 on the reduction of margins of fluctuation between the currencies of Member States in accordance with the rules set forth above (see paragraph 3).

6.4 It requests the Central Banks of Member States to modify as follows the rules on short-term monetary support by 1 January 1979 at the latest:

(a) The total of debtor quotas available for drawings by the Central Banks of Member States shall be increased to an aggregate amount of 7.9 billion ECU.

(b) The total of creditor quotas made available by the Central Banks of Member States for financing the debtor quotas shall be increased to an aggregate amount of 15.8 billion ECU.

(c) The total of the additional creditor amount as well as the total of the additional debtor amount may not exceed 8.8 billion ECU.

(d) The duration of credit under the extended Short-Term Monetary Support may be prolonged *twice* for a period of 3 months.

B

Measures designed to strengthen the economies of the less prosperous Member States of the European Monetary System

1. We stress that, within the context of a broadly-based strategy aimed at improving the prospects of economic development and based on symmetrical rights and obligations of all participants, the most important concern should be to enhance the convergence of economic policies towards greater stability. We request the Council (Economic and Finance Ministers) to strengthen its procedures for coordination in order to improve that convergence.

European Monetary System

2. We are aware that the convergence of economic policies and of economic performance will not be easy to achieve. Therefore, steps must be taken to strengthen the economic potential of the less prosperous countries of the Community. This is primarily the responsibility of the Member States concerned. Community measures can and should serve a supporting role.

3. The European Council agrees that in the context of the European Monetary System, the following measures in favour of the less prosperous Member States effectively and fully participating in the Exchange Rate and Intervention Mechanisms will be taken.

3.1 The European Council requests the Community institutions by the utilization of the new financial instrument and the European Investment Bank to make available for a period of 5 years loans of up to 1 000 million EUA per year to these countries on special conditions.

3.2 The European Council requests the Commission to submit a proposal to provide interest rate subsidies of 3% for these loans, with the following elements:

The total cost of this measure, divided into annual tranches of 200 million EUA each over a period of 5 years shall not exceed 1 000 million EUA.

3.3 Any less prosperous member country which subsequently effectively and fully participates in the mechanisms would have the right of access to this facility within the financial limits mentioned above. Member States not participating effectively and fully in the mechanisms will not contribute to the financing of the scheme.

3.4 The funds thus provided are to be concentrated on the financing of selected infrastructure projects and programmes, with the understanding that any direct or indirect distortion of the competitive position of specific industries within Member States will have to be avoided.

3.5 The European Council requests the Council (Economics and Finance Ministers) to take a decision on the abovementioned proposals in time so that the relevant measures can become effective on 1 April 1979 at the latest. There should be a review at the end of the initial phase of the EMS.

4. The European Council requests the Commission to study the relationship between greater convergence in economic performance of the Member States and the utilization of Community instruments, in particular the funds which aim at reducing structural imbalances. The results of these studies will be discussed at the next European Council.'

Statements by Heads of State or Government and by the President of the Commission

1.1.12. After the meeting of the European Council on 4 and 5 December, a number of Heads of State or Government—Mr Valéry Giscard d'Estaing, President of the French Republic, Mr Helmut Schmidt, Chancellor of the Federal Republic of Germany, and the British Prime Minister, Mr James Callaghan—and Mr Roy Jenkins, President of the Commission, commented on the results obtained with regard to the establishment of a European Monetary System. They analysed the mechanisms of the new system and emphasized its importance for the future of the building of Europe.

President Giscard d'Estaing recalled that the idea of the EMS sprang from a Franco-German initiative which had taken shape at the European Councils in Copenhagen and Bremen. He stressed that the system was not simply a continuation or revival of the European 'snake', since it provided for measures and machinery covering a much wider field. The French President also emphasized the importance of a progressive return to a system of uniform pricing on agricultural markets, since the divergencies which existed at present were anomalous.

Chancellor Helmut Schmidt felt that the EMS would bring considerable benefits to all Community Members by paving the way for European unity and by stimulating economic growth, thus helping to reduce unemployment and also ensuring greater monetary stability. He felt none the less that the system might have been taken further and that the current achievements should be seen as a limited success.

The British Prime Minister, Mr James Callaghan, took the view that the EMS should serve as a prelude to a new move towards greater stability of exchange rates with the dollar and perhaps other currencies. Mr Callaghan spoke not in terms of failure, but referred to a temporary set-back for Europe, and dwelt at length on the difficulties and cost of the common agricultural policy.

Mr Roy Jenkins, President of the Commission, echoed Mr Schmidt's view that the European Council was a limited success. But he stressed that although the EMS could not be regarded as a truly Community enterprise without the participation of all nine Members, it was still a great achievement that it had been started on a Community basis and that the Commission had been able to play its part.

On the same theme, the joint communiqué released in Washington at the end of the talks held on 14 December between President Carter and Mr Roy Jenkins indicated that 'President Carter viewed the European Monetary System (EMS) as an important step towards the European integration that the United States had long supported'. The President of the Commission stated that the creation of such a system was designed not only to establish a zone of monetary stability in Europe but also to contribute to greater stability in the world monetary system as a whole, of which a strong dollar was an essential part. He underlined that the EMS was entirely compatible with the relevant articles of the International Monetary Fund, to which Europe gives its wholehearted confidence and support.

European Community NEWS

No. 32/1978

December 8, 1978

EUROPEAN COUNCIL AGREES TO ESTABLISH EUROPEAN MONETARY SYSTEM

The European Council, the heads of state or government of the nine member states of the Euopean Community, agreed at their meeting in Brussels on December 4 and 5 to establish a European Monetary System (EMS) on January 1, 1979.

The new system will have as its center a European Currency Unit (ECU), and will incorporate a compulsory intervention mechanism to ensure greater stability of European exchange rates. The system will also continue and extend present credit mechanisms to strengthen the economic potential of the less prosperous countries of the Community.

EMS, according to the Council resolution, will be open to all European countries with particularly close economic and financial ties with the European Community. Because of its international implications, EMS will require coordination of exchange policies with third countries and concertation with their monetary authorities. The system will remain fully compatible with the International Monetary Fund; it is expected to lessen speculation among European currencies and thereby aid the U.S. dollar.

Plans for the EMS were put forward this year by German Chancellor Helmut Schmidt and French President Valery Giscard d'Estaing following a call last year by Commission President Roy Jenkins for renewed steps toward European monetary union.

A complete text of the Council resolution on EMS is reprinted below:

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A.

1.) Introduction -

In Bremen we discussed a "scheme for the creation of closer monetary cooperation leading to a zone of monetary stability in Europe." We regarded such a zone "as a highly desirable objective" and envisaged "a durable and effective scheme."

Today, after careful examination of the preparatory work done by the Council and other Community bodies, we are agreed as follows: A European Monetary System (EMS) will be set up on 1 January 1979.

We are firmly resolved to ensure the lasting success of the EMS by policies conducive to greater stability at home and abroad for both deficit and surplus countries.

The following chapters deal primarily with the initial phase of the EMS.

We remain firmly resolved to consolidate, not later than two years after the start of the scheme, into a final system the provisions and procedures thus created. This system will entail the creation of the European Monetary Fund as announced in the conclusions of the European Council meeting at Bremen on 6/7 July 1978, as well as the full utilization of the ECU as a reserve asset and a means of settlement. It will be based on adequate legislation at the Community as well as the national level.

2.) The ECU and its functions -

A European Currency Unit (ECU) will be at the center of the EMS; the value and the composition of the ECU will be identical with the value of the EUA* at the outset of the system.

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*The European Unit of Account (EUA) is a composite basket of fixed amounts of currencies of the nine Member States as follows:

0.028	German marks,
1.15	French francs,
0.0885	Pounds sterling,
109	Italian lira,
0.286	Dutch florins,
3.66	Belgian francs,
0.140	Luxembourg francs,
0.217	Danish crowns,
0.00759	Irish pounds.

The equivalent of the EUA in any currency is equal to the sum of the equivalents of these amounts in that currency.

The ECU will be used -

a.) As the denominator (numeraire) for the exchange rate mechanism
b.) As the basis for a divergence indicator
c.) As the denominator for operation in both the intervention and the credit mechanism
d.) As a means of settlement between monetary authorities of the EC.

The weights of currencies in the ECU will be reexamined and if necessary revised within six months of the entry into force of the system and thereafter every five years or, on request, if the weight of any currency has changed by 25 per cent.

Revisions have to be mutually accepted. They will, by themselves, not modify the external value of the ECU. They will be made in line with underlying economic criteria.

3.) The exchange rate and the intervention mechanism -

Each currency will have an ECU-related central rate. These central rates will be used to establish a grid of bilateral exchange rates.

Around these exchange rates fluctuation margins of 2.25 per cent will be established. EC countries with presently floating currencies may opt for wider margins up to 6 per cent at the outset of EMS. These margins should be gradually reduced as soon as economic conditions permit to do so.

Am member state which does not participate in the exchange rate mechanism at the outset may participate at a later date.

Adjustments of central rates will be subject to mutual agreement, a common procedure which will comprise all countries participating in the exchange rate mechanism and the Commission. There will be reciprocal consultation in the Community framework about important decisions concerning exchange rate policy between countries participating and any country not participating in the system.

In principle, interventions will be made in participating currencies. Intervention in participating currencies is compulsory when the intervention points defined by the fluctuation margins are reached.

An ECU basket formula will be used as an indicator to detect divergences between Community currencies. A "threshold of divergence" will be fixed at 75 per cent of the maximum spread of divergence for each currency. It will be calculated in such a way as to eliminate the influence of weight on the probability to reach the threshold.

When a currency crosses its "threshold of divergence," this results in a presumption that the authorities concerned will correct this situation by adequate measures, namely:
a.) Diversified intervention,
b.) Measures of domestic monetary policy,
c.) Changes in central rates,
d.) Other measures of economic policy.

In case such measures, on account of special circumstances, are not taken, the reasons for this shall be given to the other authorities, especially in the "concertation between central banks." Consultations will, if necessary, then take place in the appropriate Community bodies, including the Council of Ministers.

After six months these provisions shall be reviewed in the light of experience. At that date the questions regarding imbalances accumulated by divergent creditor or debtor countries will be studied as well.

A very short-term facility of an unlimited amount will be established. Settlements will be made 45 days after the end of the month of intervention with the possiblity of prolongation for another 3 months for amounts limited to the size of debtor quotas in the short-term monetary support.

To serve as a means of settlement, an initial supply of ECU will be provided by the European Monetary Cooperation Fund (EMCF) against the deposit of 20 per cent of gold and 20 per cent of dollar reserves currently held by central banks.

This operation will take the form of specified, revolving swap arrangements. By periodical review and by an appropriate procedure it will be ensured that each central bank will maintain a deposit of at least 20 per cent of these reserves with EMCF. A member state not participating in the exchange rate mechanism may participate in this initial operation on the basis described above.

4.) The credit mechanisms -

The existing credit mechanisms with their present rules of application will be maintained for the initial phase of the EMS. They will be consolidated into a single fund in the final phase of the EMS.

The credit mechanisms will be extended to an amount of 25 billion ECU of effectively available credit. The distribution of this amount will be as follows:

Short-term monetary support	14 billion ECU
Medium-term financial assistance	11 billion ECU

The duration of the short-term monetary support will be extended for another 3 months on the same conditions as the first extension.

The increase of the medium-term financial assistance will be completed by 30 June 1979. In the meantime, countries which still need national legislation are expected to make their extended medium-term quotas available by an interim financing agreement of the central banks concerned.

5.) Third countries and international organizations -

The durability of EMS and its international implications require coordination of exchange rate policies vis-a-vis third countries and, as far as possible, a concertation with the monetary authorities of those countries.

European countries with particularly close economic and financial ties with the European Communities may participate in the exchange rate and intervention mechanism.

Participation will be based upon agreements between central banks. These agreements will be communicated to the Council and the Commission of the EC.

EMS is and will remain fully compatible with the relevant articles of the International Monetary Fund agreement.

6.) Further procedure -

To implement the decision taken under (A), the European Council requests the Council to consider and to take a decision on 18 December 1978 on the following proposals of the Commission:

(A) Council regulation modifying the unit of account used by the European Monetary Cooperation Fund, which introduces the ECU in the operations of the European Monetary Cooperation Fund and defines its composition.

(B) Council regulation permitting the EMCF to receive monetary reserves and to issue ECUs to the monetary authorities of the member states which may use them as a means of settlement.

(C) Council regulation on the impact of the European Monetary System on the Common Agricultural Policy. The European Council considers that the introduction of the EMS should not of itself result in any change in the situation obtaining prior to 1 January 1979 regarding the expression in national currencies of agricultural prices, monetary compensatory amounts (MCAs) and all other amounts fixed for the purposes of the Common Agricultural Policy.

The European Council stresses the importance of henceforth avoiding the creation of permanent MCAs and progressively reducing present MCAs in order to reestablish the unity of prices of the Common Agricultural Policy, giving also due consideration to price policy.

It requests the Commission to submit in good time a proposal to amend the Council decision of 22 March 1971 on the introduction of a mechanism for the medium-term financial support to enable the Council of Economics and Finance Ministers to take a decision on such proposal at their session of 18 December 1978.

It requests the central banks of member states to modify their agreement of 10 April 1972 on the reduction of margins of fluctuation between the currencies of member states in accordance with the rules set forth above (see paragraph 3).

It requests the central banks of member states to modify as follows the rules on short-term monetary support by 1 January 1979 at the latest:

a.) The total of debtor quotas available for drawings by the central banks of member states shall be increased to an aggregate amount of 7.9 billion ECU.
b.) The total of creditor quotas made available by the central banks of member states for financing the debtor quotas shall be increased to an aggregate amount of 15.8 billion ECU.
c.) The total of the additional creditor amount as well as the total of the additional creditor amount may not exceed 8.8 billion ECU.
d.) The duration of credit under the extended short-term monetary support may be prolonged twice for a period of 3 months.

B. Measures designed to strengthen the economies of the less prosperous member states of the European Monetary System

We stress that, within the context of a broadly-based strategy aimed at improving the prospects of economic development and based on symmetrical rights and obligations of all participants, the most important concern should be to enhance the convergence of economic policies toward greater stability. We request the Council (Economic and Finance Ministers) to strengthen its procedures for coordination in order to improve that convergence.

We are aware that the convergence of economic policies and of steps must be taken to strengthen the economic potential of the less prosperous countries of the Community. This is primarily the responsibility of the member states concerned. Community measures can and should serve a supporting role.

The European Council agrees that, in the context of the European Monetary system, the following measures in favor of the less prosperous member states effectively and fully participating in the exchange rate and intervention mechanisms will be taken.

The European Council requests the Community institutions by the utilization of the new financial instrument and the European Investment Bank to make available for a period of 5 years loans of up to 1 billion EUA per year to these countries on special conditions.

The European Council requests the Commission to submit a proposal to provide interest-rate subsidies of 3 per cent for these loans, with the following elements: The total cost of this measure, divided into annual tranches fo 200 million EUA each over a period of 5 years shall not exceed 1 billion EUA.

Any less prosperous member country which subsequently effectively and fully participates in the mechanisms would have the right of access to this facility within the financial limits mentioned above. Member states not participating effectively and fully in the mechanisms will not contribute to the financing of the scheme.

The funds thus provided are to be concentrated on the financing of selected infrastructure projects and programs, with the understanding that any direct or indirect distortion of the competitive position of specific industries within member states will have to be avoided.

The European Council requests the Council (Economics and Finance Ministers) to take a decision on the above mentioned proposals in time so that the relevant measures can become effective on 1 April 1979 at the latest. There should be a review at the end of the initial phase of the EMS.

The European Council requests the Commission to study the relationship between greater convergence in economic performance of the member states and the utilization of Community instruments, in particular the funds which aim at reducing structural imbalances. The results of these studies will be discussed at the next European Council.

In remarks at a Tuesday press conference at the conclusion of the Council, President Jenkins termed the two-day meeting "a success in getting a European Monetary System worked out in detail, with a full measure of agreement." He acknowledged that the likelihood of immediate British participation had been small, and expressed his disappointment that Italy and Ireland had been unable to indicate their willingness to join at the Brussels meeting.

Belgium, Denmark, France, Germany, Luxembourg and the Netherlands announced at the Council that they would participate in the EMS from the January 1 starting date. Italy and Ireland are expected to reach a decision within one or two weeks.

Jenkins emphasized his belief that the EMS "should be a Community scheme" and he said it was important "to start on a basis of a Community scheme which makes the possibility of others joining easier." He affirmed that the Commission "will play its full part and will do its best to represent the common collective interest."

BRITISH INFORMATION SERVICES

POLICY AND REFERENCE DIVISION

December 6, 1978

POLICY STATEMENTS
(FULL TEXT)

48/78. ECONOMIC POLICY: EUROPEAN MONETARY SYSTEM

Mr. James Callaghan, Prime Minister, in the House of Commons on December 6, 1978:

Following his return from the meeting in Brussels on December 4 - 5 of the European Council to discuss the proposed European Monetary System and related matters, the Prime Minister, Mr. James Callaghan, reported to the House of Commons.

The text of his statement follows.

Topics Covered:

1. European Monetary System
2. Exchange rate mechanism
3. Community credit
4. Common Agricultural Policy
5. Emoluments to European Assembly Members

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European Monetary System

"With permission, Mr. Speaker, I will make a statement on the meeting of the European Council in Brussels which I attended with My Rt.Hon. Friend the Foreign and Commonwealth Secretary on December 4 and 5. The main topic of discussion was the European Monetary System and matters related to it. The Council agreed that a European Monetary System should be established on January 1, 1979. The five Community countries at present in the snake indicated that they would participate in all aspects of the system, and France decided to join them. At the conclusion of the discussions, the Prime Ministers of Italy and Ireland said that they would need more time for consultations before reaching a conclusion on their participation in the exchange rate mechanism. I explained to the Council that I would not be recommending to the Cabinet that the United Kingdom should participate in the exchange rate mechanism when it begins to function. I informed the other Heads of Government that we intend to work for a continuation of the exchange rate stability which sterling has enjoyed for nearly two years.

"I am arranging for the relevant document which was agreed to be published as a White Paper.

Exchange Rate Mechanism

"It was agreed that the United Kingdom would be free to join the exchange rate mechanism at a later date if we wish; or of course to remain outside it. We shall of course join in the development of the ECU* and of the European Monetary Fund. All Community currencies will be included in the ECU. We are free to choose whether or not we wish to deposit 20 per cent of our gold and dollar reserves with the European Monetary Cooperation Fund against issue to us of a corresponding value of ECUs. That is a matter the Chancellor of the Exchequer will consider shortly with the Bank of England. In taking a decision we shall take into account the possibility that intervention in Community currencies could be helpful to us in maintaining the stability of sterling.

/Community ...

* The proposed European Currency Unit, a new monetary unit based on the weighted average of the nine European Community currencies, and which will act as the "numeraire" of the European Monetary System.

Community Credit

"We shall participate in the enlarged Community credit which is linked to the establishment of the EMS. This will be without reservation in the increase in medium-term credit. As regards the short-term monetary support which is more closely linked to day-to-day exchange rate intervention, we have agreed not to call on the credit increase which is now being made, and our partners have agreed not to call on us. There is also provision for reciprocal consultation about important decisions concerning exchange rate policy between countries inside and outside the exchange rate mechanism.

"At the previous Council meeting in Bremen I called for studies in the context of EMS about measures to strengthen the economies of the less prosperous member countries. This part of our work was less thoroughly prepared than the work on the system itself. The proposals which eventually emerged provide for additional loan facilities of up to 1,000 million EUA* over five years for less prosperous countries participating in the exchange rate mechanism, with a three percent interest rate subsidy. There was a limitation on these loans that they should not be used for projects which might create distortion of competition within other member countries. Member countries not participating in the exchange rate mechanism will not contribute to the financing of this scheme. I stressed the importance of Community policies, taken as a whole, contributing to convergence in the economic performance of members of the Community. It was doubts about the value of the proposals so far made that contributed to the unwillingness of Italy and Ireland to commit themselves. The Commission was invited to look into this whole question and report back to the next European Council.

Common Agricultural Policy

"As regards the Common Agricultural Policy, the Commission made a report recommending a rigorous price policy as a way of tackling the problem of surpluses, with a freeze on common prices for 1979/80. The President of the Commission announced that the Commission would make

/its ...

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* The European Unit of Account comprises a basket of the nine Community currencies, its value against each being calculated daily by the Commission. It was set up to facilitate transactions within the EEC.

its detailed proposals for next year's prices on this basis. The Council agreed to return to this problem and to establish the necessary guidelines at its next meeting in March. There was a short discussion about Fisheries and the Commission was asked to make further efforts towards finding a satisfactory settlement.

"Among other topics I should report briefly on two. The first was the agreement to ask a Committee of three drawn from France, the Netherlands and Britain to look at the way the Community works and make practical suggestions for improvements, with a view particularly to the prospective enlargement to twelve. My Rt. Hon. Friend the Member for Birkenhead* has been good enough to accept an invitation to serve together with M. Barend Biesheuvel of the Netherlands and Mr. Robert Marjolin of France.

Emoluments to European Assembly Members

"Secondly, Foreign Ministers discussed the emoluments which should be received by directly-elected members of the European Assembly. They agreed that the emoluments should be based on those of members of national parliaments and be subject to national taxation. There will be consultation with the Assembly by the President of the Council of Ministers.

"Mr. Speaker, we were greatly helped throughout this long and arduous meeting by the skilful chairmanship of Chancellor Schmidt. We can be satisfied that our country played a constructive part in the months of discussion that led to the construction of the European Monetary System. The initial decision has now been taken and it is for each country to decide whether the proposals now on offer are commensurate with the greater risks involved of going into the exchange rate mechanism. The British Government hopes that the greater stability which the dollar has enjoyed in recent weeks will continue and will help the exchange rate mechanism of the EMS when it begins to operate. We for our part look forward to participating in further work which remains to be done on both the internal aspects of the system and in its wider international implications.

"The broad conclusion I offer to the House is that well-constructed and effective international monetary

/arrangements ...

*Mr Edmund Dell, who resigned from the Cabinet post of Secretary of State for Trade in November.

arrangements can assist those who take part in them in certain circumstances but they can be no more than additional supports and that in the end it will be the success of our own efforts in restraining inflation, keeping down prices, maintaining the stability of sterling and remaining competitive that will ensure the long-term well-being of our people."

(Prev. Ref. 47/78)

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