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Monetary cooperation and monetary policy in the EU

The Delors Plan, the Maastricht criteria

Lecture 2

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Lecture 2

In this lecture you will learn about:

- The advantages of a single currency compared to an exchange rate regime
- The single market and single currency agendas of the Delors Committee (1985-1995)
- The Delors Plan of introducing the EEMU
- The Treaty on European Union (the Maastricht Treaty) and the EEMU
- The Maastricht criteria of joining the monetary union
- The 1990s: the road to EEMU

From European monetary cooperation to European monetary union

The Werner Plan was eventually not adopted. However, the European Monetary System (EMS) was launched in 1979.

The EMS operated smoothly in the course of the 1980s therefore **the heads of the EEC member states decided to revitalise the European monetary union project**. It occurred in parallel with the single market agenda, also launched in the 1980s. Both projects were nurtured by **at-that-time President of the European Commission, Jacques Delors**.

Jacques Delors

Jacques Lucien Jean Delors (born 20 July 1925) is a French politician who served as the **8th President of the European Commission** from 1985 to 1995. He served as Minister of Finance of France from 1981 to 1984. He was a Member of the European Parliament from 1979 to 1981. As President Delors was the most visible and influential leader in European affairs. He implemented the policies that closely linked the member nations together and tirelessly promoted the need for unity. He had critics but on the whole was well respected for his imagination and commitment to the cause of European unity. His two main achievements were creating a single market that made possible the free movement of persons, capital, goods, and services within the Community. He also headed the committee that proposed the monetary union to create the euro, a new currency to replace individual national currencies.

Delors promoted an alternative interpretation of capitalism that embedded it in the European social structure. He synthesized three themes. From the left came favouring the redistribution of wealth, and the protection of the weakest. Second a neo-mercantilist approach wanted to maximize European industrial output. A third was reliance on the marketplace. His emphasis on the social nature of Europe is been central to a important exceptionalism narrative that became central to the self-identification of the European Union.

The Delors presidency has been considered as the apex of the European Commission's influence on European integration.

The **advantages of a monetary union** are the following:

- it helps reduce transaction costs in an increasingly integrated regional market;
- it helps increase price transparency, thus increasing inner-regional competition and market efficiency;
- in Europe, a monetary union was seen to be an essential step toward the further political integration of the EU.

The single market and single currency agendas of the Delors Committee (1985-1995)

After the recession of the 1970s, **the 1980s saw a new big impetus to European integration**. Firstly, with the Southern enlargement, the less developed countries of Greece (1981), and then Portugal and Spain (1986) joined the EEC. In the meantime, in the **Milan Summit** of the European Council in 1985, a **White Book on the completion of the Single European Market** (SEM) was published and debated. The document identified the three major areas of obstacles in the completion of the single market:

- **physical obstacles** (internal borders among member states);
- **technical obstacles** (production standards and other quality and safety requirements);
- and **administrative obstacles** (including the quality of financial services backing internal cross-border trade, and tax policy disharmonies).

The consultation of the White Book led to the first amendment to the Treaty of Rome in 1986. The document was called the **Single European Act**, as its focus was on the completion of the Single European Market. The deadline set for the adoption of the connecting legislation by the member states was **1 January 1993**.

In parallel with the launch of the Single European Market, the **preparation for the common currency started**: the at-that-time President of the European Commission, **Jacques Delors** chaired a committee that elaborated the **plans for the economic and monetary union**.

The Delors Committee (1988-1989)

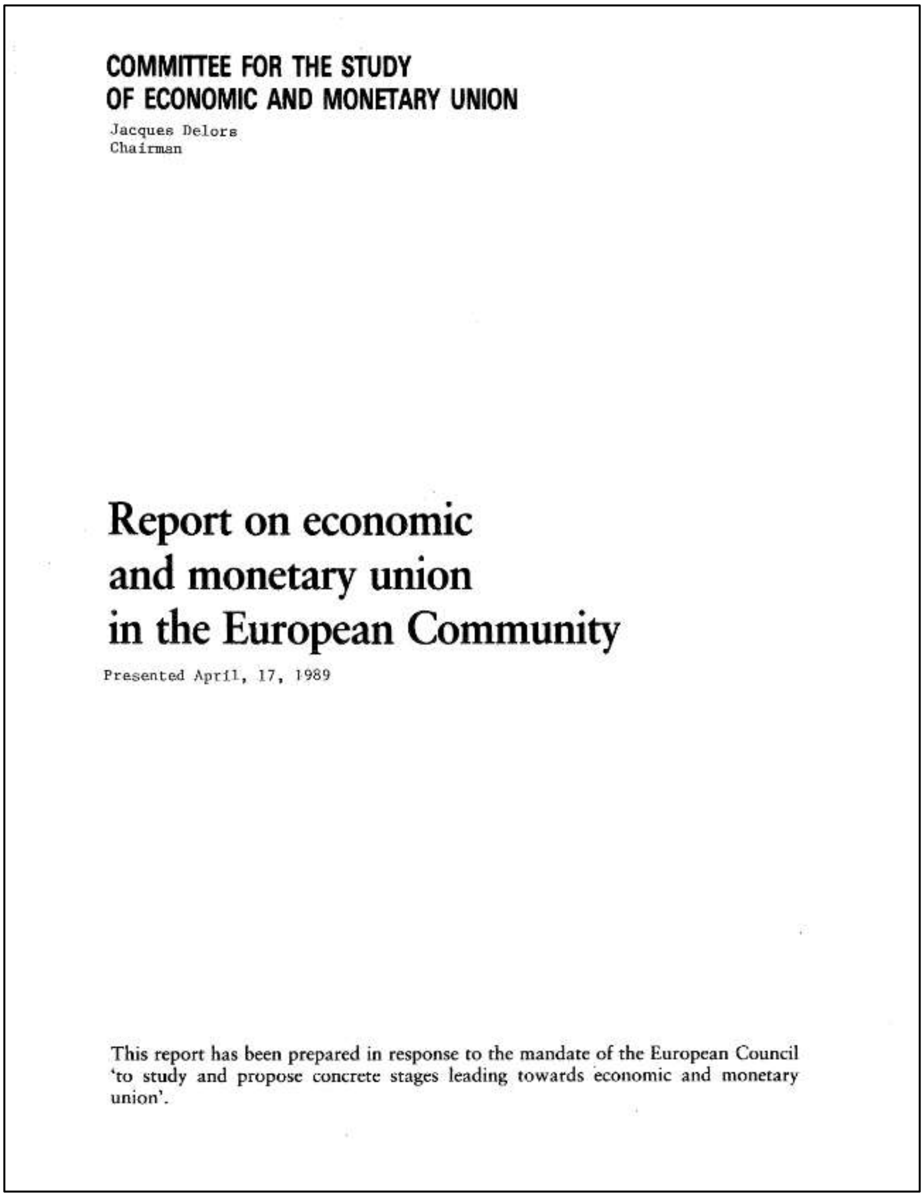
The Committee for the Study of Economic and Monetary Union, better known as the Delors Committee, was set up in June 1988. Its establishment followed a European Council mandate to examine and propose concrete stages leading to European Economic and Monetary Union. The Committee was chaired by Jacques Delors, the President of the European Commission at the time. It consisted of the Governors of the European Economic Community Member States' central banks and some other members. Among them was Alexandre Lamfalussy, then General Manager of the Bank for International Settlements in Basel and later the first President of the European Monetary Institute.

The Delors Committee fulfilled its mandate by launching a report in April 1989 on "Economic and Monetary Union in the European Community". Among other proposals, the report suggested three stages for achieving Economic and Monetary Union and helped the monetary and economic unification process to develop.

This was a time of vivid debates: some theoreticians and practitioners voted for the economic integration preceding the monetary union, while others thought that a monetary integration would result in economic integration. Eventually, the representatives of the latter opinion "won the battle". This way, the plan for introducing the common currency was drafted, and realised.

The Delors Plan

The Delors Plan, drafted by the Delors Committee, envisaged the introduction of a European economic and monetary union in stages, just as the Werner Report did 20 years earlier.



COMMITTEE FOR THE STUDY
OF ECONOMIC AND MONETARY UNION

Jacques Delors
Chairman

Report on economic
and monetary union
in the European Community

Presented April, 17, 1989

This report has been prepared in response to the mandate of the European Council 'to study and propose concrete stages leading towards economic and monetary union'.

The **phases of the Delors Plan** were presented with timing:

1. **Phase One (1990-1993)**: With the completion of the Single European Market, the **full liberalisation of capital markets** is realised. From this time on, capital can move freely in the whole of the EU. The realisation of the freedom of capital flow required the **full and unlimited convertibility of the EU member states' currencies** among each other. European exchange rates are handled in the Exchange Rate Mechanism (ERM) of the European Monetary System (EMS).

In the middle of Phase I, the perhaps so far biggest step forward was taken in European economic integration: the text of the **Treaty on European Union (TEU)** was agreed on in the Dutch city of Maastricht, in the European Summit held in December 1991.

2. **Phase Two (1994-1998)**: In the so-called **convergence phase**, the member states were obliged to fulfil the criteria of entering the monetary union set out in Maastricht. The greatest challenge about meeting the convergence criteria was to keep down inflation and budget deficits at the same time, while reducing government debts without raising the levels of long-term interest rates.

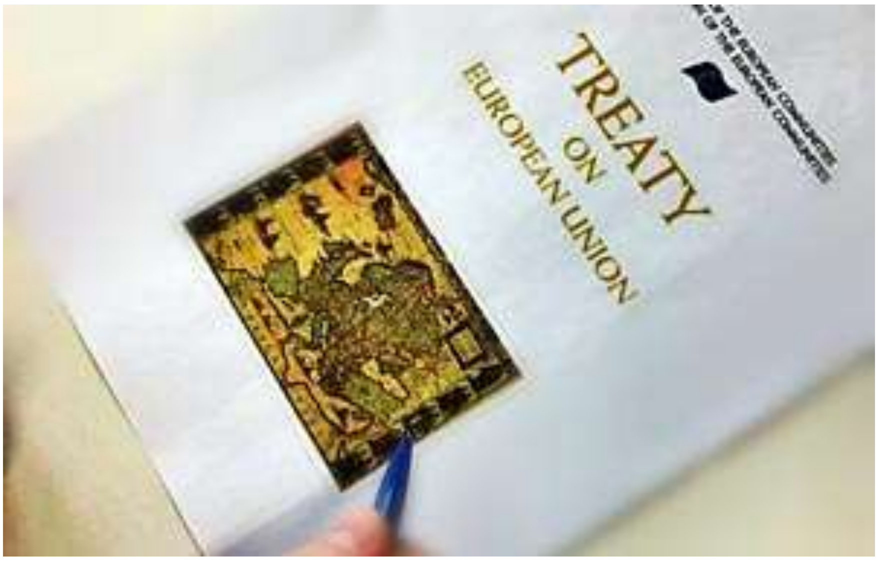
The **1993 White Book on Growth, Employment and Competitiveness** gave the "recipe" for the EU member states' economic policies in this period: deficit and debt can only be "grown out", and economic growth can only be stable if there are **high levels of employment** and if **products and services are competitive**, not only in the internal market of the EU, but also on the global platform. Most of the member states were successful in their economic policies in this time period.

The other important task in Phase II was the construction of the **institutions, tools and set of objectives of the common monetary policy**. A transitory institution elaborating all this was set up: the **European Monetary Institute (EMI)** existed only in Phase Two and was eventually the legal predecessor of the European Central Bank (ECB), established in 1998.

3. **Phase Three (1999-): The Economic and Monetary Union was launched**. The introduction itself had a transitional period when the euro was only used as an **accounting currency**: the exchange rates of the participating countries were fixed but **national currencies remained in circulation until the end of 2001**.

The Maastricht Treaty

The text of the **Treaty on European Union** (TEU) was adopted in Maastricht, in December 2001, that is why we often refer to it as the Maastricht Treaty. It was of fundamental importance for European integration. **It created the European Union that is based on the European Economic and Monetary Union**.



The Maastricht Treaty was signed on 7 February 1992, and entered into force on 1 November 1993. The purpose of the Treaty was to prepare for the EEMU and introduce elements of a political union (citizenship, common foreign and internal affairs policy).

The **main changes** incurring in European integration according to the TEU were:

- establishment of the European Union based on the economic and monetary union;
- introduction of the co-decision procedure, giving Parliament more say in decision-making;
- new forms of cooperation between EU governments – for example on defence and justice and home affairs.

The Maastricht criteria

In order to adopt the euro, EU countries have to bring their national legislation in line with relevant EU law and **meet specific conditions designed to ensure economic convergence**. These requirements, agreed by the EU Member States in Maastricht in 1991, are known as the convergence criteria.

The Maastricht convergence criteria were put in place to measure progress in countries' preparedness to adopt the euro, and are defined as a set of **macroeconomic indicators**, which focus on:

- Price stability
- Sound public finances, to ensure they are sustainable
- Exchange-rate stability, to demonstrate that a Member State can manage its economy without recourse to excessive currency fluctuations
- Long-term interest rates, to assess the durability of the convergence

What is measured:	Price stability	Sound and sustainable public finances	Durability of convergence	Exchange rate stability
How it is measured:	Harmonised consumer price inflation	Government deficit and debt	Long-term interest rate	Exchange rate developments in ERM II
Convergence criteria:	A price performance that is sustainable and average inflation not more than 1.5 percentage points above the rate of the three best performing Member States	Not under excessive deficit procedure at the time of examination	Not more than 2 percentage points above the rate of the three best performing Member States in terms of price stability	Participation in ERM II for at least 2 years without severe tensions, in particular without devaluing against the euro

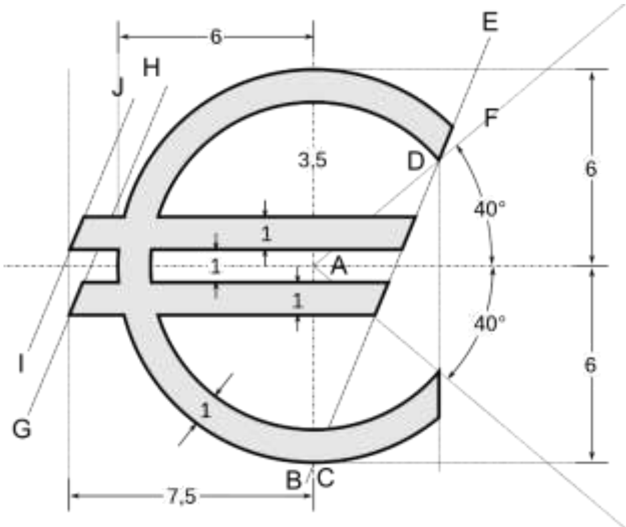
The Treaty also calls for an examination of other factors relevant to economic integration and convergence. These additional factors include the integration of markets and the development of the balance of payments. Their assessment is also seen as an important indication of whether the integration of a Member State into the euro area would proceed smoothly.

According to the Treaty, at least once every two years, or at the request of a Member State with a derogation, the Commission and the European Central Bank assess the progress made by the euro-area candidate countries and publish their conclusions in respective Convergence Reports.

The 1990s: the road to EEMU

In the middle of the 1990s, in parallel with the establishment of the Economic and Monetary Union, the membership of the EU grew from 12 to 15 as Austria, Finland and Sweden joined the EU in 1995.

At the **Madrid Summit in 1995**, the **name of the single currency** was decided and thus the term **"euro"** and the abbreviation **"EUR"** was born. Later, its sign was designed:



The design was presented to the public by the European Commission on 12 December 1996.

From the obligation to fulfil the **Maastricht criteria**, only the **United Kingdom** and **Denmark** has enjoyed and **opt-out right**, based on a Protocol amended to the Treaty on European Union, meaning that even if they fulfil the criteria to accede the monetary union, they have the right not to join it. A third country, **Sweden, did not enter the ERM**. In the 1990s, **Greece performed badly in meeting the criteria**. Accordingly, the European Economic and Monetary Union (EEMU) was launched with 11 member states on 1 January 1999.

However, even the citizens of these 11 member states did not realise this huge step forward at that time as the **national currencies were not replaced by the euro banknotes and coins immediately**.

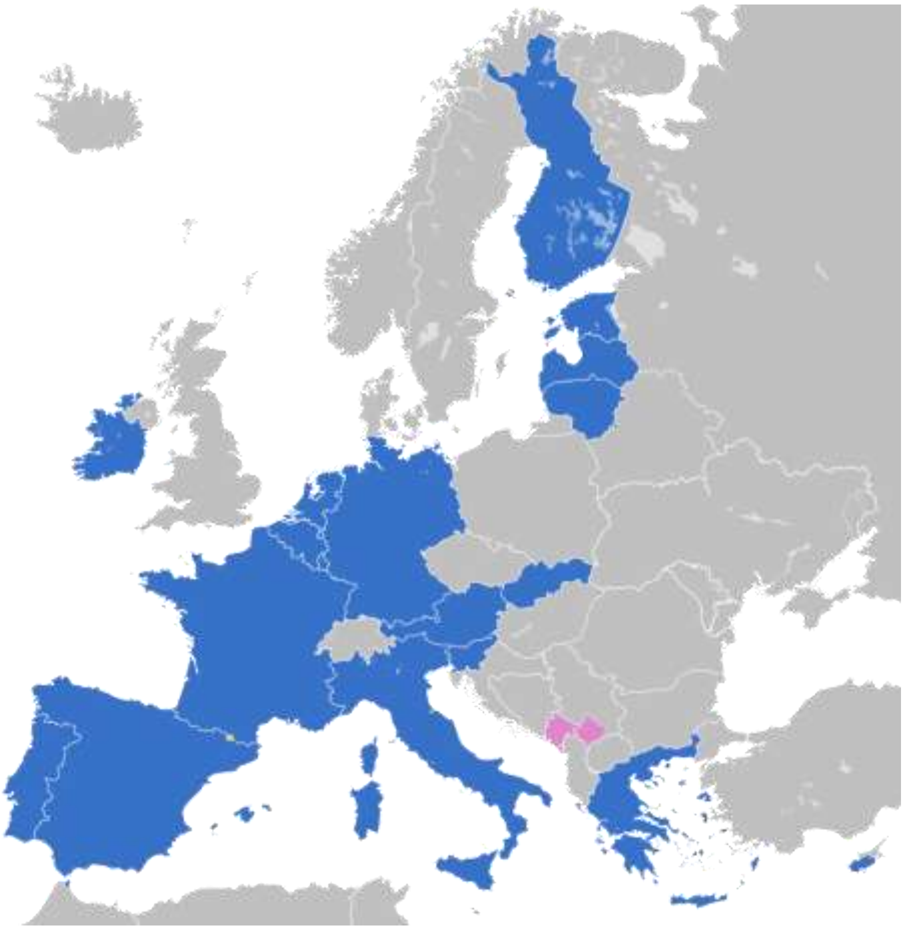
During the year of 2001, Greece succeeded in performing macroeconomic data that qualified the country into the monetary union. This way, **on 1 January 2002, the euro banknotes and coins were introduced in 12 member states – this was the so-called cash changeover**. In the case of later accessions to the Eurozone (Slovenia, Malta, Cyprus, Slovakia and Estonia), there was no such transitional period any more.

The member states of the EU can be divided according to their Eurozone membership. **In 2020, there are 19 members of the Eurozone**. The dates of the countries' joining of the monetary union are the following:

- 1 January 1999 (launch of the monetary union): Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain
- 1 January 2001: Greece
- 1 January 2007: Slovenia
- 1 January 2008: Cyprus and Malta
- 1 January 2009: Slovakia
- 1 January 2011: Estonia
- 1 January 2014: Latvia
- 1 January 2015: Lithuania

Of the member states outside the Eurozone, **Denmark and the United Kingdom have continued to apply their opt-out rights** (and then, on 31 January 2020, the United Kingdom left the EU). **Sweden has still not entered the exchange rate mechanism** (neither the original ERM, nor the ERM-II which, since 1999, connects the national currencies outside the Eurozone to the euro).

Of the Eastern new member states, only Slovenia, Cyprus, Malta, Slovakia, Estonia, Latvia and Lithuania have met the convergence criteria; **the remaining six new member states have not entered the ERM-II until summer 2020**.



Questions for self-study

1. What are the advantages of a single currency compared to a fixed exchange rate regime of national currencies?
2. How are the single market and the single currency projects related in European economic integration?
3. When was the Delors Plan introduced to the European Council? When was it implemented?
4. Which were the three stages of introducing the EMU according to the Delors Plan?
5. What areas do the Maastricht convergence criteria cover?
6. When did the EMI exist and what was its main role?
7. What is the significance of the 1995 Madrid Summit?
8. How has the membership of the Eurozone developed since 1999? How many member countries does it currently have?

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