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Treasury Chambers, Parliament Street, SW1P 3AG  
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Prime Minister

Are you content  
with the general  
approach proposed

October 1989

by the Chancellor?  
It seems very much  
on the right lines to me.

Charles Powell Esq  
Private Secretary  
10 Downing Street  
London  
SW1A 2AA

*W. H. Williams*

Dear Charles

**ECONOMIC AND MONETARY UNION**

I attach a draft of the Chancellor's opening speech for Thursday's adjournment debate. He has not had a chance to look at the draft himself although he discussed the main themes with officials. He proposes to stress that the Government cannot accept the federal approach to the future of Europe, which underlies Delors' proposals; and to make clear the problems of accountability which those proposals raise.

CDP  
31/10

The Chancellor would be grateful to know whether the Prime Minister is content with the approach taken in the draft speech.

I am copying this letter to the Private Secretaries of the Secretary of State for Foreign and Commonwealth Affairs, the Secretary of State for Trade and Industry, the Lord President of the Council and the Leader of the House of Lords.

Yours sincerely  
*J M G Taylor*  
J M G TAYLOR

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ADJOURNMENT DEBATE ON ECONOMIC AND MONETARY UNION, 2 NOVEMBER 1989  
CHANCELLOR'S OPENING SPEECH: DRAFT OF 31 OCTOBER

1. Mr Speaker, I very much welcome this opportunity for a debate on economic and monetary union in the European Community. It comes at a particularly relevant time.

2. The Delors report, which the Select Committee on European Legislation has recommended for debate, was published in April this year. It was - and we should be quite clear about this - a report from a group of experts. The Governor of the Bank of England, who was a member of the Delors Committee, explained their approach to the Treasury and Civil Service Select Committee in May. They devoted themselves - and I quote - "very much to how economic and monetary union might be achieved, rather than whether or when. We took the view that whether or when was a matter for political leaders".

3. The Delors report was considered by the European Council in Madrid in June. The Council agreed to adopt the first stage of its proposals, and I will say more about these later. It asked the relevant Community bodies to carry out further preparatory work on developments beyond that stage with a view to the organisation of an intergovernmental conference, which would meet once the first stage had begun.

4. The Council of Finance Ministers and the General Affairs Council are now engaged in the further work agreed at Madrid. My Rt Hon Friend the Secretary of State for Foreign and Commonwealth Affairs will be attending a meeting of the General Affairs Council next Monday at which economic and monetary union will be on the agenda. I will be attending the Council of Economic and Finance Ministers for a full discussion of EMU on Monday 13 November. Economic and monetary union will be discussed again in December at the European Council in Strasbourg. So this debate will give my

Rt Hon Friends the Prime Minister and the Foreign Secretary, as well as myself, the opportunity to take full note of the House's views as we prepare for these vital discussions.

5. Mr Speaker, the subject of economic and monetary union goes to the heart of the debate about the future development of the Community - indeed the future development of the whole of Europe. Whether Europe should develop, as some want, into a federation governed under some centralist and centralising structure; or whether, as we seek, it should <sup>continue to</sup> develop into an even closer partnership of member states, working closely together, certainly within an institutional structure, to achieve mutually agreed objectives.

6. M. Delors has made very clear the sort of Community - the sort of Europe - which he would like to see. Speaking in Bruges last month he said:

"How can we pave the way for a solution other than by reinforcing certain federalist characteristics of the Community .....

He went on to say that the European Council this December should start the process of amending the Treaty of Rome in order to provide for full economic and monetary union; and that the whole process of Treaty change, including ratification by national parliaments, should be completed by the end of 1992.

7. I have to say categorically to this House that Her Majesty's Government does not, and never will, agree that Europe should proceed down the federal path. I will quote from another speech in Bruges, which my Rt hon Friend the Prime Minister made a year ago:

"I am the first to say that on many great issues the countries of Europe should try to speak with a single voice .... But working more closely together does not require power to be centralised in Brussels or decisions to be taken by an appointed bureaucracy. Indeed, it is ironic that just when those countries such as the Soviet Union which

have tried to run everything from the centre are learning that success depends on dispersing power and decisions away from the centre, there are some in the Community who seem to want to move in the opposite direction".

8. Mr Speaker, I hope that the House can unite behind these words. We should not forget that in discussing future economic and monetary arrangements we are discussing the ultimate political shape of Europe and the Community. They are inextricably linked.

9. Mr Speaker, the idea of moving towards economic and monetary union in the Community has a long history. A report in 1970 by M. Pierre Werner, then Prime Minister of Luxembourg, made detailed proposals for progressing to EMU: transferring major economic policy decisions to Community level, adopting a single currency and setting up a single central bank. The Community endorsed these proposals and agreed that full EMU would be achieved by December 1980 at the latest. Mr Speaker, after that endorsement other events intervened and nothing much came of the Werner proposals.

10. Nevertheless throughout the seventies the Community continued to endorse the principle of progressing towards economic and monetary union. My Rt Hon Friend the member for Bexley [whom I am glad to see in his place today] took part in a conference of Heads of current and future member states in October 1972 which reaffirmed the Community's resolve to move towards EMU. The European Council in Brussels in 1977, attended by the then Prime Minister, the Rt hon Lord Callaghan of Cardiff, reaffirmed - and I quote - "its attachment to the objective of EMU." And the Single European Act of 1986 recalled, in its preamble, the objective of the progressive realisation of EMU.

11. The House may fairly ask what successive UK Governments - Governments of both complexions - understood by these commitments to EMU. I can only speak for the present Government. The objectives of economic union are well established. They include sustained increases in living standards

and more flexible market-oriented economies. The objectives of monetary union are more complex. What we understand by them are:

- price and currency stability throughout the Community;
- equal access to capital and financial services by all citizens and all businesses in the Community, especially across borders;
- lower costs of financial transactions throughout the Community.

12. Mr Speaker, just as there are different views about the future political shape of the Community, so there will be different views about the right way to approach these monetary objectives. The Delors report is not definitive. As the Madrid Council agreed, it is a basis for consideration.

13. Let us look more closely at the Delors prescription. The House will be familiar with its main proposals:

- as a first stage, the Community must complete the process of establishing a genuinely single market in goods, services, and capital; competition policy should be strengthened; all Community currencies should join the Exchange Rate Mechanism of the European monetary system on the same terms; and the coordination of member states' economic and monetary policies should be strengthened. The Commission's proposals for revised coordination arrangements are among the documents listed for our debate today. We agree with these proposals for Stage 1. It is only with the Delors proposals for the later stages where the difficulties emerge;
- in a second stage, as envisaged by Delors, member states would begin to work within Community-wide macro-economic policy guidelines adopted by majority decision, and would set up a new European System of Central Banks;

- and in a third and final stage, exchange rates would be irrevocably locked; national currencies would eventually be replaced by a single Community currency; national budgetary policies would be subject to binding central rules; and the European System of Central Banks, "independent of instructions from national governments" (that is a quote from the Delors report), would take sole responsibility for formulating Community monetary policy and for operating Community exchange rates vis a vis the rest of the world.

14. I am quite ready to acknowledge that the analysis in the Delors report is a useful contribution to the debate. It sets out a helpful prescription for Stage I. But I have to put it to the House that there are fundamental flaws in its prescription for developments beyond Stage I. It is quite simply, the wrong way for Europe. There must be a better way.

15. Mr Speaker, I have today placed in the Library of this House and deposited in the Vote Office copies of a paper entitled "An Evolutionary Approach to Economic and Monetary Union". I am also circulating this paper to Community Economic and Finance Ministers. It sets out the views of the British Government on an alternative approach, an evolutionary approach, to economic and monetary union. It is intended to be a contribution to the debate on EMU within the Community, starting with the discussion at the Economic and Finance Ministers Council this month.

16. The Government's fundamental concern about the Delors approach beyond Stage I is its centralising prescription for economic and monetary union. It relies on administrative fiat and institutional change. It skates over vital issues of political accountability. It ignores the basic fact that changes in economic and monetary arrangements must reflect real changes in economic behaviour in the market place - they must work with the grain of the market.

17. Her Majesty's Government - and I hope the overwhelming majority of this House - takes issue with the Delors prescription for the later stages on four particular counts:

- first, the Delors proposals for a single monetary policy, a single currency and a single independent central bank are unacceptable. <sup>raise serious issues of accountability. They</sup> They are landmarks on the path to the vision of a federal, centralist Europe;
- secondly, there would be no guarantee that a single centrally-run monetary policy would reflect the views of those Community countries most wedded to low inflation. There is a strong risk that policy and inflation would converge on the average, not the best;
- thirdly, binding Community rules on national budget deficits, as proposed by Delors, are neither necessary nor desirable. [They are not necessary because monetary unions can and do tolerate diversity of budgetary positions in their component regions. And markets will impose a discipline tending to prevent deficits getting too far out of line. On the desirability of binding rules,] I note the conclusion of the Treasury and Civil Service Select Committee: "The power of the House of Commons over the centuries has depended fundamentally on the control of money, both taxation and expenditure. This would be jeopardised by the form of monetary union proposed by the Delors Report which would involve central undemocratic direction from within Europe of domestic budgetary policies."
- fourthly, Delors' proposals for increased regional and structural aid are misconceived. There must of course be greater opportunities for the living standards of the less prosperous regions to rise. The Community's structural funds are already being doubled in the five years between 1988 and 1993. But there is no reason to think that a route to EMU which relies primarily on the operation of the market - not government intervention - would have a negative impact on the less prosperous areas.

18. Mr Speaker, this Government is fully committed to progressively strengthening economic and monetary integration in the European Community. Our commitment is just as strong, just as deep, as that of our Community partners. But we prefer to express it in more practical terms.

19. The Government's approach rests on three principles:

- the overriding objective of price stability;
- increasing the influence of markets and competition;
- retaining national control over economic policy-making to the maximum extent possible.

20. I will draw the attention of the House to just four of the main points made in our paper

21. First, Stage I will bring about massive changes in the European economy. The completion of the single market will progressively increase freedom of trade in both goods and services, and freedom of movement of capital and labour. Regulations and technical barriers will be drastically reduced; industries will be restructured; businesses become more efficient; consumers will benefit.

22. As I told the House on Tuesday, the UK Government will join the ERM during Stage I when the level of UK inflation is significantly lower, when there is capital liberalisation in the Community, and when real progress has been made towards completion of the single market, freedom of financial services and strengthened competition policy.

23. In the environment created by Stage I there will be powerful pressures on Governments to adopt low inflation. Governments will have a strong incentive to minimise inflation in order to attract economic activity. With the removal of exchange controls and the creation of a single financial area, the capital markets will react more quickly and directly when they fear that a country is



not operating sufficiently sound monetary policies. This will be a powerful discipline. Greater stability of prices will in turn mean greater stability of exchange rates. All this will be achieved through the market - not through centralised regulation and direction.

24. Our second point, Mr Speaker, is that the changes I have described will take many years to complete. More than half of the 279 single market measures have yet to be adopted at Community level. Only 7 have been implemented in the legislation of all 12 member states - though I should say that the UK's record in implementation is among the best in the Community and way above this figure. The competitive forces which will be released as the single market becomes a reality will lead to a period of increased integration. This will be an evolutionary process. We simply cannot predict its outcome.

25. That is why this Government is so concerned not to rush into drawing up blueprints for the future, before Stage I has even started. Remember Werner.

26. The third point made in our paper is that further measures will be needed after Stage I to continue the process of integration. The pressures on Governments to keep down inflation and enhance the stability of currencies would be increased by removing all unnecessary restrictions on the use of Community currencies.

27. The costs of changing between current Community currencies could also be reduced further. They are likely to come down with technological improvements and increased competition between banks. We shall need to remove any unnecessary barriers to further reductions in transactions costs in, for example, cheque clearing, use of credit cards abroad, and access to automatic teller machines throughout the Community.

28. Our final point, Mr Speaker, is that over time, all these measures will strengthen the process of convergence on price and exchange rate stability. Realignments should become rarer,

fluctuations within the bands of the Exchange Rate Mechanism should become smaller, and we could eventually see a system of more or less fixed exchange rates. With minimal exchange rate uncertainty and reduced costs of switching between currencies, all Community currencies would become effectively interchangeable. In this way a practical monetary union could be achieved as the result of a gradual evolutionary process.

29. Mr Speaker, I hope it will be clear to the House - and clear to our partners in Europe - that this Government wishes to play a constructive part in the debate on Economic and Monetary Union in the European Community.

30. But we will be not swept into unwise and premature decisions. I believe a number of others in the Community are beginning to draw back from this Gadarene rush. The Madrid Council agreed that more work was needed. That work must be very thorough and very well considered. It must not be rushed. The future development of Europe is of enormous significance. Changes cannot be imposed; they must be agreed.

31. Mr Speaker, Britain has played, and will continue to play, a full part in Europe. We do not wish to stand aside from its development. That is why we have put forward the alternative, evolutionary, approach which I have described to the House this afternoon. It avoids the pitfalls of the Delors prescription, and offers a sound basis for developing the enormous potential still locked within the Community.

32. Mr Speaker, I commend to the House our evolutionary approach to economic and monetary union in the European Community.

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10 DOWNING STREET

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*From the Private Secretary*

1 November 1989

*Dear Jonathan,*

ECONOMIC AND MONETARY UNION

Thank you for your letter of 31 October enclosing the first draft of the Chancellor's opening speech for Thursday's Adjournment Debate. The Prime Minister is well content with the general line taken in the draft. You will no doubt let me see any subsequent version.

I am copying this letter to the Private Secretaries to the Secretary of State for Foreign and Commonwealth Affairs, the Secretary of State for Trade and Industry, the Lord President of the Council and the Leader of the House of Lords.

*Yours sincerely,  
Charles Powell*

CHARLES POWELL

J M G Taylor Esq  
HM Treasury

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