Klaus Liebscher: European Economic and Monetary Union - how to continue a success story?

Speech by Dr Klaus Liebscher, Governor of the Austrian National Bank, at the International Financial and Economic Forum, Vienna, 13 November 2003.

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Ladies and Gentlemen,

By the end of last month, the successful era of President Willem Duisenberg at the helm of the European Central Bank came to an end. At the beginning of this month, Mr. Jean-Claude Trichet became second President of the European Central Bank. Certainly, already this change at the top of the ECB provides a good opportunity for both looking back and looking into the future. Moreover, from a broader perspective, we are at the threshold of the historic event of the accession of five Central European and three Baltic countries as well as two Mediterranean islands to the European Union.

When eleven EU member states entered the third stage of the Economic and Monetary Union by adopting the common currency, the euro, on the 1st of January 1999, this historic step was accomplished in such a smooth way that it is often simply taken as a matter of fact. However, looking back, it should be highlighted that there were not at all any problems, despite heightened uncertainties in the international financial markets following the turbulences in Asia, Russia and Brazil. Certainly, this was due to the fact that this step was indeed well-prepared. Moreover, the acting persons, and in particular the first President of the ECB, Willem Duisenberg, whose appointment became effective already as of June 1st 1998, had a strong commitment and merited high credibility.

In the meantime, the ECB became a successfully working institution, the Eurosystem prepared and realized a great number of logistical, operational and organizational issues - highlighted by the smooth Cash Changeover in 2002. And the euro establishes itself as a leading world-currency.

In 2002, the share of the euro in the settlement and invoicing of global exports of individual euro area countries to countries outside the euro area has risen to between 40% and 58%. Moreover, the euro has been well-received in the financial markets. In particular, a significant European corporate bond market has emerged.

Further to its role in trade and financial markets, the euro has been used by many third countries as an important official reserve currency and as an anchor in their exchange rate regimes.

The success of the Economic and Monetary Union in Europe can be measured not only by looking at all that what happened, but also by taking into account what could be avoided. Within the euro area, the monetary union has kept member countries from being exposed to harmful intra-European exchange rate tensions of the type that many countries used to suffer when external shocks occurred. It has become quite obvious that the countries constituting the euro area are protected from negative shocks much more comprehensively now than was possible under past regimes. Indeed, major external developments in recent years, like the bursting of the equity bubble, the repercussions of the terrorist attack on September 11, 2001 and the more recent substantial depreciation of the US dollar that has resulted from the sizeable imbalances in the US economy, otherwise might have led to phases of instability within the European economy. Instead, they could be weathered within a stable framework.

During the past five years, the Eurosystem successfully achieved its primary objective of maintaining price stability over the medium term. Despite some years of rising world energy prices combined with a strong appreciation of the US dollar, the Eurosystem managed to achieve low inflation and low interest rates, which will ultimately stimulate further investment and contribute to sustainable growth in the euro area. Thereby, the euro will contribute to more balanced global growth and to more stability in the international financial system.

The current state of the European Economic and Monetary Union, its “stability architecture” and its developed rule-based “stability culture” truly represent a culminating point in the process of European integration. Indeed, over the last half century, Europe has followed an impressive path of voluntary integration of nations, so far unparalleled in history. Economic integration, in particular, was successively deepened. Moreover, in parallel to the process of deepening the integration, the European Union was successively enlarged. At present, we are at the threshold of a further historic enlargement of the European Union. The accession of ten new Member States, scheduled for May 1st 2004, is of great political importance and also has non-negligible economic implications.

Looking into the future, there are two main challenges for the European Economic and Monetary Union. The first challenge consists in strengthening the hitherto developed architecture and culture of stability, the second in successively integrating the incoming new Member States, and both challenges are certainly inter-linked.

Regarding the “stability architecture”, the legal fundaments of the Economic and Monetary Union have to be transposed appropriately into the Treaty establishing a Constitution for Europe, in order to ensure that the essence of the stability orientation of the Economic and Monetary Union will be preserved and the institutional position of the Eurosystem within the whole European Union will be better defined.

At least as important as the architecture is the way how the authorities live in the well-established house of the Economic and Monetary Union. This is what I would like to term the “stability culture”. It is certainly a significant task for monetary policy makers to thoroughly honour their obligations to conduct a stability-oriented balanced monetary policy for the whole euro area. Moreover, it is a formidable challenge for fiscal policy to maintain a culture of stability, in particular in times of slow growth. Nonetheless, it is essential that all EU Member States remain credibly committed to and, thus, comply with the existing framework of democratically established self-imposed rules. The challenge consists in responding positively to the fiscal consolidation pressure which results from obeying the rules. In addition, acute pressures may be avoided by anticipating longer-term reform measures in a timely manner. Obviously, this is directly linked to the next major ingredient of a “stability culture”, namely structural reform. Finally, the required “culture of stability” comprises also a responsible attitude on the side of both employers and employees, in particular in member countries where central wage bargaining prevails.

Ladies and Gentlemen, I am convinced indeed that the solid foundation of the stability architecture and the attitude of a stability culture will certainly make the decisive contribution to continue the success of the EMU.

Now, turning to the second main challenge for the Economic and Monetary Union, I would like to state very clearly that I highly welcome the acceding countries’ joining the European Union. After the fall of the “iron curtain” 14 years ago, the Central and Eastern European countries have undergone an impressive and successful, if often painful, process of transformation and we see their joining our Union as a well-deserved and historic step.

Upon entering the European Union, the new Member States also become members of the Economic and Monetary Union. While they do not take part in EMU to the full extent, as they cannot immediately join the euro area, they are already required to observe a number of obligations embodied in the stability architecture of EMU: They generally have to bring into line their economic and monetary policies with the overall goals of EMU. Their central banks will be represented in the General Council of the ESCB and take part in monetary policy coordination within the EU. The new Member States will participate in the coordination of economic policies and in the multilateral fiscal surveillance. Moreover, they shall treat its exchange-rate policy as a matter of common interest, as the functioning of the single market must not be weakened by real exchange-rate misalignments or excessive nominal exchange rate fluctuations.

From my point of view, it is vital for the new member countries to perform catching-up real growth that permits their income-per-capita levels to gradually approach the average income level in the present EU member countries.

Therefore, economic policies of the new member countries and any further steps in monetary integration should be oriented towards achieving real and sustainable nominal convergence, as both convergence processes are complementary to each other and should be pursued in parallel.

The speed of further monetary integration must not compromise its quality and there will be no uniform appropriate speed, due to differences in the economic situation among new member countries. Decisions have to be taken in accordance with the legal fundaments on a case-by-case basis, and, simultaneously, equal treatment between new and current EU member states must be ensured throughout the whole process.

The acceding countries are in midst of an integration and catching-up process, and their equilibrium exchange rates will be subject to gradual changes and shocks over time. Therefore, any premature euro area participation has to be avoided. This corresponds to the economic reasoning behind the Treaty provision that the Commission and the ECB have to examine the achievement of a high degree of sustainable convergence in their convergence reports to the Council before a decision will be taken on any new Member State's adoption of the euro.

Ladies and Gentlemen, I am sure that the participation of the new member countries in the stability architecture of the Economic and Monetary Union from their accession onwards will decisively contribute to enhancing the success of EMU into the enlarged European Union. Therefore, I am looking forward to this new era, which lies in front of us, characterized by a larger number of Member States and, in terms of ideas, by an even larger potential of human beings. For the Eurosystem, this new era will be personalized by the new president of the ECB, Mr Jean-Claude Trichet, whom I wish all the best, indeed.

Thank you very much for your attention.