The negotiations which led to the creation of the European Monetary System thirty years ago can shed light on the Eurozone's current crisis

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The Euro's roots can be traced back to the creation of the European Monetary System (EMS) in 1979. **Emmanuel Mourlon-Druol** *argues that the negotiations that led to the establishment of the EMS can shed light on the current travails of the Eurozone, and that there are some striking similarities with recent Eurozone summits. Looking at the EMS negotiations now furthers our understanding of European integration and the evolution of the world monetary system.*

"The Germans, especially when they get onto their persecution theme, "You are sacrificing German stability on the altar of external monetary stability" rightly get little sympathy." It is not a Spanish, Greek or Italian minister who made this statement at a press conference this year, following yet another failure to reach an agreement on the creation of Eurobonds or growth issues. It is from a British report at the time of the negotiations on the creation of the European Monetary System. The EMS, created in 1979, is part of the prehistory of the euro: it was a first concrete attempt at organising the European Union's – that was still then the European Economic Community (EEC) – currency relations. And the discussions that took place then bear a striking resemblance to our current predicament.

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Back in late 1960s, EEC's heads of government talked with great fanfare about the creation of a European Monetary Union by 1980. By 1980 however, what had been put in place was a pretty trivial piece of administrative business – an exchange rate system almost identical with the one already in operation, the so-called snake. True, the EMS had a number of advantages. Unlike the snake, it managed to bring together all EEC currencies (except the sterling), it increased the credit mechanisms, its wider bands for less developed economies – Ireland and Italy – made it overall more flexible, and, crucially, it was based on a wider economic policy consensus than ever before.

The traditional explanation of the EMS creation focuses on one year of negotiations, 1978, and the doings of the "great men" of the time, namely Valéry Giscard d'Estaing, the French president, Helmut Schmidt, the German chancellor, and Roy Jenkins, the president of the European Commission. According to that explanation, the EMS emerges suddenly, its negotiations would have been swift, and they would have led to the creation of a brand-new scheme, considerably improved by comparison with the snake.

This conventional view of the EMS creation can be challenged by highlighting two longer-term processes that are still at work at the present day. Based on extensive archive research, I have shown that the emergence of the EMS must also be seen in the context of two interacting longer-term processes. The first was a transnational learning process involving powerful, networked European monetary elite that shaped a habit of cooperation among technocrats. The second stresses the importance of the European Council, which held regular meetings between heads of government beginning in 1974, giving EEC legitimacy to monetary initiatives that had previously involved semi-secret and bilateral negotiations. The interaction of these two features changed the EMS from a fairly trivial piece of administrative business to a tremendously important political agreement.

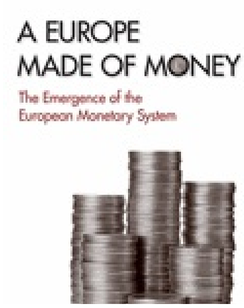
As European leaders desperately needed a victory, they largely puffed up the agreement as some sort of mega-demonstration of the joys of European integration. Valéry Giscard d'Estaing elaborated at length on the rechristening of the European unit of account into the "European Currency Unit", the ECU, as if it were the embryo of a future common or single currency. The reality of the agreement, however, was different. The EMS did not solve the central problems of European economies: it set out no mechanism able to improve the convergence of the EEC member states, the dream of setting up a European Monetary Fund had been put off due to German opposition, and the overall agreement rested on the goodwill of European leaders to implement individual national economic policies that would be compatible with it, rather than an all-encompassing supranational scheme. The EMS was not really the turning point announced, but instead an important political and monetary agreement, the foundations of which remained particularly shaky.

Is this what is happening now? The Irish prime minister talked of a "seismic shift" after the conclusion of the agreement at the last European summit. Mario Monti appeared as a great negotiator, while François Hollande's call for "talking growth" rather than austerity alone seemed to have received some echo. The new European agreement is certainly full of potential. It does highlight a determination to find a solution to the current travails of the Eurozone. The creation of a banking union, as well as the recapitalisation of Spanish banks could prove important steps on the way to a recovery. But as in the 1970s, the last Eurozone compact is also largely puffed up. Countless policymakers described it as a "breakthrough" or a "very ambitious decision." Yet the reality is somewhat more nuanced. To take but one example, the €120 billion allocated to stimulate growth are, in fact, made of sums that are not really new: €55 billion come from unused structural funds, €4.5 billion from the project bond pilot phase, and €60 billion from European Investment Bank (EIB) loans (resulting from a €10 billion capital increase of the EIB).

The parallel with the 1970s is here striking. During the EMS negotiations, Ireland and Italy asked for "transfer of resources" from richer member states (chiefly Germany) to less developed ones. They needed it, they argued, in order to sustain their participation to a European-wide monetary scheme. During the last crucial negotiation on the EMS, at the European Council in Brussels in December 1978, Helmut Schmidt strongly opposed any such help. Italy and Ireland then asked for "a pause of reflection" before saying whether or not they would participate in the EMS. Intense political discussions took place after the summit between all the countries involved. They resulted in an agreement to give interest rate subsidies on EIB loans for Ireland. No real transfer of resources would take place (let alone any increase in the EEC's budget): the German opposition was total. It was the responsibility of each member state to reform itself and converge with the European average.

The June 2012 growth package, both by its size and by its nature, is unlikely to solve from one day to the next the Eurozone's problems – just as the EIB's interest rate subsidy deal struck in 1978 was unlikely to solve by itself the EEC's structural problems. And the most important issues, like the creation of a banking union – or, back in the 1970s, the creation of a European Monetary Fund – are indeed still under discussion. Looking back at the EMS negotiations therefore not only provides insights into the past, but also helps in understanding the pitfalls of present negotiations.

This article is based on Emmanuel Mourlon-Druol's new book, **A Europe Made of Money: the Emergence of the European Monetary System** *(Cornell University Press, 2012)*



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