



TURBULENT WATERS IN THE EMU: TRANSLATION FROM WIRTSCHAFTSWOCHE

KARL OTTO PÖHL*

In September 2010 the German business weekly, *WirtschaftsWoche*, interviewed Mr. Pöhl on old and new conflicts in the European Monetary Union, the future of the euro and necessary structure reforms for the ECB and the Bundesbank.

WirtschaftsWoche: Mr. Pöhl, the Bundesbank is caught up in difficult times. How did you react to the recent debate over Mr. Sarrazin, and what lessons should we learn from it?

I do not want to comment on this issue in detail, but it would surely make sense to change the Bundesbank statute. One should give thought to reforming the procedures for appointments to the executive board. As it now stands it is too federalist. The influence of the federal states on appointments to the executive board has historical reasons that are no longer valid today. What ties does the Bundesbank still have with the federal states? My suggestion would be that only the federal government make appointments to the executive board, and it should include the Bundesbank in this decision making.

Another important issue is the European Monetary Union. How do you evaluate the current debt crisis of the euro countries?

I put no stock in the rescue programme for the euro area. It gives the countries the wrong incentives and violates the spirit and letter of the monetary union. We never wanted a transfer union – but now we are caught up in one. The rescue programme is, after all, a traditional French position. Already in 1979 France wanted a common European fund. Chancellor Schmidt supported President Giscard d'Estaing on this matter. Then the wish was to stabilise the exchange rates in the European Monetary System

(EMS). The idea was that the member states could borrow money from the fund with relative ease. Italy, for example, would have been able to take out a loan in deutschmarks and pay it back in lira. That would have been a real inflation machine. The Bundesbank was strictly opposed to this at the time, and a strong confrontation with the federal government was the result. Helmut Schmidt even threatened us with a reform of the Bundesbank statute to deprive us of our power. However, in the end we prevailed and the fund did not come about. This time the French managed to get their idea through, which could prove to be very expensive for us. If countries such as Greece, Portugal or Ireland do in fact make use of the rescue programme, it will become prohibitively expensive.

Would there have been other options in your opinion?

Of course. Greece should never have been accepted into the monetary union. But it was. Now it must be possible to leave the union. Then, a haircut should have been carried out (partial debt forgiveness by the creditors), the Greeks would have devalued in order to improve their competitiveness. But Mr. Sarkozy was no doubt fearful of the French banks, which were strongly committed in Greece.

Apart from the problem of technical feasibility – wouldn't that have resulted in incredible turbulence?

That's what many say, but I'm not so sure. There might have been the risk of the monetary union collapsing, but the risk was much smaller than most believed. Greece is not really that important after all. The core countries would have remained in the euro area. I do not believe that there would have been major deformations.

ECB President Jean-Claude Trichet has said again and again that the Europeans are bound together by fate. You were involved – as he is – in the process of European unification for many decades. Do Europeans share a common fate?

We are indeed a community. But I do not see things as dramatically as Mr. Trichet does. I have known

* Former Bundesbank President.

him for decades, he is an honest man, and he would never act against his convictions. It was certainly a difficult situation at the beginning of May, when the decision was made on the rescue programme. But I don't believe that Europe itself was threatened because of Greece. The ECB unfortunately has moved into turbulent waters by throwing major principles overboard. It is now purchasing government bonds from euro countries and is thus weakening its independence.

Can this be undone?

In my opinion it is irreversible. They can't 'do this' one minute and 'do that' the next. The bond purchases and the rescue programme are a breach of the Maastricht Treaty by mutual agreement. Of course it was an emergency, but now it has also become a precedent, and that is the great danger.

Now the situation on the financial markets has stabilised somewhat and the euro is also on the road to recovery ...

... which is still no justification for throwing your principles overboard.

What can the ECB do to restore its credibility?

One possibility would be to make Axel Weber its president in autumn next year. Mr. Weber stands for stability policies that the Bundesbank still holds high. It would be even more important, however, to change the ECB statutes. At the beginning of the 1990s when we drafted the statutes, I strongly favoured the principle of 'one country one vote'. That surprised many at the time. Weighting the votes of a country according to economic strength or population size, for example, would not have succeeded politically. But the times have now changed. Then I would not have considered it possible that countries such as Malta and Cyprus would be included in the euro. I thought it would be limited to the six founding members. Now the monetary union has become larger than we originally believed. And therefore the principle of 'one country one vote' is no longer in keeping with the times. It is not acceptable for the central banks of Malta or Cyprus to have the same voting power in the ECB as the Bundesbank. This waters down the decisions of the European Central Bank. Voting rights in the ECB should be changed and weighted votes should be assigned according to the strength

of the countries. This would help the ECB manage future crises more convincingly.

Will there still be the euro in ten years?

I believe so, yes. The euro is irreversible. Perhaps there will be a different euro, perhaps limited to fewer countries. This I consider possible and it would also be desirable. But it will not cease to exist.

There is always tension between monetary policy and government policy, as was the case during German reunification. At the time, as President of the Bundesbank, you spoke out against an immediate German monetary union. How do you see this now – 20 years later?

The main issue at the time was the D-mark/GDR-mark exchange rate. The experts at the time agreed that a 1:1 exchange rate would be false economically. The correct rate would have been perhaps three eastern marks to one D-mark. But this was unacceptable for Mr. Kohl and Mr. Waigel. They wanted to push through the monetary union and simply overruled me and the Bundesbank. This was one of the reasons I resigned, since it was a policy I couldn't support. Today I realise that there had been enormous pressure. The east German population wanted to finally have the prosperity they had been dreaming about for decades. Just imagine that wages in the east, with an exchange rate of 3:1, would have fallen by around two thirds – there would have been a popular uprising. In this respect political reality was stronger than economic logic.

Looking back on your career, you came a long way from a convinced social democrat to a market liberal ...

I have always been a liberal. Karl Schiller was my great model at the SPD, and he was in fact a liberal. That was certainly possible in the SPD of the 1970s in the social-liberal coalition. The liberals (FDP) had Otto Graf Lambsdorff, who was a friend of mine. I always worked closely with Mr. Lambsdorff and Mr. Genscher, much more so than with some SPD ministers.

The liberal wing of the SPD does not exist anymore, at least not since Wolfgang Clement's withdrawal ...

... which is why I also left the party in 2005. I could no longer identify with the course of the SPD.

With the policies of Mr. Beck and now Mr. Gabriel and Ms. Nahles, it will never win another election. The SPD is out of touch, its programme is no longer in accord with the times. It should be more open economically; it should take a stand on globalization and international competition. But it hasn't done that.

Let's go back again to the 1980s. This was also the time that the course was laid out for the euro in the context of European integration ...

Correct. Helmut Schmidt and Giscard d'Estaing had just set up the European Monetary System (EMS), which called for fixed exchange rates between the countries of the European Community. However, it was a difficult birth. In the 1980s there were eleven realignments in the EMS that is re-evaluations of the exchange rates. In spite of these setbacks, integration made further progress. The Single Market and the Schengen Agreement were realised. This was backed by the insight and political will that Europe can be only be advanced as a joint effort. It's like riding a bike – you have to keep on pedalling because if you stop you fall over.

At the time there were also financial crises ...

I remember there always being crises, since my involvement in government. My first day in the Chancellor's office in 1970 began with Karl Schiller freeing the Bundesbank of its intervention obligation *vis-à-vis* the dollar. I almost had a stroke. I had to explain to Willy Brandt why that was necessary. Then came the European 'currency snake', the forerunner of EMS. It failed because there was always someone who couldn't maintain the exchange rate parity. Then came the EWS with its eleven revaluations. And in 1992, when Mr. Soros was speculating against the pound, the British unfortunately had to leave. There was always some crisis.

Is the current financial crisis fundamentally different?

This crisis has a new quality – only because of its dimensions. This is due to increasing globalisation. The states depend so strongly on each other that undesirable developments are expanded exponentially. Fluctuations become greater. This crisis also accelerates the shifts in the international balance of power. China and India have increased their weight in world politics. The United States with its gigantic mountain of debt has been weakened.

You studied economics in the 1950s. Then John Maynard Keynes was the guru of the economists. Are we experiencing his comeback in the financial and economic crisis?

I don't think that the return to Keynesianism in economic policy will be permanent. At least not to the simple state dirigisme of his time. Just image, in my final examination at the University of Göttingen in 1955 I defended the thesis that the amount of indebtedness is limited by tax revenue. I was given the grade 'good' for this (laughs). Today of course I would not put it that way – and John Maynard Keynes probably wouldn't either.