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Warnings of the Euro – Take 2

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(Work in progress; first and very preliminary version.
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Abstract

Many warnings against the introduction of the Euro that were given before 1999 did not treat the real problems that strained the monetary union (balance of payment crisis, "original sin", speculative attacks on member countries etc.) but others (dangers of inflation due to a weak central bank, dangers of asymmetric shocks, traditional analysis of optimum currency areas, etc.) that turned out to be of only minor importance at best. So the alerters seem, at most, to be right for the wrong reasons.

In this paper the analysis of these warnings which was started in another paper (SCHMIDT 2018) is carried on and widened. The main focus lies on the contributions of the German council of economic experts ("Sachverständigenrat"): in its annual reports the council has stated its opinions concerning exchange rate regimes in general and the monetary system(s) in Europe in particular. It will be shown that the council's analyses are a prime example of concentrating on matters that turned out to be of minor importance in the Euro crisis whereas other topics were not touched upon at all.

Apart from the presentation of the council's contribution, it will be shown that before the outbreak of the Euro crisis some characteristics that turned out to be detrimental for the monetary union were not regarded as a bug, but as a feature. One example are the current account imbalances: these were regarded as beneficial due to facilitated capital imports; the famous Feldstein-Horioka paradox seemed to dissipate and the rising foreign indebtedness of members of the Eurozone experienced a benign neglect. Another example is the fact of the Euro being like a foreign currency from the perspective of the member states; but that the Euro is a "money you cannot make by yourself" was not regarded as problematic but as a progress.

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1. Introduction

"We warned you" – that was a common reaction by many economists when the Euro crisis broke out in 2010 and it reflected their opinion that the profession had hinted to the problematic aspects of the Euro and the organisation of the European monetary union.

But is this opinion really justified? There is no doubt that before the introduction of the Euro many warnings have been issued. But what were these warnings about? Did they hint at the crucial points that became dangerous problems during the crisis and led to the Euro's near collapse?

The central thesis of this paper is that the contents of the warnings that were given before and during the first years of the monetary union did not have much in common with the real sticking points. It will be shown that many economists' sceptical outlooks on the monetary union did not point to the problems that became virulent during the crisis. On the other hand, some characteristics of the monetary union that turned out to be detrimental to the Euro zone were seen as positive and beneficial features.

The paper is the sequel to another one with the same topic (SCHMIDT 2018). That former paper analysed the development of the textbook by DE GRAUWE from the 1st to the current (12th) edition and showed that the problems that were discussed before and during the first years of the monetary union were quite different from the ones that were important in the crisis. Furthermore, it analysed two manifestos in Germany against the Euro and the debate in the *Journal of Economic Perspectives* between CHARLES WYPLOSZ and MARTIN FELDSTEIN.

In this paper the contributions of the German council of economic experts take centre stage. The council is one of the main economic advisory boards in Germany and publishes annual reports presenting the economic situation and discussing economic policy proposals. Section 3 of this paper (after briefly reviewing the causes of the Euro crisis in section 2) gives an overview of the council's deliberations concerning exchange rate regimes in general and the European monetary system(s) in particular. In its discussion of proposals for a monetary union in Europe the council – which from its start in the 1960s was a proponent of flexible exchange rates – mainly focused on the question whether the organization of the EMU was adequate for ensuring price stability; in this connection the council again and again emphasized the (alleged) importance of sound public finances whereas questions of financial stability and the institutions necessary for ensuring it (e.g. a lender of last resort) are notably absent. Section 4 presents some remarkable statements by other economists; here the common theme is that characteristics that became detrimental for the monetary union were not regarded as a bug, but as a feature. One example are the current account imbalances: these were regarded as beneficial due to facilitated capital imports; the famous Feldstein-Horioka paradox seemed to dissipate and the rising foreign indebtedness of members of the Eurozone experienced a benign neglect. Another example is the fact of the Euro being like a foreign currency from the perspective of the member states; but that the Euro is a "money you cannot make by yourself" was not regarded as problematic but as a progress. Section 5 draws some brief conclusions.

2. The Construction Problems of the Euro zone

Which problems were actually relevant when the Euro crisis broke out? I want to sketch this only briefly as these problems were already analysed in very many publications.

- Fiscal profligacy?

The fiscal proflicagy many politicians named as the main culprit was relevant only for one country, Greece. And even here one could say that the amount of government debt would not have been much of a problem if Greece had not been a member of the monetary union. Countries with their own currency did not have the problems the European crisis countries had. On the other hand, Spain was one of the five crisis countries (besides Portugal, Italy, Ireland and Greece) although it had – until 2012 – a debt ratio lower than Germany.

- Diverging competitiveness and differing inflation rates

From the start of the monetary union the competitive positions of the member countries started to diverge. Some countries, especially Germany, had continuous real depreciations vis-à-vis the other countries. A main reason for that were diverging developments of the unit labour costs – they stayed constant or even declined in Germany and rose faster in other countries. As the growth rate of unit labour cost is one of the main determinants of inflation, inflation rates differed: they were below 2% in Germany and above 2% in the southern countries which led to an average inflation in the Eurozone of about 2% but a divergence of competitive positions; that, in turn, contributed to the buildup of large current account balances.

- Original sin and missing lender of last resort

As PAUL DE GRAUWE analysed in the course of the Euro crisis, financial markets were able to force default on member countries they distrust for some reason. The countries hit by this speculation had large current account deficits and negative net international investment positions, sometimes (e.g. Ireland, Spain, Portugal and Greece) 100% of GDP and more. When financial investors started to sell government bonds of these countries it turned out that the Euro has to be regarded as similar to a foreign currency the government has no control of so that the analysis of „original sin“ (EICHENGREEN/HAUSMAN/PANIZZA 2007) which was seen as a problem mainly for developing countries and emerging markets applied also to the countries of the Eurozone. Furthermore, the national central banks could not act as lenders of last resort and end the speculation;finally, with MARIO DRAGHI's speech in July 2012, the ECB accepted this task – which was not seen as a regular task of the ECB before the crisis –, at least reluctantly and with some caveats.

- Missing fiscal capacity on the European level

The construction of the monetary union did not provide for fiscal policy action on the European level. There was neither a European budget that could alleviate local/national shocks to aggregate demand nor European-wide automatic stabilizers – e.g. a European unemployment insurance – that would dampen boom-bust cycles. The countries can only rely on national fiscal policy which underlie severe restrictions. This situation makes it possible that the Euro crisis can come up again as the financial investors cannot be sure that the ECB will always fulfil the role as lender of last resort.

3. The German Council of Economic Experts

> “The German Council of Economic Experts is an academic body that advises on economic policy issues. Set up by law in 1963, it is mandated with the task of providing an impartial expert view in the form of periodic assessments of macroeconomic developments in Germany, thus helping economic policymakers and the general public to make informed decisions. The Council is fully independent in its advisory role and operates in a transparent manner. It describes the current economic situation and its likely future development, highlighting any adverse trends and possible ways of averting or mitigating them. To this end it discusses various indicators of economic output, quality of life, sustainability, and politically defined targets. It also analyses the progress, opportunities and risks of current economic policies and identifies potentially conflicting objectives. The Council’s reports and assessments form a key part of the economic policy debate in Germany and have significantly influenced the political decision-making process.”[1]

Since its set-up in the beginning of the 1960s, the German council of Economic Experts has given many statements regarding the exchange rate system in general and the exchange rate policy in Europe in particular. For a better understanding of the position of the council the following sub-sections report not only the council’s positions closely connected to the European Monetary Union as it was realised in 1999 but start in section 3.1 with its stance on exchange rate systems – the council was an early supporter of flexible exchange rates. The other sub-sections present – in roughly chronological order – the council’s statements on the attempts of exchange rate stabilisation in Europe in the 1970s (3.2), on the European Monetary System (3.3), on the policy after the adoption of the Maastricht Treaty (3.4), on the developments of the first years of the European Monetary Union (3.5), and the proposals for dealing with the crisis (3.6).

3.1 Support for Flexible Exchange Rates

The German council of economic experts[2] started its work in the 1960s, a period with increasing inflation rates within the Bretton Woods system, that is with fixed (but adjustable) exchange rates. Already in its first annual economic report it sympathised – based on a report by FRIEDRICH LUTZ and EGON SOHMEN – with a regime change towards flexible exchange rates: such a system would offer to each country the possibility to go for the economic targets that correspond to its economic and socio-political preferences (annual report 1964/65, p. 134). This support of flexible exchange rates was a common theme in the reports to come. Only in the reports of 1966/67 and 1967/68, the council discussed possibilities of securing internal stability without giving up the system of fixed exchange rates. The remarks about a hardened currency standard (“gehärteter Devisenstandard”) in the report of 1966/67 (p. 147 ff.) show the influence of WOLFGANG STÜTZEL, one of the few economists at that time supporting fixed exchange rates vehemently. But STÜTZEL left the council already in September 1968, supposedly due to irreconcilable differences concerning exchange rate regimes. From then on – although the members of the council change continuously (the regular tenure lasts five years) – the (majority of the) council supports a transition to flexible exchange rates.

1 This information is taken from the Council’s website: https://www.sachverstaendigenrat-wirtschaft.de/en/about-us/objectives.html For further information see the appendix..

2 Appendix 1 cites the objectives and the organization of the council as it is found on its website.

In 1968, the report discusses possibilities correcting the foreign trade disequilibrium. The interesting thing here is that the current account surplus is at about 3% of GDP (annual report 1968/69, p. 22) and is regarded as way too high (the aim at that time was about 1.5% of GDP). Again, the council proposes as one of several possibilities for correcting this imbalance the introduction of a system of flexible current and forward exchange rates. Alternatively – if flexible exchange rates are excluded – the council proposes an increase in the margin of fluctuations (which was 2% in the Bretton Woods System). This increase in margins could be combined with a realignment of parities; the realignment, in turn, could be combined with steps towards a European monetary union but then one would have to check if there is a necessity to change currency relations within the European Economic Community (EEC) to correct the German surpluses vis-à-vis the deficits in other countries of the EEC. The council emphasizes that such a step would force the EEC members into increased cooperation concerning their monetary and business cycle policy (annual repot 1968/69, p. 65 f.).

In 1969, the council makes a counterfactual analysis: what would have happened if the D-Mark had been flexible? (annual report 1969/70, p. 79 ff.) It concludes that a flexible exchange would have had many advantages: it would allow the central bank to concentrate on reaching price stability, it would smooth the business cycle and it would ensure a balance of payments equilibrium. All in all, the council is confident that flexible exchange rates are the best way to enable the attainment of the important aims of economic policy (annual report 1969/70, p. 89 f.). The council makes the case for flexible exchange rates also for Europe: it denies that flexible rates within the EEC could hamper the economic integration, on the contrary: the experience of recent years is said to have shown that sticking to obsolete exchange rates leads to disintegrating interventions in the free movements of goods and capital. One further problem of fixed exchange rates the council treats is the following: if there are inflationary wage increases in a country then the other countries would have to follow immediately. Otherwise, the producers in the other countries would have a cost advantage so that more will be exported to the inflationary country than is justified by longer-term market tendencies. As there will be inflationary adjustment processes in the countries with the temporary cost advantage the market shares in the country leading the inflationary process will be lost again. The council's conclusion: as long as economic policies in the countries diverge, the rigid link of economies via a fixed exchange rate hampers integration (annual report 1969/70, p. 92 f.). Flexible exchange rates might mean more frequent changes but these changes are thought to be small so that divergences in prices and cost are equalised immediately, domestic and foreign prices signal the medium-term equilibrium more clearly, and firms are protected against wrong decisions of their governments (annual report 1969/70, p. 93). According to the council, the disadvantages of fixed exchange rates can only be avoided if economic policy, especially wage policy, is widely harmonised.

This plea for flexible exchange rates is a recurring theme in later reports; in 1971 the council described the tasks an exchange rate system has to fulfil and concludes that, in principle, only a system of flexible exchange rates can satisfy these demands as the Bretton Woods system, according to the council, could not (annual report 1971/72, p. 91 ff.). At first sight, the council states that completely fixed as well as completely flexible exchange rates have their disadvantages, but the proposed system – frequent but small and rules-based parity changes, wide fluctuation margins (that are also sufficient for large differences in business cycles between the countries), scarce special drawing rights, and sanctions in case of breaking the rules – comes quite close to a flexible exchange rate system as the council notes itself (annual report 1971/72, p. 99).

In 1978, the council took a stand concerning the connection between wage policy and exchange rate movements. The reason for this was the fear that flexible exchange rates might foil cost advantages resulting from restrained wages increases. The council stated – which is interesting in light of later developments in the Euro area – that in fixed exchange rate system a domestic cost advantage could easily be transformed in a competitive advantage or a higher profitability. But there could also be an inflation differential (that is: a higher foreign inflation rate) which would be an additional but artificial advantage (annual report 1978/79). The interesting thing here is that the council differentiates between wage-related cost advantages and "artificial" advantages due to inflation differentials. That may be due to the fact that the council – at least at that time – is strictly monetarist: inflation is high or low depending on expansive or restrictive monetary policy; wages are relevant for employment. Therefore, it is not surprising that the council does not relate the appreciation of the D-Mark to restrained wage increases but to a longer-term market assessment of Germany's ability to stabilise the price level; there might be overreactions especially in case of increasing inflation in other countries.

In 1986, the council defends the system of flexible exchange rates against proposals for a system of managed exchange rates. For the council, the main difficulty of such a system lies in the agreement on the parities; furthermore, there is no tie to a standard that could limit the danger of inflation. The council does not regard the EMS that worked rather successfully in the 1980s as a relevant counter-example as the success is mainly due to the German Mark as the stable lead currency that led other countries to adaptations concerning their stability policy (annual report 1986/87, p. 134 f.). Instead of managing exchange rates directly, the council recommends – as always – a reliable and steady economic policy without high budget deficits and without high inflation rates; in that case, large capital movements and sudden changes of exchange rates are not to be expected.

In the 1990s, the council declined all proposals that wanted to introduce target zones for exchange rates or other methods for reducing exchange rate volatility (like a Tobin tax). The basic difficulty with fixed exchange rates, the council states, is the determination of the equilibrium exchange rate which is extremely difficult and might be burdened with political considerations which might, in turn, increase uncertainty and lead to distorted currency relations which could result in speculative attacks. The only way for the council to calm exchange rate volatility is a strictly stability-oriented and – in this respect – credible economic policy which would give orientation to the financial markets; then the resulting exchange rate movements would be guided by the macroeconomic fundamentals; remaining risks can be covered by many ways of hedging (annual report 1995/96, p. 240 ff.). The only alternative would be corner solutions like anchoring a country's exchange rate to another stability-oriented one or the introduction of a currency board (annual report 1995/96, p. 244 f.). This preference for corner solutions is repeated again in 2002; in the same year, the council pleads for introducing a sovereign-debt default mechanism which was proposed at that time by the IMF (annual report 2002/03, p. 311 ff.). This plea were repeated again when reform proposals after the Euro crisis were discussed (see below).

With the onset of the financial crisis in 2007, the council already makes some pleas for a European banking regulation (annual report 2007/08, p. 145).

3.2 Stabilising the Currency Relations in Europe – the 1970s

The comments to a European currency union that was planned at the beginning of the 1970s are characterized by scepticism. Although it is conceded that a European currency block is on equal footing with the United States concerning its economic power, the internal relations are considered as problematic: other countries do not have the same stability tradition as Germany: price stability might range below full employment, as can be seen by looking at the higher inflation rates in other EEC countries (annual report 1971/72, p. 101). Already in 1971, the council confronts two strategies for achieving monetary union (annual report 1971/72, p. 101): on the one hand, the so-called "crowning strategy" views the introduction of a common currency as the final step of a process of harmonising targets and politics in the EEC which makes, in the end, currency relations unnecessary. On the other hand, the "decision theory", as it might be called, emphasizes that harmonisation will not come by ifself but requires a decision to form a monetary union; it irrevocably changes the conditions for political action so that politicians will be eager to quickly realise all working conditions for a smoothly functioning currency union as everybody will understand that harmonisation of important policy fields is a vital necessity. The council does not, in this report, favour one or the other strategy, but it emphasises the freedom of capital movements as a necessary foundation of a monetary union, regardless which strategy is chosen (annual report 1971/72, p. 101). This support for completely free capital movements can be found again and again in later reports.

Already one year later, the council states that, with the reduction of the fluctuation margins the EEC has taken up more than it was willing to bear as it (re-)introduced capital controls when the Italian Lira got weaker. The council emphasized that small margins and free capital movements would enforce a common monetary and credit policy; the freedom of capital movements is a necessary condition for a monetary union, or even more, it is what the whole monetary union is about ("sie [freedom of capital movements] ist eigentlich die Sache selbst" [annual report 1972/73, p. 112). Furthermore, according to the council, the currency union cannot succeed when there are different national priorities regarding economic aims and the control of aberrations (annual report 1972/73, p. 121). In the end, if there is no agreement on an adequate stability policy then it would be better to go for a union with free capital movements and a degree of exchange rate flexibility that matches the lack of discipline; the successes concerning European integration might be greater (annual report 1972/73, p. 177).

In the 1970s, the council is quite reluctant when assessing the progress in stabilising the currency relations in Europe. It is more focused on defending the worldwide "system" of flexible exchange rates against arguments doubting its usefulness and stability. The common theme of the council's argumentation here is that the seeming instability of flexible exchange rates mainly comes from the instability and the lacking consistency of economic policy. If the states, so the argument goes, followed a policy of stability-oriented, foreseeable and consistent economic policy, stable exchange rates would result, as the economic actors are able to build stable exchange rate expectations. Transitory problems should not be a reason for abolishing flexible rates (annual report 1974/75, p. 21) as they make life easier for monetary policy and allow to have inflation rates different from other countries (annual report 1974/75, p. 165). All in all, the council seems to be convinced that, at least in the long run, exchange rates move according to the purchasing power principle. This support for flexible rates is repeated in later reports: the council sees the large fluctuations but explains them with the lacking practice with flexible rates and reminds the politicians that a convergence in economic policy is the right way to stabilise exchange rates and exchange rate expectations (annual report 1975/76, p. 166); concerning the block of European currencies the council emphasises the importance of a downward alignment of inflation rates (annual report 1975/76, p. 165).

In the mid and late 70s, the council makes the case for an independent monetary policy, combined with a plea for (medium-term) monetary targeting: the money supply should be externalised and "detracted from the plebiscite of the day" (annual report 1976/77, p. 178).

3.3 The European Monetary System

In its first assessment of the plans for the European Monetary System (EMS) the council remains sceptical. On the one hand, fixed exchange rates might increase the national autonomy concerning employment policy: Restrained wages and cost-dampening supply-side policies would no longer be hampered by flexible exchange rates; an improvement of a country's competitiveness could now only be compensated by an equivalent slowing of foreign increases of costs and prices. The possibility to reach a competitive advantage not only on the level of firms or sectors but also in the whole sphere of foreign trade could lead, according to the council, to a stimulation of the international competition for stability and growth (annual report 1978/79, p. 154 f.) – which is regarded as unambiguously positive by the council. On the other hand, the council distrusts the rules for mutual assistance and obligatory interventions on the foreign exchange market: they might lead to too expansive increases of the money supply especially in the countries under revaluation pressure and, in the end, an alignment of inflation rates on a medium level instead of the lowest one (annual report 1978/79, p. 155). Furthermore, if there is no inflationary pressure on countries with low inflation rates the most stable currency in the EMS would take a leading role as without binding agreements on the harmonisation of monetary policy an anchor currency would be indispensable for the operativeness of the EMS – but then it might be the case that such a system cannot be assigned to a group of countries that include partners that are seen as equals (annual report 1978/79, p. 155). But all in all, the council thinks that the hope for a harmonisation of monetary policies is – at the beginning of the EMS – unfounded; the initial situation is rather worse than at the beginning of the 1970s, mainly due to higher inflationary differences (annual report 1978/79, p. 159 f.).[3] Therefore, the council recommends – if a common currency is strived for at all – a market-driven gradual process of currency substitution: the common currency could then firstly be used by those actors looking for a protection against decline of their national currencies and against the risks of inflation and depreciation and where national monetary and exchange rate policy is regarded as practically ineffectice in influencing employment.

Whereas in 1982 the council still criticised the differences in inflation rates as a source of necessary realignments (annual report 1982/83, p. 31) there were practically no negative comments

[3] This assessment is repeated one year later (annual report 1979/70, p. 137).

in the following reports, and the council had to concede in 1986 that the EMS was quite successful – but more or less only due to the anchoring function of the German Mark. One year later, it rejected the criticism that Germany's monetary and fiscal policy was too restrictive: while conceding in general that an excessive policy of restriction by a dominant member country might endanger the coherence of the system the council denied that Germany followed such a policy path in the mid-80s.

When the discussion about introducing a common European currency gained momentum, the council warned against a quick fixation of exchange rates (annual report 1988/89, p. 166). It would be much more important to reach a convergence of monetary policy (subject to price stability); here the council emphasises the importance of an independent monetary policy. Apart from that, the council pleads for a convergence of fiscal policy in the member states: it sees the willingness to give up sovereignty in the field of public finances as a test case for the willingness to go for a political union. The council does, at this stage, state nothing concerning fiscal policy on the European level, but in any case it does not seem to see a role for national fiscal policies; furthermore, the differences concerning budget deficits and debts are seen as major burden: as inflationing away the debt is excluded in a monetary union, that could mean transfers from countries with lower debts and deficits – a perspective the council disapproves of as long as the political union is not established; for the council in 1988, the willingness to such a union cannot be enforced by fixing exchange rates prematurely. The completion of the internal market is seen as one important step in the dirction of political union; but for this, spectacular decisions concerning currency policy are not demanded. Instead of that, a complete and irrevocable liberalisation of capital movements as well as a more intensive coordination of the monetary and fiscal policies of the member states should be strived for – always subject to the primacy of stability.

In 1989, after the publication of the Delors report, the council warns against precipitate steps especially concerning the fixation of parities: during the transition process, the instrument of realignments is still needed. On the one hand, the stability of parities since the beginning of 1987 has put pressure on some countries that enabled them to reduce their inflation rates. But other countries have still higher inflation and higher interest rates which has led to large capital movements to these countries: in the end, a large pressure for adjustment has accumulated which might lead to massive speculative capital movements and a realignment (annual report 1989/90, p. 181). For the council, the function of the German Mark and the Bundesbank as anchors for stability is still essential; it pleas for the independence of all other European central banks and a "stability competition" between them – only that could make the German anchor dispensable.

Additionally, the council starts to focus on the role of budget deficits and debt. Both are, according to the council, important for the solvency risk of a country: it increases with rising deficits and increasing debt, if interest payments make up already a large part of the budget (annual report 1989/90, p. 184). As the exchange rate risk decreases – the EMS will try to introduce realignments more and more infrequently – the pressure for a convergence of inflation rates will increase. But that, in turn, bears the danger that the level of inflation in Europe will increase as some member states still have high budget deficits and let them finance by loans from the central bank. Therefore, the council demands a prohibition of (direct) monetisation of budget deficits. That prohibition introduces limits for the deficit-financed spending of goverments which could force them to undertake unpopular measures: but instead of that, there is the danger that there might be a pressure on other countries to introduce financial help for supporting the consolidation process in the highly-indebted countries. As the high deficits and debts might also absorb savings of other countries investments in those other countries might be hampered.

For all of these reasons the council demands rules for the budget policy of the member states of the EMS and the prospective members of the monetary union: limiting the deficits to the amount of net investment is not enough for the council; there must be rules that take account of the business cycle. In a boom it would not be wise to use the scope for deficits limited to the amount of net investment, due to a transgression of the productive potential, whereas in a self-enforcing recession it might be necessary to go beyond that limit (annual report 1989/90, p. 185 f.). But this seeming plea for an active fiscal policy is immediately taken back as the council states that the pretense of managing the business cycle must not be a gateway for an amount of government debt that endangers stability; furthermore, the scope of investment expenditures is difficult to define. Therefore, the council demands rules that are easy to handle and they should start with the assessment that, in general, restrained financing via credit is less harmful than a careless one: the rules should include percentaged shares of public investment or of GDP as limits for public deficits, and there should also be limits on the stock of government debt as a share of GDP; furthermore, financing public deficits via the central bank should be forbidden (annual report 1989/90, p. 186).

The council also distrusts financial markets as fulfilling the role of guardians of sound finances adequately. For the council that results from the promise of fixed exchange rates. If financial markets see that countries have current account deficits and levels of private and/or public consumption that are too high in the long run and would require a realignment of parities they should not move capital to those countries in the first place. But the strict rejection of realignments by the political and monetary authorities would, nevertheless, tempt financial actors to invest in these countries as they hope to get out again in time or that the central banks will defend the parities (annual report 1989/90, p. 187).

In later reports, the strict orientation on price stability gets more intensified. In 1990, the council supports the aim for an extensive monetary and real convergence of the European states before introducing irrevocably fixed exchange rates or a common currency; furthermore, the internal market has to be finalised including freedom of capital movement; the completion of these requirements has a strict priority over reaching deadlines (annual report 1990/91, p. 223 f.). The German Bundesbank and its structure is, in principle, seen as a role model for the prospective European Central Bank; the most important requirement is its independence. The council rejects all proposals for wider-ranging coordination of macroeconomic policies as that would lead to guidelines for the central bank and, finally, weaken or even abolish its independence. Even the proposal for a "support of general economic policy" is seen as problematic (although a similar assignment could be found in the German Bundesbank law) as the tradition of stability in Europe is not as pronounced as in Germany. In the same report, the council discusses the need for fiscal rules; the argument that high deficits of a country would increase the risk premia and therefore the interest rate the country has to pay and that these higher interest rates would lead to a moderation of deficit finance is rejected. On the one hand, the council doubts that – due to the duration of the average credit being longer than a legislative period – politicians can really be deterred from excessive deficits by high interest rates. On the other hand, high deficits in large or many countries could lead to an increased pressure on the European Central Bank to loosen its monetary policy; and the council regards it as unrealistic to believe that the bank could elude this pressure despite its formal independence. Therefore, rules for deficits (e.g. linking deficits to the amount of investment) are necessary (annual report 1990/91, p. 226). Transfer payments within the prospective monetary union are declined: the benefit from joining a monetary union is the advantage of a common and stable currency; there are no disadvantages that would justify financial compensations. Of course, according to the council, the abandonment of the exchange rate mechanism requires flexibility of other economic variables, e.g. wages. But if this flexibility cannot be achieved, the country should not join the monetary union (annual report 1990/91, p. 227).

In its report of 1991/92, the council repeats its demand for a strict stability orientation of European monetary policy; the European Central Bank must not have an aim apart from price stability and the prospective countries must obey strict criteria concerning public deficits and inflation rates (annual report 1991/92, p. 213 ff.). In the same year, with the approval of the Maastricht Treaty, the increase in capital mobility, and the planning of the Monetary Union, the council points out the new conditions for wage policy (annual report 1991/92, p. 202 ff.): wage increases in Germany must consider the possibility of relocations of capital to other countries in case of excessive wage increases; there is no longer only a domestic stability conflict but also a conflict between locations. Furthermore, other European countries – the council mentions France, Denmark and Ireland – have seen lower increases of unit labour costs, sometimes even lower than in Germany. This necessary flexibility is mentioned again in 1997 (annual report 1997/98, p. 201 ff.).

3.4 After Maastricht

As the German Bundesbank increased interest rates after German unification a conflict broke out between the (perceived) domectic need of higher interest rates and its effect on other European countries. But the council thinks that the Bundesbank must not weaken its restrictive course only because of the external effects; rather the domestic inflationary forces have to be pushed back so that there would no longer be a reason for a restrictive course (annual report 1992/93, p. 200). In the same report, the council – albeit reluctantly – lauds the stability criteria in the Maastricht Treaty; especially, it praises the result that quantitative factors objectify the assessment whether the policy of the member states is consistent with stability requirements. On the other hand, the convergence concerning real variables (development and productivity) cannot be derived from these nominal criteria but that is important as a monetary union of countries with different levels of development would increase the pressure for expansive monetary policy and financial transfers – two things the council strongly declines (annual report 1992/93, p. 237). Furthermore, it praises that the Maastricht Treaty does not demand that the European Central Bank supports the general economic policy of the Union, particularly if that would endanger price stability (annual report 1992/93, p. 239).

Against the background of the crisis in the European Monetary System and the enlargement of the fluctuation margin (+/- 15%) in 1993, the (majority of the) council makes now an interesting turn: since its setup, the council was a defender of flexible exchange rates and only a reluctant supporter of the system of fixed but adjustable rates in Europe; now it pleaded for the accomplishment of the European Monetary Union. The reason is that the council fears a re-nationalisation of economic policy when countries have a degree of freedom concerning the exchange rate which might lead to competitive devaluations; that would endanger the steps of European integration accomplished so far. The council sees that the free movement of capital might lead to expectations of exchange rate changes that are not connected to economic fundamentals. But the conclusion is not that capital movements should be re-regulated or restricted; rather, the potentially destabilising effects of unrestricted capital movements and the speculative attacks that are connected with them can be controlled only by a radical step: the transition to the European Monetary Union (annual report 1993/94, p. 233)[4] The interesting turn is that, in earlier reports, the council regarded free capital movements as a necessary condition for forming a monetary union; now the monetary union is the necessary answer to get the speculative capital movements under control.

In the reports of the years before the start of the monetary union, the council mainly emphasises the necessity of a strict application of the criteria for joining the monetary union, especially the inflation and deficit criteria, without margins of discretion (annual report 1995/96, p. 246 ff.; 1996/97, p. 214 ff.) and sanctions that should be applied more or less automatically should the criteria be breached; the sanctions should be equal to an interference with the sovereign rights of a country (annual report 1995/96, p. 255; 1996/97, p. 157).

On the cusp of monetary union, the council again emphasised stability orientation as the conditio sine qua non of European monetary policy and recommends a monetary targeting; the – at that time – quite new policy of inflation targeting is met with scepticism (annual report 1997/98, p. 221 ff.). One year later, the council again recommends a objectivation of the money supply and pleads for an adherence to rules, preferably monetary rules (under the assumption that the money demand function is stable); furthermore, the council still emphasises the necessity of consolidation of public budgets (annual report 1998/99, p. 179 ff.).

In the same report, the council deals with apprehensions that there is a deflationary danger in the Eurozone due to a possible downward spiral of wages. The council declines this and states that such fears are misplaced and that the idea of a downward spiral is fanciful (annual report 1998/99, p.178). It concedes that jobs within the monetary union compete more intensively due to higher transparency of prices and costs but that there is no danger of a downward spiral: a restrained wage policy just means wage increases below the productivity increase to create more jobs; if that is accomplished and the unemployment has gone down then the competition for workers will make sure that wages rise according to productivity again. Furthermore, changes in the real exchange rates within a monetary union will take place: when a country has got into a crisis this real depreciation (via restrained wage increases or even wage reductions)

[4] One member of the council, Horst Siebert, objected to this majority opinion and did not regard the danger of a re-nationalisation as very important. Concerning the speculative capital movements, Siebert holds the view that the economic policy must be shaped in a way so that markets do not see a discrepancy between currency relations and real economic facts – he seems to think that this is possible. For him reaching a real convergence is necessary condition for monetary integration (annual report 1993/94, p. 233 ff.).

will bring a new macroeconomic equilibrium; when that is reached there will be no need for further changes and therefore there will be no downward spiral (annual report 1998/99, p. 196 f.). One can see here that the (majority of the) council locates the reason for unemployment nearly exclusively in wage policy.

3.5 The First Years of the Monetary Union

After the start of the monetary union, the council mainly discusses the monetary policy strategy of the European Central Bank, emphasising the necessity of a credible course, again demanding a clear monetary target and declining a role for the ECB in business cycle policy (annual report 1999/2000, p. 148 f.). Furthermore, fiscal policy is a recurring theme in these years, emphasising the importance of consolidation of public budgets. In this context, the council discusses intensively the importance of non-keynesian effects of discretionary policy which again is an argument for consolidation (annual report 2003/04, p. 443 ff.). Insisting on a strict adherence to the stability pact is a kind of *ceterum censeo* in the coucil's reports in this decade. Even in 2009, during the financial crisis and on the cusp of the Euro crisis, the council still pleas for consolidation of public budgets and regards balanced budgets as a longer-term goal (annual report 2009/10, p. 82 ff.).

In several reports, the council discusses problems that came up in the first years of the monetary union, but it did not draw the conclusions that would have been necessary concerning the development of the Euro crisis:

- Persistent inflation differentials
  - Already in 1999, the differing development of the price levels in several Euro countries is mentiond. That phenomenon and its persistence is discussed again in 2001. Insofar as these differing inflation rates are caused by differing positions of the countries in the business cycle, the council sees them as positive, as they are automatic stabilisers; the persistence is regarded as a potentially greater problem but the council does – at least in 2001 – neither connect it to current account imbalances nor to wage policy. The Balassa-Samuelson effect that explains differing inflation rates in countries is seen as not very important for explaining the differences within the Euro zone (annual report 2001/02, p. 267 ff.).
  - In 2002, one of the members of the council, JÜRGEN KROMPHARDT, connects the developments of prices and wages in a minority vote: he mentions the problem that a restrictive wage policy in a member state of the monetary union might lead to an inflation rate below the average of the union. As nominal interest rates are the same in all countries the real interest rate in the low-inflation country is higher than in the other countries and burdens investment in the low-inflation country. Problems concerning the competitiveness of countries are not mentioned yet (annual report 2002/03, p. 271).
  - In 2005, the council treated the problem once more and listed several reasons for differing inflation rates. Besides other points (Balassa-Samuelson effect, cyclical shocks, changes in indirect taxes, different consumption baskets when calculating inflation, different external linkages, heterogenous development of real estate prices, differing product market regulations) the differing developments of unit labour cost were mentioned, and the council even stated that unit labour cost were more important than other

points. However, the council did not criticise that unit labour cost in Germany increased insufficiently but it only mentions that Ireland, Portugal, Spain and Italy had deteriorations of the cost competitiveness and had also inflation rates above the Euro zone average (annual report 2005/06, p. 422).

- Current account imbalances
  - Interestingly, the council states as one of the positive effects of the common currency that all benefits of a restrained wage policy are no longer nullified by appreciations (annual report 2005/06, p. 408 f.). That can be interpreted as a calling for further wage restraint and indeed, even in 2009, the council recommends that the bargaining partners should continue with the non-exhaustion of the margin of distribution, that is to agree on nominal wage increases below the sum of productivity increase and inflation target of the central bank and so to contribute to the creation of competitive jobs; the council even warns of demands to diminish the export dependency of the German economy as the jobs in the export sector that cease to exist would only be incompletely substituted by domestic sectors (annual report 2009/10, p. 280).[5]
  - Also in 2005, the council discusses the problems resulting from differing inflation rates in terms of competitiveness. But the council does it by confronting two transmission channels through which differing inflation rates affect the countries of the monetary union: the real interest rate channel enforces the diverging developments of the countries as a higher inflation rate (which signals an overheated economy) means lower real interest rates and therefore an additional stimulus; on the other hand there is the competitiveness channel: the higher inflation rate means a real appreciation; as these changes accumulate over time, this channel is regarded – at least in the long term – as an effective adjustment mechanism that precludes a destabilisation of the currency union due to differing inflation rates (annual report 2005/06, p. 420 ff.). Five years before the crises, the council is quite optimistic about the self-regulation of current account deficits; there is no need to undertake specific measures. The degree to which current account deficits that are unsustainable in the long run can be financed within a currency union are underestimated by far.
  - One year later, the council discusses current account imbalances again – not only within the Euro zone, but on a global level. But the discussion is focussed on the current account deficit of the US (the issue of private indebtedness in the US is broached) and the council discusses the risks for an export-oriented economy like Germany (annual report 2006/07, p. 156 ff). The council sees the main responsibility in the field of the United States and the Asian countries; furthermore, a recovery of domestic demand in Europe could be helpful, but German wage policy is not discussed as a possible contribution to that (annual report 2006/07, p. 160 f.).

[5] Only one member, Peter Bofinger, rejects this recommendation in a minority vote (annual report 2009/10, p. 299 ff.)

3.6 The council during the crisis

With the outbreak of the Euro crisis the council suddenly discusses all the points that have been come up as important causes of the Euro crisis and that were briefly summarised in section of this paper:

- The current account imbalances and the large financial balances in the private sector that caused them (annual report 2010/11, p. 71 ff.)
- The problem of "original sin" so that the Euro is a foreign currency when looked at from the perspective of a single member country (annual report 2010/11, p. 81 ff., annual report 2011/12, p. 93 ff.)

But interestingly, the reform proposals that the council derives from this analysis are still not very different from its former stance. So the council does still sees consolidation of public budgets as important; it does not think that are more expansive fiscal policy or larger wage increases, especially by Germany, could play a role in bringing down the imbalances (annual report 2010/11, p. 111 ff.); it still emphasises the intertemporal approach when looking at the balance of payments and does not see large current account deficits as necessarily problematic as they can be a sign of a country being a very attractive investment location with a high growth potential (annual report 2010/11, p. 107) and it still favors introducing a sovereign debt-default mechanism within the Euro zone and a stronger stability pact whereas it rejects the introduction of a common fiscal capacity and of common bonds due to the risk of moral hazard (annual report 2017/18, p. 55).

4. Characteristics of the EMU: Features or Bugs?

4.1 Barry Eichengreen and the Improbability of Government Default

In the years before the start of European Monetary Union, Barry Eichengreen has analysed several of its problems in about a dozen papers. They were collected in Eichengreen (1997). The majority of them deals with aspects familiar from the theory of optimum currency areas: labour market flexibility, the problem of asymmetric shocks, the exchange rate as an instrument for adjusting relative prices and so on. But two papers in the collection are quite relevant for our question at hand: one deals with the EMS crises at the beginning of the 1990s, the other one treats the necessity (or redundancy) of the stability pact.

In the paper "The Unstable EMS" Eichengreen/Wyplosz analysed the crises of the European Monetary System at the beginning of the 1990s. Their conclusion is that the crises cannot be fully explained by a recourse to the economic fundamentals (although they do play a role); so the first-generation models of currency crises that explained them as a result "when fundamentals (inflation, the real exchange rate, the budget and current account) are out of line" (Eichengreen 1997, p. 5) are insufficient but the second-generation models are helpful as they show that "attacks con occur and succeed even in the absence of any ex ante imbalance in fundamentals. If the government and central bank respond to the crisis by abandoning their defence of the currency peg and relaxing policy, then a speculative attack can be self-fulfilling" (Eichengreen 1997, p. 5).

As a result of their analyses EICHENGREEN/WYPLOSZ forecast (in 1992) further currency crises in case the political/institutional framework does not change. As possible remedies they discuss: more frequent realignments; a faster rush to monetary union, possibly only with a core of countries; more exchange rate flexibility; throwing sand in the wheels of speculation, e.g. by a kind of Tobin tax. EICHENGREEN/WYPLOSZ see more realignments as problematic given that capital movements are completely unrestricted and that markets tend to anticipate future events. "Central banks that believe they can peg the exchange rate for significant periods and then change it discretely overlook this elementary fact" (EICHENGREEN/WYPLOSZ 1993, p. 207). A faster rush to monetary union is seen as improbable as strong-currency countries would not allow it if the other candidates do not fulfil the convergence criteria (which seemed not to be very plausible in 1992/93). Although EICHENGREEN/WYPLOSZ think that more exchange rate flexibility is anathema for many actors in Europe as it threatens to destabilise the common market that was exactly the measure decided by the members of the EMS (increase in the fluctuation margin to +/-15%). In contrast, EICHENGREEN/WYPLOSZ (1993, p. 215) at that time favoured the introduction of some kind of Tobin tax to contain excessive speculative movements.

What is interesting in this analysis is the authors' (albeit implicit) assumption that going for full monetary union would end speculative currency crises. That financial markets could go for the government bond markets instead and force governments into default was seen as outside the spectrum of imaginable possibilities.

In another paper, EICHENGREEN/VON HAGEN (1996) give the answer why they think that default of one of the prospective member states of the EMU is improbable. The topic of the paper is the fear that countries that borrow unsustainably (however defined) would be in danger of getting into a debt crisis which in turn might lead to a bailout (carried out by the European Central Bank via inflation); the excessive deficit procedure of the Maastricht Treaty was introduced as a measure to preclude such a development. But EICHENGREEN/VON HAGEN regard this mechanism as superfluous. The reason they give for that lies in the member states' power to tax. As long as member states control their own tax base the reaction to a debt crisis does not need to be either bailout or default, but increase of taxes. When member states are able and also expected to do that the pressure for a bailout can be resisted. Furthermore: "That the cost of coping with the crisis will be borne by the member state itself, in the form of higher taxes, will limit moral hazard." (EICHENGREEN/VON HAGEN 1996, p. 243).[6] Obviously, the speed at which financial markets could enforce the default of governments so that there is – at least in a democracy with its inherently slow decision processes – practically no chance for tax rises was not foreseen by the authors.

66 Apart from that, EICHENGREEN/VON HAGEN point to the problem that fiscal restrictions like the stability pact may even lead to an increase of fiscal competences on the European level that many of the proponents of the restrictions like to avoid. The reason is: (Partially) stripped of their capacity of tax-smoothing will demand it from the European level. "This suggests that the Excessive Deficit Procedure may spur the creation of a system of fiscal federalism in which Brussels collects taxes and provides transfers to member states in amounts that increase, say, with the level of unemployment. And because the member states will resist giving up their tax revenues as quickly as they demand additional services from the EU, the financial position of the latter will deteriorate." (EICHENGREEN 1997, p. 8)

4.2 Current Account Imbalances

With the start of the Euro, the current accounts of the member states of the EMU started to show growing surpluses and deficits. With hindsight, we know that these current account imbalances were one of the problems causing the Euro crisis as countries with current account deficits (that translated into growing negative net international investment positions) were the victims of speculative attacks or sudden stops concerning capital flows: on the government bond market current yields increased sharply as financial investors sold off bonds. The cause for that was not (maybe except the case of Greece) unsustainable public debt but large private debt that led to large current account deficits; the government bond market served as kind of a valve where the financial investors' panic showed up.

But the interesting thing is that these current account deficits were not seen as a major problem when they started to come up. One example for that is a paper by BLANCHARD/GIAVAZZI (2002) about current account deficits in the Euro area. In this paper, they focus on the current account deficits of Portugal and Greece and try to find an explanation for them. Their basic message is that there is no need to worry and that benign neglect might be the best answer to it. Portugal's and Greece's current account deficits

> "are exactly what theory suggests can and should happen when countries become more closely linked in goods and financial markets. To the extent that they are the countries with higher expected rates of return, poor countries should see an increase in investment. And to the extent that they are the countries with better growth prospects, they should also see a decrease in saving. Thus, on both counts, poorer countries should run larger current account deficits, and, symmetrically, richer countries should run larger current account surpluses." (Blanchard/Giavazzi 2002, p. 148)

Using the model of intertemporal optimization of the representative consumer, BLANCHARD/GIAVAZZI build a model for explaining the deficits and attribute them to European integration. This integration process has, according to the authors, led to three effects that resulted in less saving and more investment in these countries and therefore higher current account deficits. First, the goods market integration (the single European market) led to an increase of the elasticity of demand for each good: harmonization of safety requirements and the more extended distribution networks made goods closer substitutes for each other. "As a result, goods market integration has reduced the adverse terms-of-trade effect a country faces, when it needs to generate a current account surplus to repay its debt, and this has made borrowing more attractive." (BLANCHARD/GIAVAZZI 2002, p. 153). Second, financial integration has reduced the rate at which prospective debtors can borrow; due to the harmonization of financial market rules the regulatory uncertainty foreign lenders face has been reduced and the transparency of information on potential borrowers has been increased, reduding risk premia. (BLANCHARD/GIAVAZZI 2002, p. 153). Third, monetary union has eliminated the currency risk which further reduced the risk premium lenders demand; in addition, it has led to deeper and larger capital markets. These developments make borrowing more attractive but could also lead to more investment. The reason for that – apart from lower cost of finance – is: "the higher the elasticity of demand, the smaller the decrease in price needed to sell the additional output in the future, and so the more attractive investment is in this period." (BLANCHARD/GIAVAZZI 2002, p. 154) And as poor countries have less capital, the marginal product of capital will be higher which also makes investment more attractive.

BLANCHARD/GIAVAZZI state that this increased integration leads to a decrease in the correlation between national saving and national investment, thus dissolving the decades-old Feldstein-Horioka puzzle of high correlations between these two variables; savers can look for the best way of allocating their savings and are no longer confined to the national capital market. Therefore, there is no need to actively intervene in this process (BLANCHARD/GIAVAZZI 2002, p. 183 ff.)

With hindsight, one can say that the whole idea that current account deficits for poor (or developing) countries did not fulfill its promises. Historical experience tells us that all successful processes of catch-up and development were closely connected with current account surpluses – China only being the latest example for that. Rightly, the European Union now takes a closer look to current account imbalances; the benign neglect only led to problems that emerged abruptly in the Euro crisis but were not seen before. One reason for that was that only public debt was seen as a potential problem – also BLANCHARD/GIAVAZZI state that

> "if these current account deficits had their origin in large fiscal deficits, issues of intergenerational distribution would obviously arise. Greater government debt would mean higher taxes in the future, and thus a larger burden on future generations. But in this case the issue is moot: as we have seen, the current account deficits have their origin in private saving and private investment. The consumers taking out mortgages in Portugal are the ones who will have to repay them, not future generations. They may be too optimistic about their future income prospects, but we do not typically think of this as a reason for macroeconomic policy intervention." (BLANCHARD/GIAVAZZI 2002, p. 184)

4.3 A Money You Cannot Make by Yourself

One of the problems that became visible during the Euro crisis was that from the perspective of a single member country of the EMU the Euro is a foreign currency as it cannot be created by the national central bank which, as a result, cannot act as a lender of last resort on the government bond market. This was the central difference to countries with their own central bank like Great Britain or the United States who were not hit by a crisis in the government bond market.

But exactly this problem of the monetary union was seen – at least by some economists – as one of the main features of the monetary union. In section 3 it was already shown that the German Council of Economic Experts seemed to have some sympathy for an objectivation of the money supply and that governments should not be able to produce money at their will. But other economists expressed this more openly. One example is OLAF SIEVERT, himself a former member of the Council of Economic Experts. His main argument in favour of the European monetary union (SIEVERT 1993) is indeed that the prospective member states of the European monetary union want to introduce a money that they can´t make by themselves. And this decision is seen as beneficial in nearly every aspect. On the other hand, the history of monetary relations is, according to SIEVERT, a history of the improper use of the right to create money: using benefits one is not entitled to by spending money one does not have but can create (so that the income and wealth made that way do not have any real foundation and are therefore created at the expense of others) and by voiding debt one had promised to pay back with sound money. SIEVERT lauds the gold standard period which precluded all these abuses and he thinks that the monetary union comes close to this "golden" period of monetary history (SIEVERT 1993,

p. 14)[7] He takes this argument one step further by saying that also the incompleteness of the monetary union – a common currency without a common budget and, of course, without a central state – is in fact also a feature, a benefit, and he would regard it as a mistake to go for a full political union as a unitary state or a federal state are much closer to the central bank than the members of a federation of states (SIEVERT 1993, p. 15).

In his paper, SIEVERT makes other claims concerning the benefits resulting from a monetary union: the labour markets in the union will become truly competitive markets, and as the responsibility for price stability is clearly assigned to the European Central Bank, then wage policy must accept its responsibility for employment: nominal wages are also real wages as the monetary conditions that determine inflation are no longer changed according to the wage policy in the member countries (SIEVERT 1993, p. 17). And as changes of the exchange rate are no longer possible and unions cannot hope that the central bank will act inflationary that will act as an effective barrier against false wage policies.

The astonishing thing is that SIEVERT obviously sees no necessity for any safeguards as, for example, a lender of last resort. For him it seems to be obvious that crises are the result of unsustainable and irresponsible behavior by governments and that the incentives for such an irresponsible behavior can be removed by introducing a money you cannot make by yourself. Similarly, one is puzzled about his unrestricted support for the gold standard when at about the same time EICHENGREEN (1992) showed that the adherence to the gold standard *do or die* intensified the depression in the 1930s. And what is seen now as one of the great design faults of the monetary union – that there is no lender of last resort and that the problems are similar to that of the gold standard era – was seen as one of the great features of EMU.

5. Conclusion

The paper has shown that many discussions about the European Monetary Union before its start focussed on the one hand on problems that did not become very important during the crisis. The German Council of Economic Experts focussed on the possible dangers for price stability when Germany loses its role as stability anchor within the European Monetary System. It insisted on the strict application of the convergence criteria and was practically blind for the problems that really came up during the crisis. And even after the crisis broke out and the council's analyses made some important points it still shows a nearly stubborn adherence to questions of sound public finances and consolidation without admitting the necessity of a lender of last resort (on the government bond market) or a fiscal capacity on the European level; instead of that, the introduction of a sovereign-debt default mechanism is demanded.

[7] In the original: „Die Geschichte des Geldwesens ist nicht eine Geschichte der Entwicklung hin zu immer besserem Geld. Sie ist vor allem eine wechselvolle Geschichte der mißbräuchlichen Nutzung des Rechts, Geld zu schaffen: Handlungsmöglichkeiten und Vorteile gewinnen und nutzen, die einem nicht zustehen, indem man Geld ausgibt, das man nicht hat, aber herstellen kann, indem man Einkommen und Vermögen entstehen läßt, für die es eine reale Grundlage nicht gibt, die also, wenn überhaupt, nur auf Kosten von anderen gewonnen werden können, und – nicht zuletzt – indem man Schulden entwertet, die mit gutem Geld zu bezahlen man versprochen hat, kurz, Lug und Trug im Gewande staatlicher Hoheit, das hat über die Jahrhunderte die Attraktivität der staatlichen Souveränität über das Geldwesen ausgemacht. Man kann eine internationale Geldordnung haben, und es hat sie gegeben, wenn auch nur eine Zeitlang, während des fast weltweit beachteten Goldstandards nämlich, mit der alledem Einhalt geboten wird. Eine seltene, wenn nicht einmalige Konstellation scheint dies in Europa neuerlich möglich zu machen." (SIEVERT 1993, p. 14)

On the other hand, one can find analyses before (and shortly after) the start of the EMU that emphasise supposed features and benefits of the monetary union that turned out to be its greatest faults: the formation of current account imbalances and the fact that the Euro is a foreign currency from the perspective of a single member state.

When one tries to give a short summary about the contents of the warnings that were given before the start of the Euro, one could state: the alerters were afraid of a monetary union that threatened to undermine the alleged conditions for general prosperity: free markets, sound money, and balanced public budgets. Nearly all of the warnings either mentioned the seemingly serious – for some commentators: the central and overarching – problem of increasing inflation, the pitfalls of overly excessive fiscal policy or the danger of a central bank giving in to (unwarranted) demands for expansive monetary policy. One is puzzled by the authors' confidence that market processes will lead to a beneficial outcome and that there is no necessity to make provisions for the possibility of a major crisis. If you strive for stability, everything else will fall into place.

Of course, it might seem smart-alec to criticise with hindsight that economic experts did not point to the real problems of the Euro zone; but the fact that at least some economists – often rather heterodox ones – pointed to real problems (e.g. GODLEY 1992) should lead to questions whether the perspective was really adequate. At the very least, the failure of tackling the real problems in advance should lead to an intellectual modesty.

Appendix: Additional information on the German Council of Economic Experts[8]

The following is a list of the Council's individual tasks according to its legal mandate:

- Analysing the current economic situation and its likely development.
- Examining ways and means of ensuring steady and adequate growth within the framework of the free market-economy system, whilst simultaneously maintaining high employment, price stability and a foreign trade equilibrium.
- While taking into account the accumulation and distribution of earnings and capital.
- Pointing out the causes of current and potential conflicts of macroeconomic demand and supply.
- Pointing out undesirable developments and examining ways and means of avoiding or eliminating these without suggesting specific economic or socio-economic measures.

In line with its legal mandate, the Council compiles and publishes an Annual Economic Report which is released in mid-November. In order to assess particular current problems and depending on the mandate issued by the government, the Council also prepares ad-hoc Special Reports. Since 2005, the Council has also been releasing Occasional Reports on selected topics upon the request of the Federal Government. Since 2014, the Council has additionally published annual economic forecast updates in spring.

Since 1 August 2019 the German Council of Economic Experts has also been appointed as the National Productivity Board (NPB) of Germany. The basis of the NPBs is a recommendation issued by the Council of the European Union on 20 September 2016. The NPBs shall analyse developments in the field of productivity and competitiveness. This includes diagnoses of the long-term drivers of economic development, the conditions for increasing productivity and competitiveness, for example through the promotion of innovation, research and development, education, skills and training, and the capacity to attract investment, enterprises and human capital. A broad consultation process at national level and a regular exchange and intensive cooperation at European level should feed into the analysis. The German Council of Economic Experts has been addressing the issues of productivity and competitiveness in its annual reports since it was founded, and will give an additional analytical focus to these issues starting with the annual report 2019/20.

The Council of Economic Experts consists of five members who are specialists in the field of economic theory and economic policy. They are appointed every five years by the Federal President on the recommendation of the Federal Government. Reappointments are permitted. The Council then selects one of its members as chairperson for three years.

The Council of Economic Experts is supported by the Staff chaired by the secretary general. Furthermore, the Council resorts to the Liaision Office at the Federal Statistical Office in matters of organisation and statistics.

8 This information is taken from the Council's website: https://www.sachverstaendigenrat-wirtschaft.de/en/about-us/objectives.html

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