Launching the economic and monetary union on January 1, 1999

The euro was launched as a common currency in eleven member states of the European Community[1] on January 1, 1999. That marked the start of Stage Three of European economic and monetary union (EMU). The responsibility for the single monetary policy of the euro-zone was transferred to the European System of Central Banks (ESCB), and entailed corresponding amendments of the national central bank acts. With the start of Stage Three of EMU, Federal bonds, five-year special Federal bonds and Federal Treasury notes due for redemption after January 20, 1999 were converted into euros by act of law, and new issues have been floated in euros since then. In EMU there is no longer an autonomous foreign exchange market in which the currencies that have given way to the euro are traded, but only direct quotations of the euro against non-Community currencies. A tradeable new exchange rate mechanism (ERM II) governs relations with the EU member states which have not yet introduced the euro. The Stability and Growth Pact and the coordination of economic policies are increasing in importance for the durability of the convergence of member states, and may contribute materially to the success of EMU.

1 Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, Netherlands, Portugal and Spain.

Fixing the conversion rates and transfer of the responsibility for monetary policy to the European System of Central Banks

Setting the conversion rates on December 31, 1998

The euro was launched as a common currency in eleven member states of the European Community on January 1, 1999. That marked the start of Stage Three of EMU. One of the main prerequisites of the launch of monetary union was the setting of the conversion rates between the national currencies of the participating member states and the euro. That was effected by a Regulation of the Council of the European Union based on a unanimous decision by the ministers of economics and finance of the participating member states. This regulation came into force on January 1, 1999. According to it, the conversion rate works out at DM 1.95583 for €1. The conversion rates are based on the market value of the ECU on December 31, 1998, since, under the Treaty, the external value of the ECU must not change as a result of the setting of the conversion rates, and the ECU was replaced 1:1 by the euro. The finance ministers had announced back in early May 1998 that they would use the bilateral central rates in the exchange rate mechanism of the old European Monetary System (EMS) as a basis for fixing the conversion rates of the euro[2] and the national central banks had agreed to ensure, by means of suitable market techniques, that the market rates on December 31,1998 would coincide with those rates. Hence those rates actually materialised in the market on December 31, 1998.

Euro as a currency in its own right available only in the form of deposit money until the end of 2001

In legal terms, the euro became a currency in its own right on January 1, 1999. It superseded the national currencies of the member states, which became non-decimal sub-units of the euro. In accordance with a decision by the heads of state and government,[3] however, the euro is available only in the form of deposit money for a transitional period of three years. Only from January 1, 2002 onwards will euro banknotes and coins be issued. In the interim, therefore, national monetary tokens will remain the sole legal tender. In line with the principle of "no compulsion – no obstruction", nobody is to be compelled to use or prevented from using the euro during the transitional period. In cashless payments, everybody can thus choose at his own discretion whether to issue a payment order in Deutsche Mark or in euros. The amount of a payment will be debited and/or credited to the respective accounts of the payer and payee in the desired currency unit, in accordance with the conversion rates and the rounding rules.

Establishment of the ECB and ESCB, its duties and institutions

Since January 1, 1999, the ESCB has borne the responsibility for the stability of the new currency. The ESCB was set up on June 1, 1998, in the wake of the appointment of the President, Vice-President and other members of the Executive Board of the European Central Bank (ECB), but it did not take up full operation until January 1, 1999. It is composed of the ECB and the national central banks of the EU member states and its primary objective is to maintain price stability in the com-

2 See Deutsche Bundesbank, European policy decisions of May 1 to 3, 1998 pave the way for the launching of the euro on January 1, 1999, Monthly Report, May 1998, page 17 ff.
3 Implemented by the Council Regulation (EC) No. 974/98 dated May 3, 1998 on the introduction of the euro.

mon monetary area. The ECB Governing Council, which comprises the members of the Executive Board of the ECB and the governors of the central banks of the euro-zone, will now issue the guidelines and take the decisions needed to perform the tasks of the ESCB, and, in particular, will formulate the single monetary policy. The national central banks, being an integral part of the ESCB, execute the monetary policy of the latter in their respective member state. The Executive Board is responsible for implementing the decisions of the ECB Governing Council and for carrying out the ongoing business operations of the ECB. Besides the ECB Governing Council and the Executive Board, there is also a General Council, as a third decision-making body, in which the central banks of the EU member states which are not yet participating in the monetary union owing to a derogation or a special status are also represented. The authority for monetary policy is, however, vested exclusively in the ECB Governing Council.

Single monetary policy for the common monetary area

The distinguishing feature of the monetary union is that only a single monetary policy can be formulated and implemented in the entire euro-zone. There can no longer be a monetary policy that differentiates between individual member states. Hence it is only logical for the goal of European monetary policy (viz. maintaining price stability) to be measured in terms of the harmonised consumer price index (HCPI) of the euro-zone.

Denationalisation of monetary policy

In the formulation of monetary policy, the members of the ECB Governing Council are independent. They act as "guardians of the euro" and not as defenders of national interests. Due account is taken of that fact by the principle of the equality of votes; that is to say, in the ECB Governing Council, every member has only one vote on monetary policy issues, and monetary policy decisions are taken by a simple majority of votes. That arrangement fosters the denationalisation of monetary policy.

Decentralised implementation of centrally-resolved monetary policy

The practical implementation of monetary policy is governed by the principle of decentralisation. Accordingly, the operations needed to implement the monetary policy decisions taken centrally by the ECB Governing Council will normally be performed decentrally by the national central banks.

Institutional changes to the Bundesbank Act

Meeting the requirements of Community law

Entry into the final stage of EMU involved some major institutional changes for the Bundesbank, too. German central bank legislation was brought into line with the corresponding provisions of Community law by the Sixth Act Amending the Deutsche Bundesbank Act (Federal Law Gazette I, page 3274). The amendments are designed to fulfil the requirements arising from Articles 107 and 108 of the EC Treaty and from the associated provisions of the Protocol on the Statute of the ESCB and of the ECB. The amendments necessary in the light of the independence of the Bundesbank[4] came into force as early as December 31, 1997, the day after the promulgation of the Sixth Act. On the other hand, those amendments of the Bundesbank Act that are mainly concerned with the integration of the Bundesbank into the ESCB did not come into effect until the start of the participation of the Federal Republic of Germany in Stage Three of EMU.[5]

Reformulation of the duties of the Bundesbank

Owing to the transfer of monetary policy responsibility to the ECB, the duties of the participating national central banks have changed. The revised text of section 3 of the Bundesbank Act now requires the Bundesbank to participate in the performance of the ESCB's tasks with the primary objective of maintaining price stability. The task of arranging for the execution of domestic and international payments remains unchanged. In addition, the Bundesbank may discharge other duties assigned to it under the Bundesbank Act and other statutory provisions. In particular, it may, as before, take action in the fields of banking supervision and of foreign trade and on behalf of the Federal Government as the state's bank.

Change in the duties of the Central Bank Council

The transfer of the monetary policy decision-making powers to the ECB Governing Council also necessitates a change in the duties of the Central Bank Council. It no longer determines the monetary policy of the Bank, but rather its business policy. In discharging the duties of the ESCB, it acts in accordance with the guidelines and instructions issued by the ECB (section 6 (1), Bundesbank Act). Its most important task is therefore the implementation of the monetary policy decisions taken by the ECB Governing Council by means of general guidelines and instructions.

Relations with the Federal Cabinet

Relations with the Federal Cabinet have been redefined. The Bundesbank continues to be independent of instructions from the Federal Cabinet. It likewise continues to support the general economic policy of the Federal Cabinet, albeit in future "without prejudice to the performance of its tasks as part of the ESCB" (section 12 sentence 2, Bundesbank Act).

Temporary continuation of the issue of DM notes

In Stage Three of EMU, the ECB has the sole right to approve the issue of banknotes within the Community. Subject to that reservation, the provisions of section 14 of the Bundesbank Act on the sole right of the Bundesbank to issue notes denominated in Deutsche Mark remain valid for the time being. During the transitional period up to the end of 2001, the Deutsche Mark will remain the sole legal tender in Germany. On the other hand, there is no longer any room for a national range of monetary policy instruments. Hence the provisions on discount, lending and open market policies, as well as on minimum reserve policy (sections 15 and 16, Bundesbank Act) have been repealed.

Decentralised implementation of monetary policy

In line with the above-mentioned principle of the decentralisation of monetary policy oper-

4 The minimum term of office of the President of the Bundesbank, the other members of the Directorate and of the Executive Boards of the Land Central Banks was extended from two years to five years (sections 7 and 8, Bundesbank Act). Moreover, the Federal Cabinet's right to request that a decision by the Central Bank Council be deferred for up to two weeks was repealed (section 13 (2), Bundesbank Act).
5 See Deutsche Bundesbank, Amendment of the Bundesbank Act for Stage Three of European economic and monetary union, Monthly Report, January 1998, page 25 ff.

ations, before the start of EMU, the ECB Governing Council laid down the operating framework for monetary policy and fundamental conditions for the new payment system TARGET.[6] In Germany those guidelines were implemented by revising the text of the Bundesbank's General Terms and Conditions, as announced by Notice No. 2013/98 dated October 6, 1998. To a certain extent, the guidelines sanction some modifying decisions by the national central banks. The Bundesbank took advantage of the available leeway in order to accommodate certain national features.[7]

General Terms and Conditions and monetary policy operations

One of the most important changes in the field of the Bundesbank's monetary policy operations, which are regulated by section V of the General Terms and Conditions, is the abolition of rediscount operations. The Bundesbank has stopped buying trade bills, although they remain of significance as collateral for loans. The principal monetary policy instrument of the ESCB is open market operations, where the initiative is taken by the ESCB. Of overriding importance in this context are main refinancing operations, which conform in essentials to the Bundesbank's existing securities repurchase transactions. These may be supplemented by longer-term refinancing operations, fine-tuning operations and structural operations. The open market operations are accompanied by what are known as "standing facilities", where the initiative is taken by the banks. While the marginal lending facility (overnight credit) has taken the place of the former lombard loans at the Bundesbank, the deposit facility constitutes a new monetary policy instrument for the Bundesbank.

General Terms and Conditions and the introduction of the euro

With the start of Stage Three of EMU, the euro became the common currency of the participating member states. The Bundesbank's accounting system was converted into euros. During the transitional period up to the end of 2001, however, accounts at the Bundesbank will be carried both in euros and in Deutsche Mark. Payment orders may be issued in either currency unit (section II (2), General Terms and Conditions). If conversions between the euro and national currency units are required, they are carried out in accordance with the conversion rates and rules laid down by Community law (section I (19)).

Capital and the accounting system of the Bundesbank

The amended provisions on the capital and the accounting system of the Bundesbank are likewise closely associated with the entry into Stage Three. The capital has been increased from DM 290 million to DM 5 billion (section 2, Bundesbank Act) and the statutory reserves set at DM 5 billion; as a result, the "other reserves" which had previously also been provided for could be abolished. From the start of Stage Three of EMU, the Bundesbank's annual accounts are to be drawn up with due consideration of its duties – especially as a part of the ESCB – (section 26 (2)). Following a decision by the Central Bank Council on December 3, 1998, in general the rules of the ECB will be adopted in future for

6 Trans-European Automated Real-Time Gross Settlement Express Transfer.
7 See Deutsche Bundesbank, The implementation of the ESCB's monetary policy by the Bundesbank and its formulation in the General Terms and Conditions, Monthly Report, November 1998, page 17 ff.

the accounting system of the Bundesbank. In particular, that implies that the foreign reserves will be valued at market prices; where that gives rise to the disclosure of undisclosed reserves, they are to be shown in a balancing item (balancing item due to revaluation). According to the new section 45 of the Bundesbank Act, the restructuring of the capital and the reserves will take place as early as the annual accounts for 1998; by contrast, the amended provisions on the accounting system will not be applied until the financial years ending after December 31, 1998 and to the opening balance sheet dated January 1, 1999. Finally, the amendment of the Bundesbank Act has resulted in the repeal of the old section 28, which provided for the publication of a Bundesbank Weekly Return.

Conversion of outstanding bonds into euros and issue of new bonds denominated in euros

Legal basis

By the Act Converting Bonds into Euros (section 6 of the Act Introducing the Euro), the German legislature created the legal basis for the conversion of public and private debt instruments denominated in Deutsche Mark or in the national currency unit of another EU member state participating in EMU and subject to German law. Bonds issued by private entities can be converted only if they are traded in a securities market. The conversion of bonds denominated in the national currency unit of another EU member state participating in EMU is possible if that state converts its public debt into euros. By virtue of the said Act, Federal bonds, five-year special Federal bonds and Federal Treasury notes due for redemption after January 20, 1999 were converted into euros with effect from January 1, 1999. All other above-specified debt instruments may be converted into euros as from January 1, 1999 by a declaration on the part of the issuer. By such conversion, public and private issuers are able, within the scope afforded by the Act, to adjust the terms of issue. For instance, as part of the conversion operation, the right to be supplied with certificates denominated in euros may be excluded or curtailed, the transferable par values may be redefined, and the provisions on the calculation of interest below one year and on the fixing of trading days may be brought into line with European practice.

Conversion of the liabilities of the Federal Government and its special funds

Simultaneously with the Federal bonds, five-year special Federal bonds and Federal Treasury notes falling due for redemption after January 20, 1999, the transferable securities of the former Treuhand Agency, of the "German Unity" Fund, of the Federal Railways Fund, of the ERP Special Fund, of the former German Federal Post Office, of the Currency Conversion Equalisation Fund and of the Indemnification Fund were also converted into euros. The only securities excepted were the funding bonds issued by the Federal Republic of Germany and Treasury notes issued by the German Federal Post Office, as well as Federal savings bonds, Federal Treasury financing bonds and Treasury discount paper (because they are unlisted).

The Federal Debt Administration published the amendments and adjustments of the respective terms of issue in the "Announce-

Federal securities as from January 1, 1999

Security	Issued in euros	Method of computing interest 1	Reference interest rate for floating-rate issues	Minimum denomination
New issues				
Federal bonds				
Fixed interest rate	yes	actual / actual	–	€ 1,000
Floating interest rate	yes	actual / 360	EURIBOR	€ 1,000
Five-year special Federal bonds	yes	actual / actual	–	€ 100
Federal Treasury notes	yes	actual / actual	–	€ 1,000
Treasury discount paper (Bubills)	yes	actual / 360	–	€ 1 million
Federal savings bonds	no 2	actual / actual	–	DM 100
Treasury financing bonds	no 2	actual / actual	–	DM 1,000

Security	Converted into euros	Method of computing interest 1: old	Method of computing interest 1: new	Reference interest rate for floating-rate issues: old	Reference interest rate for floating-rate issues: new	Minimum denomination: old	Minimum denomination: new
Old issues							
Federal bonds							
Fixed interest rate 3	yes	30 / 360	actual / actual	–	–	DM 100 / 1,000	€ 0.01
Floating interest rate							
old FIBOR	yes	30 / 360	actual / 360	old FIBOR	EURIBOR	DM 1,000	€ 0.01
new FIBOR	yes	actual / 360	–	new FIBOR	EURIBOR	DM 1,000	€ 0.01
LIBOR	yes	actual / 360	–	DM LIBOR 4	EURO LIBOR	DM 5,000	€ 0.01
Five-year special Federal bonds	yes	30 / 360	actual / actual	–	–	DM 100	€ 0.01
Federal Treasury notes	yes	30 / 360	actual / actual	–	–	DM 5,000	€ 0.01
Treasury discount paper (Bubills)	no	actual / 360	–	–	–	DM 1 million	–
Federal savings bonds	no	30 / 360	–	–	–	DM 100	–
Treasury financing bonds	no	30 / 360	–	–	–	DM 1,000	–

1 Actual / actual means that the length of the broken period will be computed to the actual number of days involved out of 365 (or 366 in leap years); for old issues, conversion as from the next interest payment date in 1999. — **2** Issues in DM expected until December 31, 2001. — **3** Section 1 of the Conversion Act does not apply to securitised interest claims arising from Reich bonds (funding bonds); they will not be converted into euros. — **4** Neither the FIBOR regulation nor section 5 (1) 3 of the Conversion Act provides a legal basis for replacing DM LIBOR by EURIBOR.

Deutsche Bundesbank

Modification of the terms of issue and conversion of other bonds

ment of the declaration on the conversion into euros of Federal bonds, five-year special Federal bonds and Federal Treasury notes" dated October 22, 1998 (and published in Federal Gazette No. 215 of November 14, 1998). The smallest transferable par values of all converted Federal securities[8] were set at 0.01 euro (1-cent method). This minimum denomination is designed to ensure the full transferability of the converted debt instruments without any disadvantages for the holders arising from the conversion. Where coupon strips (separately traded interest coupons of a Federal bond) are concerned, the smallest transferable par value was likewise lowered to one cent, while the minimum amounts for stripping and reconstruction were set at € 50,000. The procedures for the calculation of accrued interest on outstanding fixed-rate Federal bonds, five-year special Federal bonds and Federal Treasury notes were modified in accordance with the initial maturity of the first coupon in 1999. For these securities, in future, interest will be computed using the actual number of days involved (actual/actual method). For the floating-rate securities, on the maturity of the first interest payment in 1999, the euro interest method (actual/360) will be introduced, unless it already has been. With regard to the reference interest rate of floating-rate Federal bonds, on the first interest assessment in 1999, the FIBOR rate (old and new) will give way to the EURIBOR rate or, in the case of a floating-rate Federal Railways bond, the DM LIBOR to EURO LIBOR. In terms of volume, a

8 Other than funding bonds.

large proportion of the other bonds issued under German law and traded on German stock exchanges was converted into euros on January 1, 1999. The Länder Governments intend to convert their bonds by the end of the first quarter of 1999.

Issue of new debt instruments in euros

Federal bonds, five-year special Federal bonds, Federal Treasury notes and Treasury discount paper of the Federal Republic of Germany (Bubills) have been issued in euros since January 1, 1999. The first bond issue of the Federal Republic of Germany denominated in euros was launched in the first week of January. The Federal savings bonds and Treasury financing bonds of the Federal Republic of Germany, which are primarily intended for selling to private investors, are expected to go on being issued in Deutsche Mark until the end of 2001. There will in future be two methods of calculating the accrued interest of the new issues: in the case of discount paper (Bubills) and floating-rate Federal bonds, the life will be computed to the precise day and the year will be reckoned as 360 days (actual/360); in the case of Federal Treasury notes, five-year special Federal bonds, fixed-rate Federal bonds, Treasury financing bonds and Federal savings bonds, the life will be computed to the precise day in a year of 365 days (366 in leap years) (actual/actual). As the reference interest rate for newly issued floating-rate Federal bonds, the EURIBOR rate will be used in future. A minimum denomination of € 1,000 has been introduced for Federal bonds and Federal Treasury notes, while the minimum denomination for five-year special Federal bonds is € 100 and that for Treasury discount paper (Bubills) is € 1 million. The minimum denomination for Treasury financing bonds is DM 1,000 and that for Federal savings bonds is DM 100.

Conduct of foreign currency transactions in euros and abolition of national foreign exchange markets

ECB endowed with foreign reserve assets of its own

One of the ESCB's tasks is the conduct of foreign exchange operations and the holding and management of member states' foreign reserves. Under Article 30 of the Statute of the ECB/ESCB, the national central banks have provided the ECB with foreign reserve assets. The amount of the initial contributions is limited to the equivalent of € 50 billion. The contributions of the individual national central banks are proportionate to their shares in the subscribed capital of the ECB, and were paid up at the beginning of Stage Three of EMU. However, the total amount of € 50 billion was reduced by the shares of the EU member states not yet participating in EMU, with the result that the value of the reserve assets actually transferred to the ECB came to about € 39.47 billion. In line with its share in the capital of the ECB (amounting to 24.4935 % of the total) the Bundesbank transferred a sum equivalent to some € 12.25 billion, made up, in accordance with the requirements of the ECB Governing Council, of 15 % gold and 85 % foreign exchange. The transfer was effected in the first bank-week of the new year at market prices.

The foreign reserves transferred to the ECB are managed decentrally by the national cen-

The foreign reserves transferred to the ECB are managed decentrally at the national central banks

tral banks on behalf of, and in accordance with the guidelines issued by, the ECB. Those central banks must be guided by a comparative portfolio ("benchmark") provided by the ECB, which prescribes both the maximum permissible deviations and the investment vehicles and segments for such asset management.

Foreign exchange market intervention...

Its provision with reserve assets of its own enables the ECB to intervene in the foreign exchange markets in case of need. On the entry into Stage Three of EMU, after all, responsibility for foreign exchange policy, too, devolved upon the ECB. Autonomous intervention in the foreign exchange markets by the national central banks in order to influence exchange rates is no longer admissible or possible. The initiative to perform foreign exchange operations, which are conducted exclusively with the reserve assets transferred to the ECB, proceeds from that Bank. In case of need, it will issue appropriate instructions to the national central banks, and will take action itself only in exceptional circumstances.

... only in exceptional circumstances

Since the euro is floating freely against non-Community currencies, exchange market intervention is likely to remain the exception. In December 1997, the European Council, meeting in Luxembourg, reaffirmed the principle of restraint in exchange rate policy. In a resolution, it expressly drew attention to the fact that it would exercise the option of issuing general orientations for exchange rate policy in relation to non-Community currencies, in line with Article 109 (2) of the EC Treaty, only in exceptional circumstances, such as clear misalignments. Such general orientations must respect the independence of the ESCB and be consistent with the primary objective of the ESCB of maintaining price stability.

The foreign reserves remaining at the national central banks continue to be under national responsibility

The greater part of the foreign reserves at the national central banks of the euro area remain under their control and responsibility. However, the Treaty provides for the transfer of further foreign reserves to the ECB under certain conditions. The national central banks may use their reserves, in particular, to discharge their obligations to international organisations. But, from a given magnitude onwards, other transactions with those reserve assets are subject to the approval of the ECB. That serves to ensure that even major foreign exchange transactions by individual national central banks are in line with the single monetary policy of the euro area.

Daily reference exchange rates of the ECB

In EMU there is no longer an autonomous foreign exchange market of the currencies that have given way to the euro, but only direct quotations of the euro against non-Community currencies such as the US dollar, the yen, etc. Furthermore, the ECB Governing Council has decided not to conduct any official fixing of the euro involving the ECB or the national central banks. In order to satisfy the general public's justified interest in reference exchange rates, however, on every trading day since January 4, 1999, the ECB has published reference exchange rates for the major international currencies and for the currencies of those countries with which negotiations on accession to the European Union have started. These reference rates are ascertained on the basis of a daily concertation between the central banks (normally at 2:15 p.m. CET) and are published shortly afterwards by the main stock market information providers via electronic media. Only one reference figure, namely the middle rate, is published per currency, in the form of a "certain" quotation in which one euro is equated with the equivalent amount of the foreign currency (one euro = x units of the foreign currency). In Germany, such quotation is already standard practice in interbank trading. In dealings with private customers, by contrast, the opposite quotation method has so far been customary (one unit of the foreign currency = x euros). The international trend is moving in the direction of the "certain" quotation, so that it is to be expected that this form of exchange rate quotation will finally prevail in Germany, too, in business with private customers.

Exchange rate mechanism II

New exchange rate mechanism comes into force

With the beginning of Stage Three of EMU, the former European Monetary System ceased to have effect. It was replaced by the new European exchange rate mechanism ERM II.[9] By that mechanism, the four member states which are not introducing the euro for the time being are given a chance to link their currencies to the euro and thus to prepare themselves for full incorporation in the euro area. Denmark and Greece have been availing themselves of this option since January 1, 1999. Following a common procedure involving the European Commission, and after having consulted the EC Monetary Committee (which has been superseded since the beginning of the year by the Economic and Financial Committee), the ECB, the ministers of the euro area and the ministers and central bank governors of Denmark and Greece unanimously set the central rates of the Danish krone and the Greek drachma and their fluctuation margins vis-à-vis the euro on December 31, 1998. The central rate of the Danish krone was set at DKR 7.46038 per euro, and that of the Greek drachma at DR 353.109 per euro. A fluctuation margin of ± 2¼% was set for the Danish krone and the standard margin of ± 15% was agreed for the Greek drachma. On setting the central rate, it was ensured that no appreciation or depreciation should occur vis-à-vis the bilateral central rates applying in the EMS on December 31, 1998.

New agromonetary system

The transition to the final stage of EMU was particularly significant for the agricultural sector, too. A simplified agromonetary system entered into force with effect from January 1, 1999. Under the new system, all monetary variables in the Common Agricultural Policy, especially agricultural prices, are fixed in euros. Conversion of the euro amounts is effected in the euro-zone at the conversion rates set, and in the countries with a derogation at the current exchange rates against the euro; in other words, the special agricultural conversion rates existing to date have been abolished. In the euro area, there are no longer any changes in agricultural prices in national currencies, and therefore in farm income, owing to exchange rate fluctuations. On the other hand, farmers in countries with a dero-

9 See Deutsche Bundesbank, Operational features of the new European exchange rate mechanism, Monthly Report, October 1998, page 17 ff.

gation whose currencies may still appreciate or depreciate against the euro may, subject to specific conditions, continue to receive compensatory subsidies in the event of income losses due to monetary developments.

Underlying conditions of EMU for the durability of the convergence of member states (Stability and Growth Pact, coordination of economic policies)

Stable underlying economic conditions a prerequisite of the lasting success of EMU

With the introduction of the euro, the economies of the member states are linked together more closely through the single monetary policy and a uniform exchange rate. Hence stable underlying conditions throughout the euro area are a major prerequisite of the lasting success of EMU. However, such conditions cannot be guaranteed by the single monetary policy alone, but need support from, in particular, disciplined economic and fiscal policy. Ahead of Stage Three, the underlying conditions for economic and fiscal policy, which is at bottom a national responsibility, were explicitly spelled out on the basis of the provisions of the Treaty.

Member states undertake to avoid excessive deficits

In Stage Three member states are under an obligation to avoid excessive budget deficits. Compliance with this clear Treaty obligation is monitored in accordance with the procedure for monitoring the budgetary situation in member states specified in Article 104c of the EC Treaty. Given the crucial importance of sound public finance for price stability, and thus also for lasting and healthy growth, the European Council, acting on a German initiative, adopted the Stability and Growth Pact in June 1997. That Pact defines the contractual surveillance procedures for the budgetary position in more detail, and streamlines those procedures. The key feature of the Stability and Growth Pact is member states' commitment to aim at the medium-term objective of budgetary positions close to balance or in surplus; that is meant to ensure that, in the event of "normal" cyclical fluctuations, member states can comply with the reference value of 3 % of GDP for such a deficit. In line with a recommendation by the EC Monetary Committee, the Council, meeting at the level of the ministers of economics and finance, agreed last autumn to attain that objective not later than the end of 2002. The Council monitors the implementation of, or compliance with, the medium-term budget target by reference to the stability programmes to be submitted annually by member states (or convergence programmes in the case of the member states not yet participating in EMU). In the event of considerable divergences of the budgetary position from the medium-term budget objective or from the adjustment path to that goal, the Council issues recommendations to take the necessary budget measures to the member state concerned well before any excessive deficit arises. If, in exceptional cases, an excessive deficit does arise, under the provisions of the Stability and Growth Pact a procedure comes into play that provides for measures to identify and remedy the deficit quickly, and defines in more detail the conditions under which a member state may be subjected to sanctions in specific cases.

Stability declaration by the finance ministers in May 1998

In amplification of the Stability and Growth Pact, in May 1998 the finance ministers, when determining the participants in EMU, reached agreement on an additional stability declaration which includes further major commitments on the part of the member states to continue a policy of sound public finance. For instance, the member states are durably committed to making all the necessary efforts to meet the budget targets set. If economic conditions develop more favourably than expected, they are called upon to take advantage of the "growth dividend" to step up budget consolidation. In addition, member states with a high level of public debt must redouble their efforts to reduce it.

Procedures fostering economic policy coordination in Stage Three

As well as for fiscal policy, the responsibility for general economic policy, including wage-rate policy, remains in the hands of the member states during Stage Three. However, member states are still bound by the provisions of the EC Treaty, which stipulates that they must regard their economic policies as a matter of common concern and must coordinate them in accordance with the Treaty. The specific provisions on this point are largely spelled out in Article 103 of the Treaty. The most important instrument of economic policy coordination is the broad guidelines of economic policy, which the Council – acting on a recommendation from the Commission and after a discussion in the European Council – adopts annually. On the basis of reports submitted by the Commission, the Council monitors economic developments in the member states and the Community and examines the consistency of economic policies with the broad guidelines. The Commission is required to issue warnings well ahead of undesirable developments (e.g. in wages and prices). Where it is established that a member state's economic policies are not consistent with the broad guidelines, the Council may make the necessary recommendations to the member state concerned, and also decide, if need be, to make them public.

Broad guidelines of economic policy as an instrument for ensuring lasting convergence

At its meeting in Luxembourg in December 1997, the European Council decided to develop the broad guidelines of economic policy into an effective instrument for ensuring lasting convergence in the Community. To that end, the guidelines are to be formulated in more concrete and country-specific terms, and more attention is to be paid in future to structural policy considerations in member states. The greater concentration on structural policy in future is also in the interests of the single monetary policy. The structural reforms required in all member states will have to be initiated individually by each country, since the euro is no substitute for the necessary reforms, but will bring the need for them into sharper focus and will increase the pressure on policy makers to reorientate their economic policies.

The Council as the key decision-making body in connection with the coordination of economic policies

The key decision-making body in all questions of coordination is the Council, at the level of the ministers of economics and finance. It is the only body that has the mandate to formulate and approve the broad guidelines. It also ensures that cohesion is preserved between the countries of the euro-zone and the countries not yet participating in the euro. To discuss issues that arise, in particular, from participation in the common monetary area, the ministers of economics and finance of the euro-zone can meet informally, with the participation of the Commission and, possibly, the President of the ECB. That informal Euro-11 Group, which has already convened in expanded form, including the finance ministers of the countries with a derogation, cannot, however, take any legally binding decisions.

Stability and Growth Pact and economic policy cooperation constitute the framework for the policy coordination of the Euro-11 Group

With the provisions of the Stability and Growth Pact and the procedures fostering economic policy cooperation, the framework for the coordination of policies within the Euro-11 Group and the Council is duly marked out. As a result, the essential prerequisites of lasting economic convergence among the member states have been created. In Stage Three of EMU it will be of paramount importance to apply these provisions strictly in practice, so that a tension-free policy mix materialises between the single monetary policy and economic and fiscal policies, which remain in national hands.

The publications of the ESCB

Objectives and principles

The single monetary policy for the euro zone calls for a coordination of public relations work between the European Central Bank and the national central banks. The overriding aim of any communications policy on the part of the ESCB must be to speak with a single voice, in terms of content, to market players and the general public alike. The decentralised structure of the ESCB is nevertheless reflected in the fact that specific national features of the dissemination of information are taken into account, with the ESCB exploiting the communications experience of the national central banks and letting those banks act as contacts for the media and the public at large. Other fundamental objectives are that the tasks and decisions of the ESCB should be made more transparent to the general public, that confidence in its operations should be built up, and that a contribution should be made to the discharge of its information obligations under the Treaty. In this context, the ESCB attaches importance to the equal treatment of member states and the media, which is reflected, among other things, in the fact that the ECB publications, which are composed in English, are translated into all other official languages of the EU.

Publications of the ECB

With the January issue of the ECB Monthly Bulletin, the European Central Bank has embarked on the regular reporting of its activities. In addition, the ECB will issue the other publications provided for in the EC Treaty, such as Weekly Bulletins and Annual Bulletins. These documents will be translated into all EU official languages and, if necessary, published simultaneously, as is likewise envisaged for major press releases. Speeches and interviews by those holding high offices in the ECB will supplement the public relations efforts.

Publications of the Bundesbank

In order to keep the general public in Germany informed, the Bundesbank will continue its existing publications policy in largely unchanged form. That applies, in particular, to the Monthly Report and its Statistical Supplements, as well as to the Annual Report and most special publications.