

# **The 2024 Luigi De Rosa Lecture**

# The Werner Report, the Delors Report and the Birth of Euro

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## ABSTRACT

The Werner Report and the Delors Report played a crucial role in the EMU process. The vision of EMU of the two reports differed significantly. The Werner Report was in favor of an EMU with both a supranational monetary pillar (a European System of Central Banks) and a supranational economic pillar (a decision-making center for economic policy), reflecting the dominating Keynesian paradigm with a belief in discretionary fiscal policy. In the Delors Report the focus was on the monetary pillar (an independent European System of Central Banks), while there was skepticism about discretionary fiscal policy. This reflected a new consensus, as both policymakers and academics had moved away from active demand management policies and were going towards a medium-term orientation, emphasising structural, supply-side oriented policies. It will be argued that this new consensus facilitated an agreement on EMU. As the perceived room for discretionary economic policies was more limited, it implied a more limited transfer of sovereignty (focused on monetary policy), as envisaged earlier in the Werner Report. Particular attention will be given to one of the background papers of the Delors Report, "The Werner Report Revisited", by the two rapporteurs of the Delors Committee, Gunter Baer and Tommaso Padoa-Schioppa.

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## 1. INTRODUCTION

The Werner and the Delors Reports were crucial anchor points within Europe's EMU debates. They presented both a vision of EMU and a path to reach EMU. Their vision of EMU differed significantly. The Werner Report supported a symmetric EMU, with both a supranational monetary pillar (a European System of Central Banks) but also a supranational economic pillar (a decision-making center for economic policy), reflecting the still dominating Keynesian paradigm with a belief in discretionary fiscal policy. In the Delors Report the focus was on the monetary pillar (an independent European System of Central Banks), while there was skepticism about discretionary fiscal policy. This reflected a new consensus, as both policymakers and academics had moved away from active demand management policies and were going towards a medium-term orientation, emphasizing structural, supply-side oriented policies (Maes, 2024). It will be argued that this new consensus facilitated an agreement on EMU. As the perceived room for discretionary economic policies was more limited, it implied a more limited transfer of sovereignty (focused on monetary policy), as earlier envisaged in the Werner Report.

It is important to observe that the decisions about monetary integration have always been taken at the highest level, that is by Heads of State and Government, as it involved crucial decisions about sovereignty. EMU has been "high-level politics," with a special role for the Franco-German engine: Pompidou and Brandt at the Hague Summit, Giscard and Schmidt for the European Monetary System and Mitterrand and Kohl for the Maastricht Treaty process.<sup>1</sup>

We start the paper with a short overview of the golden sixties, the high days of Keynesian economics and European integration. Thereafter we go into the Werner Report, the turbulent 1970s and

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<sup>1</sup> In this paper we take the European Union's decision to go ahead with EMU as a starting point, and we do not go into the question whether Europe was an "optimal currency area".

the rise of a new economic paradigm. After that the focus will shift on the new dynamism in the European Union in the 1980s and the Delors Report. This led to the Maastricht Treaty which offered a new framework for economic governance in the European Union. Particular attention will be given to one of the background papers of the Delors Report, “The Werner Report Revisited,” by the two rapporteurs of the Delors Report, Gunter Baer and Tommaso Padoa-Schioppa (partly based on archival research in the Padoa-Schioppa archives at the EUI).

## 2. THE GOLDEN SIXTIES

At the beginning of the 1970s, the economic thought among policy-makers was dominated by the experience of the “golden sixties”: a strong economic growth, stable prices and the success of Keynesian demand management. European economic integration also thrived in the 1960s, especially with the successful completion of the customs union, a key element of the Rome Treaty project. The launching of the monetary union project, at the 1969 Hague Summit, reflected this atmosphere.

Keynesian economics strongly emphasized the role of budgetary policy in steering the aggregate demand in the economy. One of the foremost historians of Keynesian economics, Alan Coddington (1983), argued that the distinctive trait of Keynesianism is a utilitarian view of public finances. A prerequisite for taking such a utilitarian perspective of public finances is that there must be a systematic, reliable connection between fiscal policy and effective demand in the economy, so typical for hydraulic Keynesianism, which dominated mainstream economic thinking in the postwar period. Very influential in policy circles was the Heller Report, which, in line with this utilitarian view, defined the role of fiscal policy as, “not to balance the budget of the public sector, but to balance the economy as a whole” (OECD, 1968, 15).

In the Keynesian view, fiscal policy was the main instrument to

steer aggregate demand in the economy. In order for fiscal policy to influence the level of real activity, a stable and reliable relationship between prices and output is necessary. This was found in the Phillips curve, showing a negative relationship between changes in prices and unemployment (Samuelson and Solow, 1960). According to the (simplified) Keynesian framework, the main task of the policymakers was to determine the preferred tradeoff between unemployment and inflation. Demand management, especially budgetary policy, would then be used to reach the preferred tradeoff. Consequently, every country had then a preferred national inflation rate.

In December 1969, at the EU summit in the Hague, an ambitious program to relaunch European integration was established, comprising both a widening of the Community (enlargement with the United Kingdom) and a strengthening (economic and monetary union). Several factors contributed to the change in atmosphere that placed economic and monetary union in the spotlight and made it one of the Community's official objectives. During the 1960s the customs union project, with the abolition of tariffs and quotas, was realized. At the end of the 1960s then, one started to look for new projects. Moreover, the unease with the Bretton Woods system was growing. De Gaulle had always been critical of the central position of the US dollar in the Bretton Woods system. During the second half of the 1960s, French officials, in order to attain a more equilibrated international monetary system, developed ideas about a European monetary identity. A key element was a type of exchange rate mechanism, to keep European currencies closer together. At the end of the 1960s, doubts about the future of the fixed exchange rate system started to spread, especially with the devaluation of the French franc in 1969 and the vulnerable position of the American dollar. The countries of the Community feared that further exchange rate instability would lead to the disintegration of the customs union and the demise of the common agricultural policy.

Moreover, new political leaders had come to power. In 1969 de Gaulle resigned and his successor, Georges Pompidou, was more open to new European initiatives. In Germany, a new government

was formed with Willy Brandt as chancellor, a convinced proEuropean. The Brandt government proposed the EMU project. Foreign policy motives were crucial. Germany wanted to demonstrate its European credentials, also to counterbalance its new Ostpolitik (with the recognition of the German Democratic Republic as a key element).<sup>2</sup> One can observe here an important similarity with the late 1980s when the Kohl government favored both German unification and advances towards European integration with the Maastricht Treaty.

### 3. A FIRST ATTEMPT AT EMU WITH THE WERNER REPORT

After the Hague Summit, a committee, under the chairmanship of the Luxembourg prime minister (and finance minister) Pierre Werner, was set up to elaborate a plan for the creation of an economic and monetary union. The members of the group were the Chairmen of the Monetary Committee (Bernard Clappier, French treasury), the Committee of Governors of Central Banks (Hubert Ansiaux of the National Bank of Belgium), the Short-term Economic Policy Committee (Gerard Brouwers of the Dutch economics ministry), the Medium-term Economic Policy Committee (Johann Baptist Schöhlhorn of the German economics ministry, with Hans Tietmeyer as his alternate), the Budget Policy Committee (Gaetano Stammati of the Italian finance ministry) and Ugo Mosca (representing the European Commission). As one can see, through the chairmen of the economic policy committees of the European Community, all the countries of the community were represented, except for Luxembourg. Having a prime minister as its chair reinforced the weight of the committee.

The Werner Committee submitted its final report in Octo-

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<sup>3</sup> Given the reluctance of German economic policymakers (the Bundesbank and the economy and finance ministries did not want to prepare a proposal on the lines Brandt wished), Brandt turned to Jean Monnet, who asked Robert Triffin to elaborate a memorandum for Brandt (Maes and Pasotti, 2021).

ber 1970 (Council Commission of the European Communities, 1970, hereafter referred to as Werner Report). It contained a program for the establishment, by stages, of an economic and monetary union by 1980 (Danescu, 2016). In the Werner Report attention was first focused on the final objective of economic and monetary union. The implementation by stages was elaborated thereafter.

The Werner Report first presented a very general picture of the economic and monetary union: "The economic and monetary union will make it possible to realize an area within which goods and services, people and capital will circulate freely and without competitive distortions, without thereby giving rise to structural or regional disequilibrium" (Werner Report, 9). The Report also gave a definition of a monetary union (which reflected very much a Bretton Woods perspective): "A monetary union implies the total and irreversible convertibility of currencies, the elimination of margins of fluctuation in exchange rates, the irrevocable fixing of parity rates and the complete liberation of movements of capital<sup>3</sup> inside its boundaries. It may be accompanied by the maintenance of national monetary symbols or the establishment of a sole Community currency." However, the Report favored a single currency to make EMU irreversible.

To assure the cohesion of the economic and monetary union two elements were necessary: transfers of responsibility from the national to the Community level and a harmonization of the instruments of economic policy in various sectors. On the institutional plane, this implied the existence of two new, supranational, Community institutions, a center of decision for economic policy and a Community system for the central banks (very much like the Federal Reserve System in the United States).<sup>4</sup> The Werner Report had then

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<sup>3</sup> While the free movement of capital was an indispensable element of a monetary union, the Werner Report also underlined that it was an essential element of a common market (with the four freedoms, free movement of goods, services, labour and capital).

<sup>4</sup> The Werner Report did not mention the notion of central bank independence. Discussing the relations between the different institutions, it mentions "safeguarding the responsibilities proper to each" (Werner Report, 13). According to Tietmeyer (interview, 18 December 2001), this implied the independence of the central bank.

a symmetric vision of EMU, with both a strong monetary and a strong economic pillar. The center of decision for economic policy would exercise “a decisive influence over the general economic policies of the Community” (Werner Report, 12). A key responsibility concerned budgetary policy. While the Werner Report admitted that the role of the Community budget would remain limited, it emphasized that the center of decision for economic policy should have a key role in steering national budgetary policies, “the essential features of the whole of public budgets, and in particular variations in their volume, the size of the balances and the methods of financing or utilizing them, will be decided at the Community level” (Werner Report, 12). Given these important transfers of sovereignty to the Community level, the Report argued that there should also be a corresponding transfer of parliamentary responsibility from the national to the Community level. The center of decision of economic policy would be responsible to the European Parliament. The Werner Report underlined the fundamental political significance of transfers of responsibility to the Community level and came out in favor of a political union, “Economic and monetary union thus appears as a leaven for the development of political union, which in the long run it cannot do without” (Werner Report, 12).

The Werner Report further proposed a plan in three stages to attain economic and monetary union. The Report did not lay down a precise timetable for the implementation of the whole plan. Rather it wanted to maintain a measure of flexibility, while concentrating on the first phase. It proposed that the first stage would start on 1 January 1971 and cover a period of three years. The main elements were: (a) a reinforcement of procedures for consultation and policy coordination; (b) a further liberalization of intra Community capital movements and steps towards an integrated European capital market; (c) a narrowing of exchange rate fluctuations between Community currencies (as set up in the Bretton Woods framework). Of the second stage the Report noted that it “will be characterized by the promotion on a number of fronts and on ever more restrictive lines of the action undertaken during the first stage” (Werner Report, 28).

The Report also proposed to establish a European Fund for Monetary Cooperation even though no decision was made at that time whether this would be in the first or second stage.

#### 4. THE TURBULENT 1970s AND THE RISE OF A NEW ECONOMIC PARADIGM

The Werner Report was followed by intense discussions, both among policymakers and in academic circles. A key issue was the feasibility of the economic and monetary union. Many eminent economists expressed their skepticism with respect to the feasibility of the Werner Report. Macroeconomic discussions in the early 1970s took typically place in a “Phillips curve World” (De Grauwe, 1975), which assumed a stable relationship between inflation and unemployment. Of crucial importance are the preferences of the governments between unemployment and inflation. Every country has then a “national propension to inflation” (Magnifico, 1971, 13). In this type of world, inflation rates between two countries will only be equal by accident. Naturally, differences in inflation rates would lead to balance of payments imbalances, which were incompatible with fixed exchange rates. The monetary union would then force a country to accept a tradeoff between unemployment and inflation which it considered as suboptimal. The country would be forced to sacrifice its internal balance for exchange rate unification.

Europe’s monetary union project quickly ran into difficulties. The proposal for supranational European institutions was not well received in France. However, the removal of these institutions in subsequent Commission proposals was not well taken in Germany. Moreover, the new European exchange rate system (also known as the snake) quickly turned into a de facto German mark zone. The 1975 Marjolin Report, commissioned by the European Commission, described the situation as a “failure” and summarized the overall development between 1969 and 1975: “if there has been any movement it has been backward” (CEC, 1975, 1).

An important factor was that the international environment became very hostile with the collapse of the Bretton Woods system and the first oil shock. The breakdown of the Bretton Woods fixed exchange rate system implied that economic policies, especially monetary policy, did not have to be geared any more in function of the exchange rate against the dollar. This implied that policy makers had to find a new nominal anchor for their policies. Moreover, it contributed to a growing indebtedness in the world economy, as there were less constraints on economic policies (de Larosière, 2018). The first oil price shock of October 1973 challenged Western dominance in the world economy. It might then be regarded as a first manifestation of the so-called Global South.

In the 1970s the severe turmoil in the world economy contributed to a serious worsening of Europe's economic performance. Inflation as well as inflation divergencies between countries rose, and economic growth slowed down significantly. Europe's stagflation crisis had started. With the growing inflation divergencies, the monetary snake quickly ran into problems, and several countries had to leave the system. An important factor was that Europe's governments reacted very differently to the crisis, especially the increase in oil prices. For German policymakers, the oil shock was essentially an inflationary shock, to be contained with restrictive policies. The French considered, in first instance, that this might lead to a recession (as the French economy became poorer due to the deterioration of the terms of trade, it might lead to a reduction in demand) and followed more expansionary policies. So, differences in inflation rates soared, making fixed exchange rates unsustainable. The European snake had then a turbulent existence: there were several realignments of parities and many currencies dropped out. From January 1974 onwards, after the French departure, it was generally considered as a de facto German mark zone (notwithstanding a return of the French franc from July 1975 to March 1976).

Meanwhile, a new economic paradigm was on the rise. In the academic world, the "Monetarist Counter-Revolution" had already questioned the Keynesian framework. One might distinguish three

stages in these academic controversies. In the first stage discussions centered around the determination of nominal demand, with monetarists, like Milton Friedman (1956), emphasizing the money supply instead of budgetary policy, as the main determinant of effective demand. In a second stage the attention shifted towards the functioning of the labor market with monetarists attacking the Phillips curve, arguing that the curve shifted when workers adjusted their inflation expectations (Friedman, 1968). The Phillips curve did not provide then a stable relationship between prices and unemployment. In the third phase the formation of expectations became the focal point, with the "rational expectations hypothesis," implying that a change in policy could alter the behavior of the economic agents (Lucas, 1976).

In Europe, the "Konstanz Seminars" played an important role in spreading monetarism as well as in the transmission of monetarist ideas to policymakers. The first seminar was organized in June 1970 at the university of Konstanz by Karl Brunner. Among the participants there were Helmut Schlesinger, a future president of the Bundesbank and Mario Monti, a future Italian prime minister. Gradually then, a new policy conception emerged, wherein monetary policy was geared principally against inflation and inflationary expectations. Whereas after the break-down of the Bretton Woods system smaller countries continued with exchange rate pegs, bigger countries started using the money supply as an intermediate target of monetary policy, in line with monetarist ideas (the Bundesbank set its first money supply target in December 1974).

Among policymakers, the oil shock of 1973 and the ensuing stagflation were of fundamental importance to induce changes in their conceptions of economic policy, also in France. The crisis showed very clearly the openness of the economy and the vulnerability to external developments. French policymakers became more and more aware that there were limits to activist policies, and that France had to take into account the external constraint. During the second half of the 1970s, under the prime ministership of Raymond Barre, French economic policies became more stability-

oriented. The exchange rate was a crucial element in the strategy to instill discipline on the French economy. Barre also pushed through measures to liberalize prices. This reorientation of French economic policy was an important element in the decision of German policy-makers to consent to the creation of the European Monetary System (EMS).

The stagflation of the 1970s gave rise to important discussions among economic policymakers. At the G7 Bonn summit in May 1978, a coordinated macroeconomic strategy at a worldwide level, under the pressure of the American president Jimmy Carter, was drawn up. It led to the so-called concerted action, whereby Germany agreed to boost its economy with a budgetary package of 1% of GDP. However, the more expansionary budgetary policy in 1979 and 1980 coincided with an economic recovery, working procyclically. This created a severe trauma, especially in Germany (which was confronted with a balance-of-payments deficit), as well as in international institutions like OECD and the European Commission, which were important advocates of policy coordination. It also raised the issue of the efficiency of economic policy and made economists much more skeptical about possibilities for fine-tuning policy.

All this implied a shift away from discretionary demand management in favor of a medium-term orientation with an important role for monetary aggregates, as well as a focus on improving the growth potential of the economy, with attention to the structure of public expenditure, taxation and regulation. Moreover, behind the new policy orientation was a new view of the functioning of the economy, away from the mechanical Keynesian paradigm. Policy-makers were also influenced by debates in the academic world. A first element concerned the Lucas critique and rational expectations. This implied that economic agents were not responding in a mechanical or "Pavlovian" way to changes in economic policy. Policy-makers had to be aware that markets would anticipate policy measures. This further undermined the belief in the possibility of finetuning the economy and led to a greater emphasis on medium-term policies. Moreover, monetary policy was, in the long run, not

independent of budgetary policy, via the financing of public deficits. This was very much the experience of the 1970s, when stagflation contributed to increasing budget deficits, which, to an important extent, were financed by money creation (an experience which would haunt the Delors Committee).

Moreover, the notion of central bank independence gained ground. Building on monetarist and rational expectations theories, the literature on time-inconsistency pointed further to the inflationary bias of a discretionary monetary policy (Barro and Gordon, 1983). To retain flexibility, while dealing with the inflationary bias of a discretionary policy, central bank independence quickly topped the research agenda. Central bank independence became so not only a key theme of German *ordo-liberalism*, but also an important element of mainstream Anglo-Saxon economics.

The Phillips curve disappeared from the debates. The way then to improve the tradeoff between inflation and growth was to take measures on the supply side of the economy. An important element of these supply side policies were the privatizations, which started in in the United Kingdom in 1979 with the Thatcher government. In France, when Mitterrand went to power, he implemented a large-scale nationalization programme and privatisations began during the first “cohabitation,” with Balladur as finance minister in 1986.

So, at the end of the 1970s a shift occurred in Europe from a more activist policy towards a strategy based on medium-term stability, market-oriented policies and emphasis on measures enforcing the supply side of the economy. The shift was apparent in all major European countries. The clearest break was in the United Kingdom with the victory of Margaret Thatcher in 1979. In Germany a more conservative government was formed in 1982 under Helmut Kohl. However, a major change in fiscal policy had occurred already in 1981 under his socialist predecessor, Helmut Schmidt. In France the change occurred somewhat later, given the election of Mitterrand in 1981. After 18 months of a rather disastrous experiment in policy activism, the socialists reoriented their economic policy in a much less interventionist way.

## 5. FROM EUROSCLEROSIS TO A NEW DYNAMISM

The early 1980s were a period of crisis in the European Union: the economy was in the doldrums, and the integration progress was stalling. Europe's economic performance in the early 1980s was disappointing: economic growth was low, and unemployment was strongly increasing, while inflation was high and declined only stubbornly. An important factor was certainly the second oil shock in the autumn of 1979, which gave a stagflationary shock to Europe's economy. But the European performance contrasted also markedly with the situation in the United States, where the recovery was very strong, something which several observers associated with Reagan's supply side economics. "Eurosclerosis" was the term used to characterize the economic situation in the Community (Giersch, 1987). The European integration process was also in the doldrums. In the first half of the 1980s, the issue which dominated the European debate was the British contribution to the European budget, which became famous with Mrs. Thatcher's phrase "I want my money back". A solution was only reached at the Fontainebleau summit of June 1984, clearing the way for the European Community to concentrate on integration furthering projects.

The integration process was relaunched with the European Monetary System (EMS), which was founded in March 1979, under the impulse of the French president Giscard d'Estaing and the German chancellor Helmut Schmidt. Compared with the ambitions of the Werner plan, the European Monetary System was a more modest project. Moreover, the first years were very difficult: there was a lack of convergence of economic policies and performances, especially inflation, and there were several realignments (Mourlon-Druol, 2012).

The development of the EMS was one of the main preoccupations of European policymakers. Tensions in the EMS were exacerbated from May 1981 onwards, when Mitterrand, the new French President, followed an isolated Keynesian policy strategy. This led to a loss of competitiveness of the French economy, capital outflows

and speculative pressures against the French franc, leading to several realignments. After the March 1983 realignment and the change towards more orthodox economic policies in France, the EMS reached more stable waters.

Things would change in January 1985 with the Delors Commission, which developed several projects to reinvigorate the European economy and the integration process. Of special importance was the internal market project, which fitted in with the general tendency towards deregulation. A single European financial market was a key element of it (Maes, 2007). This comprised the free movement of capital, which had always been a key German condition for progress in the area of monetary integration.

The single market program was adopted by the Community. In 1986, following the adoption of the Single European Act, it became a Treaty obligation, the first major revision of the founding Treaties of the Community. The Act greatly extended the scope of the Community, simplified the decision-making process, constituted an early and crucial triumph for the single market project, and further contributed to the renewed momentum of the Community.

The internal market program was also part of a more general economic policy strategy of the Commission, aimed at improving the microeconomic foundations of the economy (Mortensen, 1990, 31). Other important elements of this strategy were wage moderation, budgetary consolidation and increasing the flexibility of markets. During these years, also a new view on industrial policy took shape (Maes, 2002). In the 1980s and 1990s, the emphasis shifted towards a more horizontal industrial policy, where the creation of a favorable environment for firms was encouraged, as well as towards competition policy. This also contributed to reinforce the internal market.

Delors further requested a report by a study group, chaired by Tommaso Padoa-Schioppa (aka TPS), on the implications of the internal market for the future of the Community, which was published with the title *Efficiency, Stability, Equity* (Padoa-Schioppa, 1987). Padoa-Schioppa had been a director general of DG II, the economic

service of the Commission (Maes, 2013). During that period, he got to know Delors, who was then chairman of the economic and monetary committee of the European Parliament. The report contained a warning that the single market (with not only the free movement of goods, but also the liberation of capital movements), was inconsistent with the prevalent combination of exchange rate stability and national autonomy of monetary policy. A thesis TPS elaborated as “the inconsistent quartet” (Masini, 2016).

The European Community continued on the internal market élan. At the summit meeting of Hanover in June 1988, the economic and monetary union was brought back on the agenda. The Heads of State and Government decided to set up a Committee with the task of studying and proposing concrete steps leading towards the economic and monetary union. This Committee, mainly composed of central bank governors and chaired by Jacques Delors, produced its report in April 1989 (Report on Economic and Monetary Union in the European Community, hereafter referred to as Delors Report). As observed by Alexandre Lamfalussy, a member of the Delors Committee and later the first President of the European Monetary Institute, the central bank governors were not in favor of a monetary union: “There never would have been a single currency if the decisions had been left to the central banks” (Lamfalussy et al., 2013, 134). Delors not only convinced the Heads of State and Government to have the committee with the central bankers on it, but also to limit the mandate of the committee to the means of achieving EMU. As Lamfalussy observed, Delors had got the European Council to “task a group dominated by central banks with preparing the way for the bankers’ own suicide. It was absolutely inspired” (Lamfalussy et al., 2013, 135). One of the first studies for the Delors Report was a paper on the Werner Report entitled “The Werner Report Revisited.” As observed by James (2012, 242), it was part of a “carefully planned strategy” by Delors.

## 6. THE WERNER REPORT REVISITED

Besides the members of the committee, four persons played an important role in the work of the Delors Committee: the two rapporteurs: Gunter Baer and Tommaso Padoa-Schioppa (aka TPS) and two close collaborators of Delors, Joly Dixon and Jean-Paul Mingasson. As mentioned before, Padoa-Schioppa was an old friend of Delors and he later became a member of the ECB Executive Board and Italian finance minister; Gunter Baer, a German, who worked with Lamfalussy at the Bank of International Settlements; Joly Dixon, a British citizen, was a member of Delors' private office, where he was responsible for the EMU dossier and Mingasson, a French citizen, was a Deputy Director General at DG II, where he was responsible for the monetary directorate (which reported directly to Delors).

In the Padoa-Schioppa archives there is a copy of the Werner Report with the annotations of TPS. They show very well some key ideas of TPS about EMU and the process to get there. TPS considered as "*critica*" (critical) that the growing interpenetration between the economies would limit the autonomy of national business cycle policies (TPSA-184, WR, 8). For the quantitative orientations which were foreseen for budgetary policy in the Werner Report, he noted "*nessun vero vincolo*" (no real constraint) (TPSA-184, WR, 8). Concerning the technical harmonisations for policy coordination with respect to the financial markets, he wrote "*vago! vago!* (vague) (TPSA-184, WR, 22). Concerning the narrowing of exchange rate fluctuations, he noted "*non si sa quando*" (we don't know when) (TPSA-184, WR, 24). The remarks already show some of the main lines of "The Werner Report Revisited."

The preparatory works for the Delors Committee started quickly after the Hanover summit. Dixon produced a first note on the Werner Report on 14 July, followed by a note by Mingasson on 18 July and a new note by Dixon of 22 July. This last note identified four "intrinsic weaknesses" of the Werner Report: a lack of institutional ambition; an excessively mechanical conception of policymaking; an over-emphasis on the importance of the harmonization of policy in-

struments; a lack of clarity over the independence of the conduct of monetary policy (TPSA-184, fax of Dixon to TPS, 26 July 1998). On 28 July, Dixon produced a new note (of seven pages) with the title “The Werner Report Revisited”.

On 2 August, TPS sent a note of four pages with comments. He emphasized that the main message of the paper should be that stages one and two of the Werner Report had been implemented but that “if the results had not been as good as hoped,” three elements were important: lack of institutional change; lack of a dynamic element; and an unfavorable economic environment. A key argument of TPS was that: “The Werner approach is essentially ‘coordination and recommendation’ rather than ‘institution and decision’” (TPSA-184, fax of TPS to Dixon, 2 August 1998). The paper went through some further drafting sessions and was discussed at the first meeting of the Delors Committee in September 1988.

The “Werner Report Revisited” is divided in four sections bearing the following titles: “Main features of the Report,” “Follow-up to the Report,” “An assessment” and “The post-Werner period.” Already in the first section the tone is set with two key messages: the Werner Report did not pay attention to the process of achieving EMU and the Report did not give much attention to the institutional structure of EMU (Baer and Padoa-Schioppa, 1988, 53). In the assessment section, besides the difficult international environment, the paper highlights four important weaknesses of the Werner Report: (a) “Insufficient constraints on national policies.” According to this view, the Werner Report was based too much on voluntary agreements and guidelines with “insufficient constraints on national policies” being one of its main flaws: “These guidelines had the character of recommendations and there was no provision to ensure their observance. Such an approach could work only as long as there was a sufficiently strong policy consensus and willingness to cooperate. However, once that consensus began to weaken, more binding constraints on national policy would have become necessary” (Baer and Padoa-Schioppa, 1989, 57); (b) “Institutional ambiguities.” It was not always clear who was responsible for which decision; (c) “Inap-

propriate policy conception." The Report was based on a very high degree of confidence in the ability of policy instruments to reach policy goals in a known and predictable way. "This over-optimistic view of the efficacy of economic management gave rise to a rather mechanistic and relatively rigid approach to policy coordination (especially in the budgetary field)." This was typical for the then dominating hydraulic Keynesian paradigm; (d) "A lack of internal momentum." The Werner Report did not envisage an interactive process in which the implementation of certain steps would trigger market reactions that in turn would necessitate further steps towards economic and monetary union.

The paper further emphasized that significant progress had been achieved in the European integration process and that a new policy consensus had been established. It observed that, while at the end of the 1960s there was an agreement on "medium-term planning and fine-tuning," the stagflation of the 1970s had led to a paradigm change: "a new consensus had developed in which attention has shifted towards medium-term financial stability, the supply side of the economy and structural policies" (Baer and Padoa-Schioppa, 1988, 58). In the conclusion, the paper further emphasized that "the full potential of the single market will only be realized with satisfactory monetary arrangements" (Baer and Padoa-Schioppa, 1988, 60).

## 7. THE DELORS REPORT AND THE MAASTRICHT TREATY

The Delors Report played a crucial role as a reference and anchor point in further discussions, just as the Werner Report had done nearly two decades earlier. It was a crucial phase on the road to the Maastricht Treaty which provided for the constitutional framework for Europe's economic and monetary union (Dyson and Featherstone, 2000). Like the Werner Report, the Delors Report basically revolved around two issues: first, which economic arrangements are necessary for a monetary union to be successful; and second, which

gradual path should be designed to reach an economic and monetary union.

Initially, the relation between Delors and Karl-Otto Pöhl, the President of the Bundesbank, was rather tense. However, the crucial aim of Delors was to get a unanimous Report (Maes and Péters 2020). So, he took a low profile and focused on seeking out a consensus. As observed by Dixon, Delors “took it very gently. We started with history; we went back to the Werner Report; we went very very gently” (JDI, 11). Delors also asked Pöhl to sketch out his vision for a future EMU, something which Pöhl could not refuse. As observed by Lamfalussy, with that maneuver, Delors had rendered Pöhl and the Bundesbank “captive” (Lamfalussy et al., 2013, 136).

In his contribution, Pöhl took a “fundamentalist” position and emphasized the new monetary order which had to be created: “Above all agreement must exist that stability of the value of money is the indispensable prerequisite for the achievement of other goals. Particular importance will therefore be attached to the principles on which a European monetary order should be based” (Pöhl, 1988, 132). He argued for price stability as the prime objective of monetary policy, which had to be conducted by an independent central bank. Pöhl further emphasized the “indivisibility of monetary policy,” that decisions should be taken either at the national level or by a common central bank. In defining the necessary conditions for a monetary union, the Delors Report referred to the Werner Report. On the institutional level, the Report proposed the creation of a “European System of Central Banks.”

Pöhl’s fundamentalist approach was deeply influential in the Delors Report and would inspire a number of principles that figured prominently in the Maastricht Treaty (Padoa-Schioppa, 1994, 9). The Delors Committee took great care to work out first its view on the final stage of EMU, especially the monetary pillar. This was a major contrast with the Werner Committee. The Delors Report proposed, at the institutional level, the creation of an independent “European System of Central Banks,” to be responsible for the single monetary policy, with price stability as the ultimate aim. In the discussions on

the independence of the central bank, Pöhl received valuable support from de Larosière, for whom the Delors Committee presented an opportunity to increase the independence of the Banque de France (Maes and Péters, 2021).

During the meetings, a crucial issue was whether fiscal discipline could be left to market forces. There were discussions about a “Centre for Economic Policy Coordination” in the Committee, but these ideas were not taken up (Maes 2024). The Report called for “both binding rules and procedures” in the area of budgetary policy (Delors Report, 28). The economic pillar of EMU would remain a difficult issue.

It is interesting to note that Lamfalussy and Duisenberg also argued in favor of giving the European Central Bank a role in the area of banking supervision (Minutes of the fourth meeting of the Delors Committee, DCA). However, they did not really pursue this issue and the Report only mentioned that the new System “would participate in the coordination of banking supervision policies” (Delors Report, 26).

To attain an economic and monetary union the Delors Committee proposed three stages which, in contrast to the emphasis put by the Werner Report on the first stage, were all developed in considerable details. From an institutional and legal point of view these stages implied the following: the preparation of a new Treaty (first stage), the creation of a new monetary institution (European System of Central Banks, second stage), and the transfer of responsibilities to this new institution (third stage). From an economic and monetary point of view, these stages implied an increased convergence and a closer coordination of economic policy. However, the Committee underlined the indivisibility of the whole process: “the decision to enter upon the first stage should be a decision to embark on the entire process” (Delors Report, 31).

The European Community followed the path indicated in the Delors Report. The first stage started in July 1990 and the intergovernmental conference on economic and monetary union, along with another one on political union, opened in Rome in December 1990.

Meanwhile, the broader European scene was changing dramatically with the breakdown of the iron curtain and the unification of Germany, speeding up the process of European monetary integration. The German government's policy line could almost be summarized in Thomas Mann's dictum: "Wir wollen ein europäisches Deutschland und kein deutsches Europa."

During the Maastricht Treaty negotiations, there were significant discussions on the European economic governance. It led to an EMU with a well elaborated monetary pillar but a weak economic one, as the transfer of sovereignty for economic policy was not acceptable for the Member States (Maes, 2004). Monetary policy was centralized. It was the responsibility of the European System of Central Banks, made up of the European Central Bank and the national central banks, which were all independent. The primary objective of the monetary policy is price stability. The responsibility for other instruments of economic policy, like budgetary policy and incomes policy, remained basically decentralized, resting with the national authorities. However, member states had to regard their economic policies as a matter of common concern and coordinate them accordingly. Important elements in this coordination process were the Broad Economic Policy Guidelines, the multilateral surveillance process and the excessive deficit procedure (with two reference values: 3% of GDP government deficit and 60% of GDP for government debt).<sup>5</sup> However, as history would show, there was a repeat of "insufficient constraints on national policies" as warned for in "The Werner Report Revisited." The different conceptions of monetary union and economic union reflected the limits of the willingness of the member states to give up national sovereignty. As Bordo and Jonung (2000, 35) observe, EMU is quite unique in history, being a monetary union among countries retaining their political independence.

An important topic in later EMU negotiations was the "Stability and Growth Pact" (SGP). Discussions were launched with the pro-

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<sup>5</sup> There was also the no bail out clause, that countries remained solely responsible for their debts.

posal by Theo Waigel, the German finance minister, in November 1995, that a “Stability Pact for Europe” should be concluded. This would tighten the rules on budgetary behavior for EMU participants and include potential sanctions. After long and extended negotiations, a political agreement was reached at the Dublin Summit in December 1996.

## 8. THE 21<sup>ST</sup> CENTURY CRISES

The first decade of Euro was, with hindsight, relatively quiet. There was however a crisis around the SGP, with the Commission taking Germany and France to the European Court of Justice that in 2005 led to a first reform of SGP. The second decade was much more tumultuous, with the Great Financial Crisis (starting in 2007 with problems in the US subprime mortgage market) and the Euro Area debt crisis, all of which were accompanied by vivid economic debates (Buti, 2021). To counteract the deflationary consequences of the Great Financial Crisis, policymakers adopted expansionary budgetary and monetary policies, which marked a return of Keynesian economics. The sovereign debt crisis became a watershed in the process of European integration. European economic policymakers responded with a range of measures, that were not limited to emergency assistance, fiscal consolidation programs and “non-conventional” monetary policy but envisaged also substantial reforms in the European economic governance. In the first instance, in the light of the major budgetary derailments in Greece, the focus was on strengthening fiscal sustainability. Moreover, major competitiveness imbalances and asset boom-bust cycles were important factors behind the crisis, as clearly shown in Ireland and Spain. It showed that asymmetric shocks could not only originate in the public sector (the focus in the Delors Committee), but also in the private sector. Consequently, a new Macroeconomic Imbalances Procedure was set up. The aim was to create a system of ex ante surveillance of macroeconomic risks and competitiveness positions. The European Union also set up new

financial stabilization mechanisms to provide for financial solidarity, especially the European Stability Mechanism. Moreover, important steps were taken to establish a Banking Union. Setting up the Single Supervisory Mechanism was a significant step in the European integration process, probably the most important one since the introduction of Euro. The completion of the Banking Union remains however on the agenda (Véron, 2024).

The covid-19 pandemic, which swept through Europe in 2020, had also significant economic consequences. The European Central Bank set up a Pandemic Emergency Program but there was also a strong consensus that a Keynesian type of budgetary impulse was necessary to avoid a depression. The Stability and Growth Pact was then suspended in 2020. Moreover, new initiatives at EU level were launched, especially the Next Generation EU (with the Recovery and Resilience Facility). The aim was not only to boost aggregate demand but also to support the most hard-hit countries (a form of ex post insurance for countries that were hardly hit by the pandemic) and strengthen the economic growth potential of the EU (with a focus on the green and digital transitions). However, the “whatever it takes” fiscal policy contributed to significant government deficits and increases in government debt in several countries. In the summer of 2021, inflation started to rise again. With the end of covid-19 as a pandemic, the issue of a normalization of policies came to the foreground, resulting also in a revision of the Stability and Growth Pact.

## 9. CONCLUSION

During the second half of the 20<sup>th</sup> century, there was an important shift in economic paradigms, both in the academic community and among policymakers. While in the 1960s Keynesian economics, a belief in discretionary economic policy dominated, in the second half of the 1980s there was a broad consensus on medium-term stability-oriented policies. This shift towards a more stability-oriented stance

of economic policy was clearly reflected in the EMU debates in Europe.

Of crucial importance for the development of the European Union was the way that a further push towards integration fitted into this new (neo-liberal) conceptual framework. The completion of the internal market, with the elimination of the remaining barriers to a free flow of goods, services, persons and capital, was compatible with the deregulation strategy being pursued in the various European countries. Macroeconomic policy in the countries of the European Community became more stability oriented, as policymakers became convinced of the illusory nature of the tradeoff between inflation and unemployment. This orientation fitted in with a policy of stable exchange rates and a move towards EMU that would have a strong monetary pillar and a weak economic pillar. This was an element of weakness when the Euro area was confronted with severe challenges in the 21<sup>st</sup> century.

On 1 January 1999, EMU effectively was launched with the participation of eleven countries. The question is why this attempt was successful, in contrast to the fate of the Werner plan in the 1970s. Two types of factors can be underlined: first, long-term structural developments which created a favorable background (a greater degree of economic and financial integration, a greater consensus on policy objectives and an increasing underlying political will to achieve European integration, as exemplified in the Kohl Mitterrand tandem) and, second, the dynamics of the process of European integration in the 1980s and 1990s. It was the period when "history accelerated" (Delors, 1992), creating a "window of opportunity," which has been skillfully exploited with the help of appropriate policy-decisions and meticulous preparations. However, on numerous occasions the project could have easily derailed. It could therefore be argued that the achievement of EMU should not be taken for granted.

The sovereignty transfer of monetary policy to the European level, was certainly not an easy decision from a German perspective and German economic policymakers, like the Bundesbank accepted

it out of compliance with a democratically taken decision. For Kohl it was a step towards a United States of Europe, a recurring theme in his speeches. He knew that France would only accept this if monetary union was in it. But the transfer of monetary sovereignty was a maximum. Countries did not accept further important transfers of economic policymaking. This led to an EMU with a strong monetary pillar, but a weak economic pillar.

In this paper considerable attention was paid to a background study for the Delors Report, "The Werner Report Revisited." This study highlighted four "intrinsic weaknesses" of the Werner Report: absence of internal momentum, inappropriate policy conception, institutional ambiguities and insufficient constraints on national policies. An interesting question is how these issues have played out in the Maastricht Treaty framework.

With the implementation of EMU, it is clear that policymakers succeeded in creating internal momentum, with a positive dynamic between policy initiatives and the working of market forces. Maybe there was also some luck involved, but there was certainly also a strong political will.

As regards an "inappropriate policy conception," one can only observe that the world has gone through several paradigm changes. It shows a certain relativity of economic theory. It is then important for policymakers to take an instrumental approach to economic theory and to identify the most appropriate economic theories. A broad and pluralist approach towards economics, involving also historical research, can hereby help. Theories are techniques of thinking and remain partial. So, it is important to select theories which highlight the relevant features of reality. The great Austrian economist Joseph Schumpeter (1954: 15), approvingly referred to Henri Poincaré's observation, "tailors can cut suits as they please; but of course, they try to cut them to fit their customers."

Regarding institutional ambiguities, the picture is mixed. For the monetary side of EMU, a strong institutional pole has been created with the European Central Bank and the Euro system. A testimony of this is that the tasks of ECB have been extended with important

responsibilities in banking supervision. However, EMU remained incomplete, with the competences of economic policy remaining mostly at the national level. Given the absence of a significant central fiscal capacity at the EU level, rules for budgetary policy have to take into account the different roles which national budgetary policies have to fulfil (not only sustainability but also stabilization of the national economy).<sup>6</sup>

“The Werner Report Revisited” highlighted very much the “insufficient constraints on national policies”. However, regarding the Maastricht Treaty framework and the Stability and Growth Pact, the situation is not much better. One could argue that the expression, “The Werner approach is essentially ‘coordination and recommendation’ rather than ‘institution and decision’” does also apply to the economic pillar of the Maastricht Treaty framework. Why this weakness has not (yet) been corrected raises some fundamental political economy questions regarding the conception and implementation of a sound economic governance framework. They not only concern issues of national sovereignty but are also related to the multidimensional aims of fiscal policy (with the Musgravian triad of allocation, stabilization and redistribution) as well as to the need for keeping the public finances sustainable.

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<sup>6</sup> The European Commission (1990) emphasised three aspects of (national) budgetary policies: autonomy (to respond to country-specific problems), discipline (to avoid excessive deficits) and coordination (to assure an appropriate policy-mix in the Community).

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