Where the EMS stands now

French President Giscard's summit eve speech over French national television summarized the prospects for the European Monetary System (EMS) succinctly: the EMS has provided a zone of stability against the West's "extravagant monetary disorder," but will not succeed unless it expands to solve the underlying problems of world development.

Only half of the original conception behind the EMS, which the European Community nations minus Great Britain founded July 6, 1978, is in effect. At that meeting, European leaders set out a two-step plan: a European Monetary System to establish fixed currency parities and pooled reserves to defend them, and, later, a European Monetary Fund to act in the world arena. A Bonn official then characterized the new institutions as "the seed crystal for an institution that will replace the World Bank and International Monetary Fund." The European Monetary Fund was originally scheduled for implementation in early 1980, a schedule which President Giscard reaffirmed in his television address.

The basis for the creation of a new fund has already been established through the pooling of 20 percent of European nations' gold reserves, valued at market price for purposes of setting members' drawing rights on EMS resources. The gold holdings of EMS members are now worth over $160 billion at the current gold price, and the value of gold in the EMS pool is $32 billion. The EMS pool, now placed in the Fund for European Monetary Cooperation, also includes foreign exchange reserves of over $20 billion.

As Giscard emphasized, the currency stability features of the system—however well they have worked so far—cannot survive without the credit features. Until the eve of the Iranian crisis, the EMS provided shelter for extremely high rates of European private-bank lending to developing countries, which financed continued high European exports. However, Europe will require government muscle to provide a continued flow of export credits to its markets in the developing world and the Comecon, particularly since the private financial markets are now paralyzed by financial warfare.

The European Monetary Fund

The European Monetary Fund is designed to provide direct loans to non-European Community nations for trade and development, at lower-than-commercial interest rates. The French and West German governments intend to expand the EMS to include Europe's trading partners, replacing the Bretton Woods institutions. The French have negotiated possible links between the new Arab Monetary Fund and the European Monetary Fund. In a Feb. 26 statement on Mexican television, Giscard offered to Mexicans direct monetary cooperation when the European Monetary Fund comes on line. French sources report that Giscard intends to bring the Soviet Union into the European system during early 1980.

The scope of what the European Monetary Fund intends to accomplish is much broader than its $70 billion resources—impressive as this figure is—would indicate. EMF gold reserves are the future reserve basis for a general reorganization of the Eurocurrency markets. Even though European private banks during 1979 took a dominant role in private Eurodollar lending, especially to developing countries, the limits of such operations under the present credit market environment are severe. Average maturity of deposits in that market is less than 30 days, and the post-Oct. 7 interest rate situation makes stable lending impossible. Therefore, the European plan is to consolidate Euromarket funds, possibly with direct help from major OPEC depositors, into low-interest and long-maturity assets at the European Monetary Fund. This could most efficiently be accomplished, European leaders agree with the suggestion of Lyndon H. LaRouche, through the issuance of gold-denomination bonds at low interest rates. Gold denomination of interest and principal repayments would guarantee investors a positive rate of return after inflation and permit the sale of such bonds with coupon yields of about 4 percent.

Britain is still the only member of the European Community to refuse to join the EMS, first on the grounds that the pound sterling was too weak, and then on the grounds that the collapse of the dollar would draw Arab funds into London, creating a "petro-pound" stronger than the European currencies. The EMS financial reorganization plan, when fully realized, would eliminate the City of London, the principal seat of the present Eurodollar market, and London has bitterly opposed the plan since its inception.