What are the necessary conditions for an Asian currency? – 7 Lessons from the history of EMU –

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A. Introduction

In the past decade, a large number of studies and discussions have been carried out as to the idea of an "Asian currency" or an "Asian Monetary Union". The background for these ideas could be the Asian financial crisis in 1997/1998 which showed the importance of currency stability within an economically integrated area. Also, the idea could have arisen under the inspiration of the introduction of the Euro in 1999.

Until now, the studies on the idea of an Asian currency seem to be composed of two fields; economic analyses mainly examine whether the East Asian area[1] constitutes an Optimal Currency Area (OCA), and political analyses discuss, for example, on whether an Asian currency would be practicable as regards international relations in East Asia, or whether a political will for it actually exists.

Economic analysis on an Asian currency is beyond this paper, thus this paper shall not examine it closely, but shall briefly point out some important lessons from Economic and Monetary Union (EMU) – Lesson 5, 6 and 7. As to the discussions on the political side, however, two points are still to be cleared when comparing Europe and East Asia: (1) What kinds of political situations and political wills were behind the history of EMU? (2) Which factors supported these political decisions?

The answers for question (1) will be discussed in Chapter C (Lesson 1 and 2) and, as to the question (2), this paper emphasises the role of institutionalisation, especially the role of legalisation which has gradually institutionalised political decisions (Lesson 3 and 4).

It should be noted that this paper takes neither side of the argument about whether the East Asian countries should or could introduce a common currency. As we shall see in Chapter B, the introduction of an Asian currency seems to be a project for the long term, and it might be too early to determine the possibility of it based on the present economic and political situation in East Asia. Keeping a distance from pro and con arguments on an Asian currency, this paper tries to

1 There is no decisive definition of "East Asia". In this thesis, unless otherwise noted, the term East Asia denotes ASEAN+3 which is composed of ten countries of the Association of Southeast Asian Nations (ASEAN: Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand and Vietnam), China, Japan, and the Republic of Korea. The reasons for this definition are (1) historically, ASEAN+3 was established after the Asian financial crisis (1997/1998) as one of the potential solutions of which the idea of an Asian currency has been discussed, (2) institutionally, main frameworks of financial co-operation in East Asia are formulated under ASEAN+3 framework such as the Chiang Mai Initiative Multilateralization (CMIM), the Asian Bond Markets Initiative (ABMI), as we will discuss in Chapter C. As to the discussion on possible East Asian frameworks, see *Munakata*, Transforming East Asia, The evolution of regional economic integration, 2006, pp. 102-108.

derive general lessons from the European experience on the way to EMU. The results will be applied to East Asia taking into account the different historical, economic and political backgrounds of both areas. In this way, this paper tries to find a series of necessary conditions for an economic and monetary union as a barometer for an Asian currency.

This paper consists of three parts: Chapter B overviews the idea of an Asian currency and analyses it in the context of regional integration theories. Chapter C deals with the history of EMU from which seven general lessons could be drawn for an economic and monetary union. Chapter D deals with the present political and economic situation in East Asian, and applies lessons from EMU to the idea of an Asian currency.

B. Theories of regional integration

I. Discussions on an Asian currency and the background

Before turning to a closer examination of the idea of an Asian currency, we must draw our attention to the regional economic integration in East Asia. With the constant development of East Asian intra-regional trade after the 1980s, the intra-regional trade ratio within the East Asian countries grew to 55.5 % in 2004, compared with only 37.1 % in 1985. The number in 2004 was at a similar level to the European intra-regional trade ratio in 1985 which amounted to 59.8 %, whereas it grew to 67.9 % in 2004. Even though there was a higher level of economic interdependency among the East Asian countries driven by trade in general and Foreign Direct Investment (FDI) with production networks,[2] there was a limited regional framework to cope with the financial and currency crisis when it happened in 1997/1998, and thus the Asian financial crisis caused serious economic damage to East Asian countries. This currency crisis contagion was the original incentive for East Asian countries, especially for the ASEAN+3 countries, to establish the current frameworks of monetary co-operation in this area.[3] Also the idea of an Asian currency arose from such an incentive, together with the successful introduction of the Euro in 1999. Therefore, the Asian financial crisis has been seen as a catalyst for East Asian regionalism.[4] So – after the Asian financial crisis –

2 *Kawai*, Evolving Economic Architecture in East Asia, ADB Institute Discussion Paper No. 84, 2007, p. 2.

3 Such as the Chiang Mai Initiative Multilateralization (CMIM), the Asia Bonds Market Initiative (ABMI) and Executives' Meeting of East Asia and Pacific Central Banks (EMEAP) as we will see in Chapter D.

the idea of an Asian currency has been intensively discussed at a governmental[5] and academic level.[6]

According to a study by the Bank of Japan, three steps basically come out of the studies for an Asian currency;[7]

Step 1: Adoption of the "basket, band and crawl" system[8] by East Asian countries.

Step 2: Unification of the weights of currencies in each country's basket.

Step 3: Introduction of a common currency.

The aim of this idea is to find possible solutions in East Asia in order to stabilise currencies and to avoid a future currency crisis in this area.

However, it should be noted that a monetary union or a common currency is one of the most advanced forms of regional integration in the sense that participating countries lose certain sovereignties with it.[9] This is not only an economic subject, but also a political subject which requires the examination of the whole context of regional integration, especially the political situation and political will as regards regional integration. For this reason, we shall examine the history of EMU by taking political aspects into account.

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4 *Padoa-Schioppa*, Regional economic integration in a global framework, European Central Bank, 2005, p. 30: "The crisis has played such a pivotal role because it has made the Asian countries realise, no doubt in a painful way, that they are closely tied together economically."

5 ASEAN+3 May 2006 Communiqué endorsed a research topic on "Toward greater financial stability in the Asian region: Exploring steps to create regional monetary units".

6 *Murase*, Monetary and Financial Co-operation in East Asia (Japanese title: Higashi-ajia-no tsuka-kinyu kyouryoku), 2007; *Walter*, Asian Regional Integration by Learning from Europe and the Euro: The Possibilities of the East Asian Community (EAC), The 14th Osaka University (OCU) International Academic Symposium, 2006; Institute for International Policy Studies, Prospects for the Global Economic and Financial System in the 2030s, 2009.

7 Bank of Japan, Is the road from Asian Monetary Unit to Currency Union far? (Japanese title: Ajia tsuka tan-i kara tsuka dome made wa toi michi ka), Working paper series No. 06-J-21, 2006, summarises the existing studies on an Asian currency and concludes that there are mainly three steps towards it.

8 The "basket, band and crawl" (BBC) system is a system in which a currency is managed against a basket of currencies of its main trading partners. For example, US dollar, Euro and Japanese yen might be one of the possible combinations in the case of East Asia. Under this system, the exchange rate of the currency floats within a certain range (band) in order to avoid a sharp fluctuation. Singapore introduced this system in 1981. *Ong*, The impact of globalisation on the formulation and implementation of monetary policy in Singapore, BIS papers No. 23, 2005, pp. 263-268.

9 If participating countries introduced a common currency, they would loose their monetary policy and seigniorage. Also, monetary co-operation such as a "Snake" or EMS requires a certain level of common policy which could restrict domestic economic policies for currency stability.

II. Theories of regional integration

Before we continue comparing Europe with East Asia, we take an overview of the various theories of regional integration to start with.

Balassa[10] outlined five steps for the development of regional integrations based on economic viewpoints, i.e. (1) free trade area (FTA), (2) customs union, (3) common market,[11] (4) economic union,[12] (5) complete economic integration.[13] In order to classify the present regional integration around the world, it is useful to work with *Balassa's* model.

In this classification, EMU can be seen as stage 4, and the most advanced integration among existing regional integrations. By contrast, ASEAN – the most integrated area in Asia[14] – is classified only as stage 1 according to *Balassa's* model, and other existing FTAs and EPAs in East Asia are also classified as stage 1.

It should be noted that the European Community (EC) already tried to establish an economic and monetary union when it was classified as stage 2 in 1970s when the Common Market was not completed, although a common market is said to be a necessary precondition for step 4, and it failed. It is important to note that, even if the actual economic needs and political wills towards a common currency exist, it could fail, and the reasons for this failure will be examined in Chapter C from institutional aspects.

Concerning monetary aspects of regional integrations, *Dieter* proposed a theory called "monetary regionalism".[15] This theory claims the need for a new classification of regional integration instead of the *Balassa's* classic theory on the grounds that today the monetary function of regionalism plays a more important role than the free movement of goods.[16] This theory emphasises the stability of currencies

10 *Balassa*, The Theory of Regional Integration, 1961, p. 2.

11 In a common market, "not only trade restrictions, but also restrictions on factor movements are abolished", ibid.

12 An economic union "combines the suppression of restrictions on commodity and factor movements with some degree of harmonization of national economic policies, in order to remove discrimination that was due to disparities in these policies", ibid.

13 A complete economic integration "presupposes the unification of monetary, fiscal, social, and countercyclical policies and requires the setting-up of a supra-national authority whose decisions are binding for the member states", ibid.

14 *Sakakibara/Yamakawa*, Market-driven regional integration in East Asia, European Central Bank, 2005, p. 40. Website of ASEAN shows detailed information about ASEAN Free Trade Area (AFTA), http://www.aseansec.org/4920.htm (1/9/2011).

15 *Dieter*, Exploring alternative theories of economic regionalism: from trade to finance in Asian co-operation?, Review of International Political Economy 10 (2003), pp. 430-454.

16 Ibid. This theory claims that the *Balassa's* theory lacks the link between the first three stages which are characterised by trade and monetary regionalism from the fourth stage.

and financial markets in a region without having to formalise trade links and suggests the following four levels of monetary regionalism:

(1) regional liquidity fund,

(2) regional monetary system with exchange rate bands,

(3) economic and monetary union,

(4) political union.

Even with this theory, the East Asian area can only be classified as level 1, because there is no exchange rate band whereas there is a regional liquidity fund, the Chiang Mai Initiative Multilateralization (CMIM).[17] By contrast, EMU could be classified as level 3.

III. Conclusion

As seen above, (1) there are many academic ideas about the steps towards an Asian currency, but (2) a monetary union should be examined not only from the viewpoint of monetary policy but also from the viewpoint of the political situation and political motivation as regards regional integration as a whole. In addition, (3) the level of East Asian integration is still at a lower level when it comes to thinking of an Asian currency, even if it is examined with classifications of monetary regionalism and thus, introduction of an Asian currency will probably be a project for the long term.[18] This is why this paper takes neither side of the argument about whether the East Asian countries should or could introduce a common currency based on the present economic and political situation. In this way, there is still a large gap between European integration and East Asian integration and thus, we should start from the beginning of the history of EMU when comparing the situation in East Asia.

17 In detail, see Chapter D.

18 *Park/Wyplosz*, Monetary and Financial Integration in East Asia: The Relevance of European Experience, European Commission Economic papers 329, 2008, p. 118, take a similar view.

C. Lessons from the history of European integration and EMU

I. The history of European integration and EMU

In the post-Second World War era, the establishment of the European Coal and Steel Community (ECSC) of 1952[19] was an important turning point for European integration. After the establishment of the ECSC and the European Economic Community (EEC, 1958), there were several moves towards monetary union which were undertaken during the 1950s and the 1960s, such as the so-called "Marjolin Memorandum" on 24 October 1962.[20] However, in reality, the Member States did not need a measure for currency stability at the Community level, because the Bretton Woods system was ensuring widespread exchange rate stability[21] and no follow-up had been executed for the Marjolin Memorandum.[22]

By contrast, from the institutional point of view, the three supranational institutions, the ECSC, the EEC and the European Atomic Energy Community (EAEC) gradually exercised spill over effects on further integration together with the development of the supranational legal system,[23] as we will discuss later in this chapter.[24]

After a series of currency crises in late 1960s, European countries started to cope with these crises using the framework of the Community. This was the starting point of the 40 years of history leading to establish EMU. Let us start with setting up three periods of the history of EMU in order to analyse the characteristics of the political and economic situation in each attempt.

19 The ECSC Treaty was signed in 1951 and entered into force in 1952.

20 This memorandum called for an economic union by the end of the 1960s with irrevocably fixed currency exchange rates within the Member States. Other movements in the field of macroeconomics and currency at the Community level were the establishment of a Committee of Governors of the central banks of the Member States of the EEC in 1964. Also, the Currency Committee (1958), the Short-term Economic Policy Committee (the Council Decision of 9 March 1960, OJ 31 of 9/5/1960, p. 764/60), the Budgetary Policy Committee (the Council Decision of 8 May 1964, OJ 77 of 21/5/1964, p. 1205/64) and the Medium-term Economic Policy Committee (the Council Decision of 15 April 1964, OJ 64 of 22/4/1964, p. 1031/64) were established in this period.

21 ECB, The European Central Bank – History, Role and Functions, 2006, p. 17.

22 *Selmayr*, Das Recht der Wirtschafts- und Währungsunion, Bd. 1 – Die Vergemeinschaftung der Währung, 2002, p. 123; ECB, (fn. 21), p. 17.

23 It should be noted that the European Court of Justice (ECJ) made clear in its case-law that there were, prior to the Lisbon Treaty, three legally distinct Communities, *Zilioli/Selmayr*, The Law of the European Central Bank, 2001, p. 5. As to the concept of "supranationality", *Selmayr*, (fn. 22), pp. 81-83.

24 Lesson 3 and 4.

1. Period 1: Werner report and the "Snake" – Political attempt without economic co-ordination

The first attempt to create an economic and monetary union was a reaction to the currency crisis in 1968/1969 caused by the gradual collapse of the Bretton Woods system, which threatened the development of the Common Market.[25] European countries tried to stabilise their currency rates and the Commission proposed a memorandum in February 1969, the "Barre Plan" which aimed for economic and monetary union.[26] On the basis of this plan, a working group chaired by *Werner*, the Prime Minister and Minister of Finance of Luxembourg, published a report (the Werner report) on 8 October 1970 proposing an economic and monetary union in three steps by 1980.[27]

After long discussions on this report,[28] the Member States agreed to establish an economic and monetary union on March 1971.[29] They started a monetary co-ordination system called the "Snake in the Tunnel" meaning that the Central Banks of the Member States were requested to intervene in foreign exchange markets to keep the spot exchange rates of two Member States within the band of 2.25 %[30] ("Snake"), and this range of currency rates had to move within a theoretical band of +/- 2.25 % against the US Dollar ("Tunnel").[31]

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25 See Lesson 6.

26 Commission Memorandum to the Council regarding the formulation of a plan by stages with a view to the creation of economic and monetary union of 12 February 1969.

27 This report proposed three stages (first stage, second stage and final stage) to an economic and monetary union. Report to the Council and the Commission on the realisation by stages of Economic and Monetary Union in the Community of 8 October 1970.

28 As to a detailed discussion on this report, *Tietmeyer*, Herausforderung EURO, 2005, pp. 51-55.

29 The Council adopted one Resolution and three Decisions: the Resolution on the attainment by stages of economic and monetary union in the Community, (OJ C 28 of 27/3/1971, p. 1), the Decision 71/141/EEC on the strengthening of the coordination of short-term economic policies (OJ L 73 of 27/3/1971, p. 12), the Decision 71/142/EEC on the strengthening of co-operation between the central banks (OJ L 73 of 27/3/1971, p. 14), the Decision 71/143/EEC on the implementation of a medium-term financial assistance mechanism (OJ L 73 of 27/3/1971, p. 15).

30 The Resolution on the application of the Resolution on the attainment by stages of economic and monetary union in the Community of 21 March 1972, OJ C 38 of 18/4/1972, p. 3. The legal analysis of this Council Resolution in Lesson 3.

In June 1973 the European Monetary Co-operation Fund (EMCF) was founded. (Regulation (EEC) No 907/73 of the Council of 3 April 1973, OJ L 89 of 5/4/1973, p. 2). Also the Council adopted a Decision on the attainment of a high degree of convergence in the Community and the Directive on stability, growth and full employment. Council Decision 74/120/EEC of 18 February 1974, OJ L 63 of 5/3/1974, p. 16.

31 This range was agreed at the Smithsonian Agreement in December 1971.

However, many countries withdrew from the system under severe economic pressure in the 1970s, i.e. the first oil shock with high inflation rates, the *Nixon* shock and the divergence of economic policies among the participating countries. In this situation, the Snake left the Tunnel because of the collapse of the Bretton Woods system and the start of a free-floating exchange rate system (March 1973). Under the high inflation caused by the first oil shock in 1973/1974, many currencies were withdrawn from the system. The "Snake" became a "mini-snake" which was composed of only the German Mark, Benelux currencies and the Danish krone.[32] In this way, "by the mid-1970s the process of integration had lost momentum under the pressure of divergent policy responses to the economic shocks of the period".[33]

2. Period 2: The EMS – A pragmatic approach under an intergovernmental framework

The second attempt to create a monetary union was the European Monetary System (EMS). With their strong collaboration, *Giscard* and *Schmidt* co-proposed currency co-operation at the European Council in Copenhagen on 7/8 April 1978.[34] After intensive discussions, the European Council decided to establish the EMS under which Member States had to keep currency rates within a band of +/- 2.5 % (alternatively Member States could select a band of +/- 6 % as a transitional measure) around the European Currency Unit (ECU).[35]

Basically the EMS was not significantly different from the Snake in the sense that the EMS was build around a grid of fixed but adjustable central rates among the participating Community currencies,[36] while the EMS introduced the ECU which was defined as a basket of fixed quantities of the currencies of the Member States and was set at the centre of the system.[37]

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32 For a while, the Swedish Krona and Norwegian Krone took part in the system. ECB, (fn. 21), p. 18.

33 The Delors Report, 1989, para. 2; *Dinan*, Europe Recast, 2004, p. 148.

34 Annex to the conclusion of the presidency of the European Council in Bremen of 6/7 July 1978. *Dinan*, (fn. 33), p. 173 et seq.

35 Council Regulation (EEC) No 3181/78 of 18 December 1978 relating to the European monetary system, OJ L 379 of 30/12/1978, p. 2. Admitting the role of the ECU in the market, however, Delores Report (1989) concluded that the results of the EMS were insufficient reasoning as follows: "Community countries have not yet joined the exchange rate mechanism. [...] The lack of sufficient convergence of fiscal policies. [...] The transition to the second stage of the EMS and the establishment of the European Monetary Fund, as foreseen by the Resolution of the European Council adopted in 1978, have not been accomplished."

36 ECB, (fn. 21), p. 19.

However, due to change of economic ideology in the 1980s from keynesian to neoliberalism represented by Thatcherism and Reaganomics, most of the Member States including France changed the direction of the economic policies drastically. Especially after the currency crisis in March 1983,[38] *Delors*, the then French Finance Minister, under the President *Mitterrand* introduced a disinflationary monetary policy and restrictive fiscal policy.[39] Together with these economic policies, the EMS stabilised the currency rates within the European countries.[40]

3. Period 3: The SEA and the Maastricht Treaty – Deeper and wider political integration

The Single European Act (SEA),[41] which was signed on 17 February 1986 and entered into force on 1 July 1987, was the first major amendment of the Treaty establishing the EEC. It aimed for the creation of the single market by the end of 1992 as its objective.[42] As to economic and monetary policy, a new chapter was inserted in the EEC Treaty which referred to an Economic and Monetary Union,[43] although the objectives of the EEC were unchanged.[44]

The Single Market program attracted investments in Europe. Economic boom arose in the late 1980s. Using this momentum of success of the SEA, *Delors*, the

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37 Agreement between the central banks of the Member States of the European Economic Community laying down the operating procedures for the European Monetary System of 13 March 1979.

38 As a solution for the crisis, the Member States agreed to readjust the central rates of currencies on 21 March 1983. Agreement of the Ministers and Central Bank Governors of the Member States on a readjustment of central rates within the EMS (changes in bilateral central rates: +5.5 % the German Mark, +3.5 % the Dutch guilder, +2.5 % the Danish krone, +1.5 % the Belgian and Luxembourg francs, -2.5 % the French franc and the Italian lira, -3.5 % the Irish pound). EC Bulletin, No 3-1983, p. 26.

39 *Dyson/Featherstone*, The Road to Maastricht, 1999, p. 148 et seq.: "Particular stress was placed on giving long-term support to the franc stable by measures to restore corporate profitability, to decentralize wage bargaining, to strengthen the role of banks in industrial financing (on the German model), and to restructure public spending by reinforcing its social dimension (for instance, towards vocational training and infrastructural investment)".

40 Ibid., p. 691 et seq.: "His [Delors'] achievements in the latter role would have been impossible, and any EMU treaty negotiations abortive, in the absence of the conversion of the French government to a policy of rigueur in the framework of a commitment to the ERM in 1982-3." *Tietmeyer*, (fn. 28), p. 92 et seq.

41 OJ L 169 of 29/6/1987.

42 Art. 8A Treaty of EEC (TEEC).

43 Art. 20 SEA. A new Chapter I was inserted in Part Three, Title II of the EEC Treaty, starting with the title: "Chapter I Co-operation in economic and monetary policy (Economic and Monetary Union)".

44 Art. 2 TEEC.

President of the European Commission, forwarded a plan for the creation of economic and monetary union. The Hanover European Council on 27/28 June 1988 entrusted "to a Committee the task of studying and proposing concrete stages leading towards economic and monetary union".[45] The Committee was chaired by *Delors*, and the Presidents or Governors of central banks of member states took part. In April 1989, the final report of the "Delors Committee" was published and outlined a three-steps plan for economic and monetary union.[46] The three steps shown in the Delors report were put onto the schedule for European integration and ended with the Maastricht Treaty in 1992.

As a whole, the progresses to EMU from the late 1980s to the early 1990s were supported by a positive economic situation and political euphoria about European integration.[47] A few years later, after the signing of the Maastricht Treaty, the economic and political situation in Europe became worse and the euphoric mood disappeared. There were currency exchange rate crises at the beginning of the 1990s, economic growth slowed down.[48] Political leaders had been changed in many Member States and some of the new political leaders complained about the convergence criteria which were set in the Treaty as a precondition for EMU.[49] However, even with such difficulties, the steps and schedules laid out in the Maastricht Treaty were automatically implemented, as we will see later, and EMU started on 1 January 1999 after 40 years of attempts.

II. 7 Lessons derived from the history of EMU

As we have seen above, the history of EMU was composed of many elements including the political, legal and economic backgrounds. In order to derive lessons effectively, we will analyse the history and preconditions of EMU from three points of view; (1) political backgrounds (Political wills or motivations and supports from national politics), (2) institutionalisation including legalisation, and (3) economic conditions.

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45 Hannover European Council of 27/28 June 1988, EC Bulletin, No 6-1988.

46 Starting from September 1988, the Committee discussed in detail aspects of EMU based on viewpoints of various specialists, and published the final report unanimously on 17 April 1989, Report on economic and monetary union in the European Community, 1989.

47 *Dinan*, (fn. 33), p. 233: "Only a few years earlier most European leaders rode a wave of Europhoria [...] Within a short time, public and political attitudes toward European integration soured."

48 Ibid., p. 298.

49 *Kohl's* successor, *Schröder*, Entscheidungen – Mein Leben in der Politik, 2007, states in his memoirs that the convergence criteria of the Maastricht Treaty were decided in a phase of short economic boom and laid a burden on German economy after German unification (pp. 88-89). In addi-

Before discussing these facts in detail, attention must be paid to the different historical, economic and political backgrounds of Europe and East Asia, and a lot of studies emphasised these points.[50] This paper claims that an easy analogy between Europe and East Asia should be excluded, but if general lessons could be extracted properly, such lessons would be useful for analysing attempts for a monetary union in other areas. Thus, this Chapter tries to seek "general" elements removing "European/time specific" elements.

1. Political backgrounds

When scrutinising the political background while the European countries were on their way to EMU, the political wills of the German and the French leaders to integrate Europe played an important role. It is worth pointing out that the political will to create EMU was a mixture of (1) co-operation and competition between Germany and France ("co-opetition" games), and (2) the philosophy of European integration.

a) Lesson 1: Co-opetition games

(1) A hypothesis of co-opetition games between Germany and France

The relationship between *Pompidou* and *Brandt*, *Giscard* and *Schmidt* and *Mitterrand* and *Kohl* were of decisive importance in making EMU possible. These relationships were not simply based on purely co-operative motivation with the straightforward objective of currency stability, but also on the pursuit of national or domestic interests. To explain these complicated motivations, we will use co-opetition game hypothesis in lesson 1. The term "co-opetition" is used in the field of business strategy and refers to the situation where there are simultaneously co-operation and competition among companies in order to obtain maximum value respectively.[51] As we will see below, the history of EMU contained a lot of "European or time specific" elements which cannot be directly applied to East Asia. For example, the German unification in 1990 was an important motivation for Germany to sacrifice its dominant economic position, especially the German Mark. This is a quite obvious example of the "European/time specific" elements. However, the hypothesis of co-opetition game might give us a useful framework to generalise from "European or time specific" elements, i.e. *Kohl* wanted to complete the German unification and *Mitterrand* wanted to avoid a dominant position

tion, the criterion of the maximum of 3 % deficit per year is inflexible and hindered economic growth during a recession period (p. 436).

50 For example, *Park/Wyplosz*, (fn. 18), pp. 107-111, point out the difference between European and East Asian integration, i.e. the motivation for regional integration and the diversity within the area.

51 There are many studies on co-opetition game in business strategy. *Brandenburger/Nalebuff*, Co-opetition, 1996, typifies these studies.

of the German Mark and the German Bundesbank (competition or domestic interests). Based on these competitive motivations, *Kohl* and *Mitterrand* at the same time co-operated with each other for the creation of EMU (co-operation). In lesson 1, recognising that this framework, of course, does not cover whole political decisions, we will analyse the history of EMU by using the co-opetition game hypothesis.

(2) Co-opetition games in each period

Period 1: In the late 1960s, the common market (the common agricultural policy and the customs union) was already highly developed. By contrast, because of the difference in economic policies among Member States, price and cost divergence among them became bigger and caused exchange rate crises and balance of payment problems. In addition, the capital inflow into the German Mark increased strongly as a result of the weakened US dollar. Thus, the common market was threatened by these endogenous and exogenous elements.[52] In order to cope with this shared problem, *Pompidou* and *Brandt* co-proposed a new initiative for the creation of economic and monetary union.[53]

On the other hand, there were other motivations for this initiative. *Pompidou* was willing to separate his image from his powerful precursor, *de Gaulle*, and he initiated new policies such as the monetary union and the opening for the negotiation with the UK on EC accession.[54] All the more, as a competitive element, *Pompidou* saw EMU as a measure to constrain German economic power.[55] On the other hand, *Brandt* attempted to utilize EMU more politically, i.e. he used it as a measure to release France and other European countries from his primary policy, *Ostpolitik*.[56]

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52 In detail, *Selmayr*, (fn. 22), pp. 134-144; ECB, (fn. 21), p. 17; *Tietmeyer*, (fn. 28), p. 30.

53 In this period, they closely communicated with each other on the subject of monetary union. *Brandt*, Erinnerungen, 1989, p. 457.

54 *Tietmeyer*, (fn. 28), p. 41.

55 *Dyson/Featherstone*, (fn. 39), p. 105: "The imbalance between French and German economic power was seen as a more acute and threatening problem requiring new forms of action to protect vital French interests. [....] French resentment at this use of German economic power at the G10 meeting rekindled domestic interest in EMU as a means to 'bind in' German power and to counter the irresponsible use of US economic power. For Pompidou in 1969 the reality of German economic and monetary power was harsher than it had been for de Gaulle in 1958. De Gaulle did not endorse an EMU initiative. But Gaullists like Pompidou could justify their advocacy of EMU by reference to de Gaulle's principal argument for European unification: that it was a means of escaping from dependency on US power and of containing German power [...] Pompidou shared Barre's and Giscard's view on the lessons of this Franco-German crisis: that France must seek to escape from its international isolation."

56 Ibid., pp. 106, 304: "It [EMU] was a flanking measure for his Ostpolitik rather than a decisive point [...]"; p. 290: "That initiative [= Brandt's initiative on EMU at the Hague summit of

In this way, we can see co-opetition during the negotiations in period 1. However, the outcome of the Werner Report was nothing more than a compromise,[57] or paying lip-service[58] to the political initiative[59] and there was less co-ordination of economic policy[60] and thus, it failed in the mid-1970s.

Period 2: The personal relationship between *Schmidt* and *Giscard* was especially strong. Their friendship stemmed from the 1950s when they were members of the Monnet Action Committee for the United States of Europe.[61] Since tackling the first oil shock in 1973/1974 as Finance Ministers, they shared the idea of the EMS and closely communicated with each other about the strategy for a successful launch of the EMS.[62] Through the financial crisis in the late 1970s, the two European leaders recognized the importance of the independence from the US Dollar[63] and the political will to be independent from US currency policy was behind their motivation to create the EMS.[64] Under the veil of secrecy,[65] *Giscard*

December 1969] had a clear foreign policy rationale: 'flanking' measure to reassure the anxious French and thereby limit potential damage to fast progress with Ostpolitik."

57 *Tietmeyer*, (fn. 28), p. 54: "*Dieser nach hartnäckigen Verhandlungen zustande gekommene Formelkompromiss stellte in der damaligen Lage sicherlich ein Maximum des politisch Erreichbaren dar.*"

58 *Selmayr*, (fn. 22), p. 144.

59 As to the legal characteristics, see Lesson 3.

60 Lesson 6: the need for economic convergence.

61 *Dyson/Featherstone*, (fn. 39), p. 113.

62 For example, *Schmidt*, Die Deutschen und ihre Nachbarn, 1990, p. 248: "*Aus einem Gefühl ökonomischer Zuversicht beschlossen wir im privaten Gespräch, den seit der ersten Ölpreisexplosion 1973/74 vernachlässigten Weg Europas in Richtung auf eine Wirtschafts- und Währungsunion im Rahmen der EG wieder aufzunehmen* [...] *Giscard und Barre waren überzeugt, das EMS zur Verwirklichung ihrer eigenen ökonomischen Politik unbedingt zu benötigen; ich war davon ebenfalls überzeugt. Experten der Finanz- und Agrarministerien, der Zentralbanken, der Geschäftsbanken und der Verbände hatten lange genug Bedenken und Hindernisse erfunden; jetzt hatten wir genug davon. Wir wußten, daß die europäischen Volkswirtschaften nicht in der Lage waren, sich einzeln gegen die Turbulenzen der Welt ausreichend zu wappnen. Deshalb wollten wir den Zusammenschluß und den gemeinsamen Erfolg.*"

63 *Tietmeyer*, (fn. 28), p. 68: "*Allerdings dürfen auch die zeitweilig negativen Erfahrungen mit der Wirtschafts- und Währungspolitik der Carter-Administration in den USA bei seiner Meinungsbildung eine Rolle gespielt haben*." *Dinan*, (fn. 33), p. 173 et seq.

64 *Schmidt*, (fn. 62), p. 249: "*Außerdem hatten sich das rücksichtslose währungspolitische Verhalten der USA sowie die Abhängigkeit der Geld- und Währungspolitik der europäischen Staaten vom Dollar, von den Dollarzinsen und der Dollarspekulation besonders schmerzhaft ausgewirkt*." *Giscard d'Estaing*, Le pouvoir et la vie, 1988, pp. 132-136, explains the background of *Schmidt's* negative attitude towards the US policies describing a series of events as regards the Neutron Bomb plan of the US.

65 *Schmidt*, (fn. 62), p. 254: "*Giscard wählte Bernard Clappier* [...] *Ich* [*Schmidt*] *bestimmte Horst Schulmann* [...] *Dazu hofften wir auf einen persönlichen Vertreter von James Callaghen. Diese drei Leute brauchten Ruhe vor ihren Kollegen und vor der Presse – mindestens bis zur übernächsten Sitzung des Europäischen Rates, die im Sommer 1978 unter meinem Vorsitz fällig war.*"

and *Schmidt* took the initiative of the EMS and co-proposed the idea of the EMS at the European Council in April 1978 in Copenhagen. Thus, these exogenous factors, especially the dependence on the US dollar, were a catalyst for the attempted currency co-operation.

From the viewpoint of competition, *Schmidt* was said to want to protect German export industries from depreciation of the US Dollar[66] and also wanted to tie Germany to Europe.[67] Note that this political will was related not simply to German national interests but also to the philosophy of European integration as we will see in lesson 2. By contrast, the top priority of *Giscard* was to recover French leadership in Europe by aligning the French economy with German standards of performance and by using the framework of the EMS.[68]

Period 3: During the currency crisis in March 1983, France faced the depreciation of the French franc. *Kohl* and other German leaders tried to negotiate with France in order to keep France as a member of the EMS,[69] and also France tried to stay in the EMS.[70] This is in contrast to the situation in the 1970s when France withdrew from the Snake as well as the economies of European countries had diverged by the middle of the 1970s. In such a situation, the conditions for a monetary union could not be realised.

Under such co-operative economic policies during 1980s, *Mitterrand* wanted to deprive Germany and the German Bundesbank of their dominant monetary power, and to obtain French leadership in the field of international monetary reform in order to challenge the power of the US Dollar.[71] During the German unification process in late 1989, Kohl was faced with the "*deutschen Frage*"[72] and was driven into a difficult situation as regards the consensus of other Member

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66 *Dinan*, (fn. 33), p. 173.

67 *Marsh*, The Bundesbank: The bank that rules Europe, 1993, p. 232 et seq.: "The EMS was part of what Schmidt liked to call, in later years, his 'grand strategy for integrating Europe'. In 1987, Schmidt revealed that a vital, though unspoken, reason behind the creation of EMS was his wish to provide an additional 'anchor' for West Germany's ties to Western Europe."

68 *Dyson/Featherstone*, (fn. 39), p. 115 et seq.; *Dinan*, (fn. 33), p. 174: "The advantage to France of linking the weak franc to the strong mark was obvious, especially if Germany would bear the cost of maintaining parity between them". *Schmidt*, (fn. 62), p. 258 et seq., explained this *Giscard's* political motivation not only from French side but also from the perspective of European integration.

69 *Kohl* also tried to keep France within the European Community, while France was almost infringing the EC Treaty by imposing customs duties which might have caused serious consequences including a withdrawal of EC. *Tietmeyer*, (fn. 28), pp. 88 and 312, fn. 28.

70 Ibid., p. 87 et seq.; *Dyson/Featherstone*, (fn. 39), p. 127.

71 Ibid., p. 65; *Marsh*, (fn. 67), pp. 237, 247.

72 *Selmayr*, (fn. 22), p. 182; *Tietmeyer*, (fn. 28), pp. 138-141.

States on German unification.[73] Faced with the objections of other Member States, *Kohl* tried to show that Germany would continue to stay in Europe even after the German unification.[74] *Mitterrand* took advantage of this timing to obtain *Kohl's* agreement to advance EMU by saying "*oui*" to German unification.[75]

In this way, German and French leaders played a co-opetition game also in Period 3, i.e. *Mitterrand* recovered French leadership in European monetary policy and *Kohl* also obtained his primary policy, German unification, at the expense of giving up the dominant position of the German Bundesbank and the German Mark.[76]

(3) Short remarks

As seen above, there had been constant co-opetition games between Germany and France concerning the attempts to create EMU. It should be noted that the Cold War forced them to co-operate even with some competitive elements. Also the co-operation with Germany had been crucially important for France under the geo-political conditions.[77] By contrast, Germany wanted to pursue its policy such as the *Ostpolitik* and the German unification in a modest way, and not to cause any economic and political fears on other Member States, and the Franco-German relationship actually contributed to this aim. Therefore, we conclude that co-opetition games are observed in the history of EMU, and this could become one of the important functional preconditions for regional integration.

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73 *Dyson/Featherstone*, (fn. 39), p. 751 et seq.: "from 1989, the diplomatic rationale of binding enhanced German power into a European framework became decisive for the French, and economic arguments were transformed into the instruments for this purpose."

74 *Kohl*, Erinnerungen 1982-1990, 2005, pp. 1010-1014; *Tietmeyer*, (fn. 28), pp. 138-140.

75 *Attali*, Verbatim III, 1995, p. 330 et seq., commented on the dialogue between *Mitterrand* and *Kohl* at the meeting of 54th Germany-French summit as follows: "*François Mitterrand: Peut-on agir? On peut aider la Pologne. On devra peut-être envoyer des vivres en URSS. La négociation de Vienne va être remise en cause. La marge de manœuvre, pour Gorbatchev, est de plus en plus étroite* [...] *Helmut Kohl: Il faudra une dimension sociale au Sommet de Strasbourg, et avancer sur une union monétaire* [...] *(comment of Attali) Au cours de cet entretien très important, François Mitterrand vient en somme de donner explicitement son feu vert à la réunification*."

76 There exist several interpretations on *Kohl's* original intention towards EMU, i.e. whether *Kohl* had originally aimed at EMU or whether he changed his indifference towards it. *Dyson/Featherstone*, (fn. 39), pp. 259, 368, maintains that *Kohl* strategically waited for the chance to introduce EMU. In contrast, *Schmidt* observes that *Kohl* firstly did not act in favour of EMU even during the Bremen Summit and changed his stance on facing other Member States' objections to German unification. *Schmidt*, (fn. 62), p. 262.

77 When we look closely at the first motivation of the ECSC, *Monnet*, Note 3 mai 1950, already predicted just after the Second World War that German economic production would soon recover and be superior to France's one sooner or later.

b) Lesson 2: Philosophy of regional integration[78] and shared memories

In addition to these co-opetition games, we must pay attention to the function of the philosophy of European integration as a backbone for political leaders. The difference between an ordinary meaning of co-operative international relationships and the philosophy of European integration might be that the philosophy of European integration is rooted in its long history and a steady accumulation of political memories about integration policies. Since the negotiations for EMU meant a long process in which member states lost their sovereignty, there were a lot of examples of political leadership based on individual beliefs, and a part of them were based on the philosophy of European integration.

(1) Shared philosophy of European integration

The philosophy of European integration shared by European leaders stemmed from the memory of numerous wars within Europe, and the ruins left after represented an important background to this philosophy.[79] This shared philosophy restricted political leaders' decisions to a certain degree, and produced mutual anticipation of a political direction among them, namely between Germany and France.

Period 1: According to *Brandt's* memoirs, *Brandt* remembered *Monnet's* tip on the European integration process.[80] When *Pompidou* sent his signal to *Brandt* about The Hague Summit, *Brandt* tried to respond as soon as possible, and this resulted in a common proposal by Germany and France at The Hague meeting in December 1969 which created a political momentum for the monetary union in this period.

Period 2: *Schmidt* and *Giscard* were the members of the Monnet Action Committee in the 1950s, and saw themselves as European statesmen.[81] *Schmidt* regarded the

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78 Although *Dyson/Featherstone*, (fn. 39), p. 748, maintain "EMU remained a matter of inter-elite communications and elite management", the philosophy of European integration and EMU should be supported, of course, by people. *Schlesinger*, former President of the German Bundesbank, told the author that diplomats could negotiate and agree with the monetary union, but what is important is a strong support from the people. (Interview in Frankfurt a.M., 2009).

79 *Dyson/Featherstone*, (fn. 39), p. 21 et seq.

80 *Brandt*, (fn. 53), p. 454: "*Einer, der sich durch keinen Rückschlag entmutigen ließ, sondern - mehr hinter den Kulissen als vom Rednerpult aus - immer wieder Anregungen gab, wie die europäischen Dinge vorangebracht werden könnten, war Jean Monnet*"; p. 455: "*Zu lernen war von ihm nicht nur Inhaltliches, sondern auch Prozedurales: ‚to re-arrange the scene', war einer seiner nicht seltenen Regiehinweise; dieselben Möbel, anders angeordnet, können tatsächlich ein neues Bild ergeben.*"

81 *Schmidt*, (fn. 62), p. 272: "*Wir waren beide atlantisch gesinnt, aber ebenso proeuropäisch, beide marktwirtschaftlich und zugleich antiinflatorisch orientiert*."

EMS as a grand strategy for European integration[82] and *Giscard* set EMU as a top priority in his agenda on European integration.[83] We can also see *Giscard's* pro-European policy in his personnel selection of the President of Banque de France and Finance Minister when he became the French President.[84]

Period 3: In the late 1980s, *Mitterrand* put European integration at the top of his agenda refocusing his mind on "*l'avantage de la durée*", on positioning EMU and other EC initiatives in the long-term context of a historic mission and a legacy of his Presidency.[85] *Kohl* also recognized himself as a "grandson" of *Adenauer*[86] and pursued German unification and European integration simultaniously.

(2) Accumulation of practical memories about European integration

In the history of European integration, there have been various instances of momentum which broke through a deadlock and re-launched the integration process, such as the Single European Act. Accordingly, political leaders in Brussels and each Member State have taken advantage of the practical memories of European integration. Such accumulation of practical memories of European policies was a positive asset for improving the policy-making process in the European context. In particular as regards monetary union, the heads of state or government of the Member States made a ceremonial announcement of the "10-year plan" for the transition to EMU,[87] but had lost momentum for the plan by the mid-1970s. This bitter memory of the Werner Plan had become a lesson for European leaders and resulted in a more realistic approach to the EMS[88] and also resulted in the re-launch of EMU in the late 1980s.[89] For instance, *Delors* at first carefully avoided

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82 *Marsh*, (fn. 67), p. 232 et seq.

83 *Dyson/Featherstone*, (fn. 39), p. 112.

84 Ibid., pp. 112, 115.

85 Ibid., pp. 64, 72, 172.

86 Ibid., pp. 257-260.

87 *Selmayr*, (fn. 22), p. 219.

88 *Dinan*, (fn. 33), p. 173: "Indeed, embarrassing memories of the EC's failure to achieve EMU by 1980 led member states to tone down their rhetoric about the EMS. Far from proclaiming the EMS a step toward EMU, member states saw it for what it was: an effort to reduce exchange rate fluctuations among participating currencies in order to fight inflation, increase investment, and improve economic performance throughout the EC. Only the Commission claimed that the EMS aimed to promote deeper integration, although the relative success of the system, which nobody predicted at the time, undoubtedly contributed to the EC's revival later in the 1980s."

89 The Delors Report, 1989, para. 1 and 2, starts from the history of EMU in the 1960s. *Dyson/Featherstone*, (fn. 39), p. 19 et seq.: "Most influential were memories of the previous failed attempt to realize EMU in the wake of the Werner Report of 1970 [...] The failure to implement the Werner Report had bequeathed, as a general legacy, the view that EMU would be a difficult,

to use the word "EMU" or "monetary union" because of the memories of the Werner Report, while he himself intended to create EMU from the beginning.[90] Also *Delors* remembered the important role of Germany in pursuing the monetary union and tried to gain *Kohl's* interest in his plan.[91] As we have seen above, the philosophy of European integration and shared memories have played a central role in the history of EMU.

2. Institutionalisation

Now we will analyse the institutional setting of EMU. Although this is an essential part of the introduction of EMU,[92] there have been only a few previous studies in relation to the idea of an Asian currency.[93]

a) Lesson 3: The effect of legalisation[94]

The basis of the euro can be legitimated not by an already proven economic necessity, but exclusively by Community law.[95] As we will see below, in the first attempt to create a monetary union in Period 1, the legal basis of the Snake system was not based on European Community law, but on public international law. However, in Period 2, the legal nature of the EMS was a mixture of EC law, international law

uncertain, and protracted task. For German negotiators like Hans Tietmeyer, [...], the lessons were twofold: that establishing the prerequisite of economic convergence for a viable monetary union would be a long-term, very practical affair; and that, until French negotiators were prepared to put in place European political union, EMU would not be able to proceed. Monetary union would be the final 'coronation' of a process of economic and political union."

90 *Dinan*, (fn. 33), p. 207: "Delors was primarily interested in more glamorous and ambitious objectives, such as EMU and defence policy co-operation. Reaction in national capitals convinced him to scale back and push instead for completion of the internal market. Given the presumed link between market integration and monetary union, Delors envisioned the internal market project not as an end in itself but as a means toward the greater goal of EMU."

91 When *Delors* relaunched EMU, he took into account the failure of *Roy Jenkins* to obtain the approval of big member states, especially Germany, France and the UK. Learning from this experience, *Delors* proposed not EMU but the single market plan at first to attract the member states. *Dyson/Featherstone*, (fn. 39), pp. 707 et seq., 742.

92 *Tietmeyer*, (fn. 28), p. 6, concludes that both (1) political decision making and (2) fundamental and functional detailed rules were essential to EMU.

93 About East Asian regionalism from a legal point of view, *Nakamura*, East Asian Regionalism from a Legal Perspective: Current Features and a Vision for the Future, 2009.

94 *Goldstein et al.*, Introduction: Legalization and World Politics, International Organization 54 (2000), p. 386, define the meaning of legalisation as follows: "Legalization, a particular form of institutionalization, represents the decision in different issue-areas to impose international legal constraints on governments."

95 *Selmayr*, (fn. 22), preface ix.

and political agreement.[96] In the end, in Period 3, three steps towards completion of EMU and other relevant conditions were clearly provided in the EC Treaty, the primary Community law.

Behind the development of the legal bases of Community law from Period 1 to Period 3, we should note the fact that Member States gradually changed their attitude towards sovereignty, i.e. the integration of a policy from the national level to the supranational level causes the loss of sovereignty, and during the history of EMU, the hesitation to transfer the competence to the Community level imposed costs on Member States, and Member States accepted this transfer of monetary sovereignty in the Maastricht Treaty.[97]

A full study of EC law in the history of EMU is beyond the scope of this paper. However, legal analyses of (1) the Community legal system as a supranational legal system, (2) a comparison between Period 1 and Period 3, are critical to the understanding of the interaction between political decisions and institutional settings.

(1) Supranational characteristic of Community law

The special characteristic of Community law had a large impact on the realisation of EMU. Since the introduction of the EEC Treaty in 1958, the EEC had developed its own legal system mainly through the interpretation of the EEC Treaty by the ECJ. The main principles such as supremacy of Community law over national law,[98] direct effect of Community law,[99] exclusive[100] and obligatory[101] jurisdiction of the ECJ developed in the 1960s.

96 Ibid., p. 167.

97 Ibid., p. 81; *Park/Wyplosz*, (fn. 18), p. 108.

98 This principle of Community law was at first declared in ECJ, case 26/62, *Van Gend en Loos*, ECR 1963, 1, that "the Community constitutes a new legal order of international law for the benefit of which the states have limited their sovereign rights, albeit within limited fields, and the subjects of which comprise not only Member States but also their nationals." Two years later, in ECJ, case 6/64, *Costa/ENEL*, ECR 1964, 585, the ECJ omitted the word "international" and declared that "By contrast with ordinary international treaties, the EEC Treaty has created its own legal system which, on the entry into force of the Treaty, became an integral part of the legal systems of the Member States and which their courts are bound to apply".

99 ECJ, case 106/77, *Simmenthal*, ECR 1978, 629.

100 On this point, *Selmayr*, (fn. 22), p. 101 et seq. Art. 344 TFEU: "Member States undertake not to submit a dispute concerning the interpretation or application of the Treaties to any method of settlement other than those provided for therein". Art. 274 TFEU: "Save where jurisdiction is conferred on the Court of Justice of the European Union by the Treaties, disputes to which the Union is a party shall not on that ground be excluded from the jurisdiction of the courts or tribunals of the Member States". Art. 267 TFEU (Preliminary Rulings).

101 Member States must comply with the obligations under the Treaties (Art. 260 TFEU).

This development of the Community legal system contributed to the effective implementation of a rule-based currency policy supported by its rigid framework, and with these characteristics, political decisions were institutionalised as an effective rule.

(2) Comparison of the legal basis between Period 1 and Period 3

Period 1: In order to attain the aim of an economic and monetary union shown in the Werner Report, the Resolution of 21 March 1972[102] set out to create an economic and monetary union by requesting the Central Banks of the Member States to intervene in the market to keep the spot exchange rates of two Member States within the band of 2.25 %.

However, this request had no legal basis in EC law. The legal nature of this Resolution was to be classified as an "atypical Council Decision".[103] As such it could not be legally challenged by any Community institution before the ECJ with an action for annulment under the then Art. 173 TEC, because such "atypical Council Decisions" were not based on Community law, but on public international law.[104] Therefore this Resolution was an act of the Member States and did not provoke any legal consequences under the Community legal system.[105] Also, the communiqué of the European Council declared a time schedule for the completion of EMU by 31 December 1980.[106] However, this time schedule was not legally binding and was never completed.

102 The Resolution on the application of the Resolution on the attainment by stages of economic and monetary union in the Community of 21 March 1972, OJ C 38 of 18/4/1972, p. 3.

103 *Selmayr*, (fn. 22), pp. 146-148.

104 ECJ, joined cases C-181/91 and C-248/91, *European Parliament/Commission*, ECR 1993, I-3685: "Whilst an action for annulment is available in the case of all measures adopted by the Community institutions, whatever their nature, form or wording, which are intended to have legal effects, acts adopted by representatives of the Member States acting not in their capacity as members of the Council but as representatives of their governments, and thus collectively exercising the powers of the Member States, are not subject to judicial review by the Court."

105 *Selmayr*, (fn. 22), p. 148.

106 Final communiqué of the Conference of the Heads of State or Government of the Member States and future Members of the European Communities on 19, 20 and 21 October 1972 in Paris, EC Bulletin No 10 1972. In this communiqué, "The Heads of State and Government reaffirm the resolve of the Member States of the enlarged Community to move irrevocably the Economic and Monetary Union, by confirming all the details of the Acts passed by the Council and by the Member States representatives on 22 March 1971 and 21 March 1972. The required decisions will have to be taken during 1973 to allow transition to the second stage of the Economic and Monetary Union on 1 January 1974 and in view of its complete realization by 31 December 1980 at the latest".

Period 3: By contrast to Period 1, the steps to EMU to be taken in Period 3 were legally binding. Also a lot of time limits were set out in the Maastricht Treaty. This legal characteristic resulted in the completion of EMU on schedule in 1999. It is true that there were huge efforts on the part of political leaders for the completion of EMU during this period. But, when we examine one of the reasons for these political efforts, the legally binding rules of the primary law forced the economic policies of Member States to keep to the convergence criteria in the EC Treaty.[107]

Table 1: Difference between Period 1 and Period 3

	Period 1 (Werner Plan)	Period 3 (Maastricht Treaty)
Legal nature	"atypical Council Decision"	Primary law with time limits
Economic policy	Different (distortion among Member States)	Similar direction (sound monetary and fiscal policy, central bank independence)
Results	Lost the momentum by mid-1970s	Introduction of the euro in 1999

Also a distinctive example of the effect of legally binding rules can be observed in the change of the German Chancellors in October 1998. Whereas *Kohl* served for 16 years as German Chancellor and contributed to the introduction of the Maastricht Treaty, *Kohl's* successor, *Schröder* was critical of the convergence criteria set out in the Maastricht Treaty. In his memoir, he observes that the convergence criteria provided in the Maastricht Treaty were decided in the phase of strong economic growth at the end of the 1980s and laid a burden on the German economy after the German unification.[108] Also he claimed that the excessive deficit procedure of 3 % of GDP[109] would be inflexible and hinder economic growth in a recession.[110] However, the legally binding rules were already set out in the EC Treaty and the change of German Government had an insignificant impact on the road to EMU. In this way, the existence of legally binding rules set out in primary Community law had a strong effect on the policy makers' discretion.

107 Art. 121 ECT and the Protocol on the convergence criteria referred to in Art. 121 ECT.

108 *Schröder*, (fn. 49), p. 88 et seq.

109 Art. 126(2) TFEU and the TFEU Protocol on the excessive deficit procedure. (ex-Art. 104(2)a TEC and ex-EC Treaty Protocol on the excessive deficit procedure).

110 *Schröder*, (fn. 49), p. 436.

Also the timetable set out in the EC Treaty by the Maastricht Treaty had a strong effect as a guideline to EMU. Although there were many other provisions, the three stages towards EMU and its main obligations were provided as follows:

The First Stage of EMU, 1 July 1990 (Resolution of the European Council of 26/27 June 1989)

- Free movement of capital and payments by the start of Stage 1

The Second Stage of EMU, 1 January 1994 (Art. 116(1) TEC):

- Establishment of a temporary institution, the European Monetary Institute (EMI)[111]
- Prohibition of all restrictions on the movement of capital between Member States[112]
- "No monetary financing" by the ECB or the national Central Banks[113]
- "No privileged access" to financial institutions[114]
- The "No-bailout" clause[115]
- Fiscal provisions to avoid excessive government deficits[116]

By 31 December 1996 (Art. 121(3) TEC):

- The Council decides whether a majority of the Member States fulfils the conditions for a single currency, whether the Community may enter the Third Stage and the date for the beginning of the Third Stage.

The Third Stage of EMU, 1 January 1999 (Art. 121(4) TEC):

- Complete application of the Excessive Deficit Procedure with sanctions[117]
- Entrusting of the single monetary policy to the ESCB[118] governed by the ECB[119]

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111 Art. 117(1), second subparagraph, (first sentence) TEC, Art. 4.2, first sentence, EMI Statute.

112 Art. 56 TEC (now Art. 63 TFEU).

113 Art. 101 TEC (now Art. 123 TFEU).

114 Art. 102(1) TEC (now Art. 124 TFEU).

115 Art. 103(1) TEC (now Art. 125(1) TFEU).

116 Art. 104(2)-(8), (10), (12), (13) TEC. (now Art. 126(2)-(8), (10), (12), (13) TFEU).

117 Art. 104(1), (9), (11) TEC (now Art. 126(1), (9), (11) TFEU).

118 European System of Central Banks.

119 Art. 105 TEC (now Art. 127 TFEU).

- Exclusive right of the ECB to issue banknotes within the Community[120]
- Independence of the ECB and national Central Banks[121]

This timetable with many obligations provided by primary Community law and Community institutions functioned as "*ein enges Terminkorsett*"[122] (a tight deadline corset) to bind political decisions of Member States and, as a result, contributed to winning the confidence of the markets. This was totally different from the timetable in Period 1 in which no such detailed legally binding timetable was introduced.

Note that the Delors Report did not show concrete dates for the three steps, although the three steps in the Delors Report became the prototype of the three steps to EMU. One of the reasons for it was quite strategic. Most of the negotiators of the Delors Committee had bitter memories of the results of the Werner Report and thus denied the setting of a timetable for EMU in advance.[123] This suggests that a careful use of the timetable in Period 3 could have contributed to the effective introduction of each stage set out in the Maastricht Treaty.

b) Lesson 4: The role of supranational institutions

Not only Community law, but also the Community institutions, especially the European Council, the Commission and the President of the Commission such as *Monet*, *Hallstein*, *Jenkins* and *Delors*, functioned as a driving force for European integration.

Delors served as a typical example for a contributor, as a President of the Commission.[124] He originally intended to achieve the completion of EMU before the start of his presidency and saw the SEA as a means towards EMU,[125] but he

120 Art. 106 TEC (now Art. 128 TFEU).

121 Art. 108 TEC (now Art. 129 TFEU).

122 *Selmayr*, (fn. 22), p. 266.

123 Ibid., p. 219. The Delors report, para. 43, says "The conditions for moving from stage to stage cannot be defined precisely in advance; nor is it possible to foresee today when these conditions will be realized. The setting of explicit deadlines is therefore not advisable."

124 *Delors* was fairly independent from the political influence of the Elysee. See *Dyson/Featherstone*, (fn. 39), p. 696: "Delors saw his role as to clarify to French policymakers what the conditions were for realizing EMU from an EC perspective. He was no longer mere agent of the French government"; p. 722: "On German reunification Delors did not see eye to eye with Mitterrand. Delors was quick to endorse German reunification in November 1989 and later made it clear that he would do all in his power to ease and speed the assimilation of the five new Bundesländer into the EC."

125 *Dinan*, (fn. 33), p. 207.

waited for the chance to start the discussion, bearing in mind the German Bundesbank's hesitation to be involved in the idea of EMU. After the Genscher memorandum,[126] *Delors* then began to talk about EMU more openly, using his position as chair of the "Delors Committee".

However, the role of *Jenkins* is more meaningful than that of *Delors*, when we pay attention to the function of supranational institutions, as he had tried to initiate a currency union, despite being from the UK which had been sceptical about the idea of a monetary union.[127] At this point, we can see a characteristic of European institutions in the sense that, although persons were originally sent by their mother countries, these persons would not necessarily act as simply an agency of their home countries, but as independent players who pursue the interests of Europe. This is partly because of their desire of political renown as a pro-European.

3. Economic backgrounds

Although a detailed economic analysis on EMU is not the purpose of this paper, we shall briefly examine some key points considering the importance of the economic background to EMU.

a) Lesson 5: The development of the Common Market as a "Sachzwang"[128]

The development of the Common Market forced political leaders to promote broader and deeper integration such as economic and monetary union. The Customs Union was completed on 1 July 1968 and the Common Agriculture Policy (CAP) was almost completed by the late 1960s, although the calculation unit of these common policies was based on the US dollar. As the Bretton Woods

126 26 February 1988; *Krägenau/Wetter*, Europäische Wirtschafts- und Währungsunion, 1993, pp. 309-312 (Dok. 50).

127 While *Schmidt*, (fn. 62), p. 249, remembered that the initiative for the EMS came from both him and *Giscard*, *Jenkins* also contributed to the idea of the EMS. *Dinan*, (fn. 33), p. 173: "The birth of the EMS is generally associated with Giscard and Schmidt, but Commission president Roy Jenkins conceived the idea." *Jenkins* had already started to propose a re-launch of the EMU in 1977, COM (77) 620 final, and tried to interest both *Schmidt* (*Dinan*, (fn. 33), p. 173; *Dyson/Featherstone*, (fn. 39), p. 707 et seq.) and *Giscard* (*Jenkins*, A letter from Jenkins to French President Giscard before the European Council in Copenhagen on 7/8 April 1978, http://ec.europa.eu/economy_finance/emu_history/documentation/documentation_chapter10.htm (1/9/2011)). Although it is difficult to determine who really contributed the proposal of EMS, it could be at least said that *Jenkins* played a key role in the realisation of the EMS in the Period 2.

128 *Hallstein* had already pointed out the spillover effects of the Customs union as a "Sachzwang" (factual constraint) in the early 1950s saying that the development of the Common Market would require more integration. *Tietmeyer*, (fn. 28), pp. 23, 37.

System gradually collapsed due to the US's immense debt caused by the Vietnam War, speculative money flowed into the German Mark as well as into the Japanese yen. The appreciation of the German Mark caused the depreciation of the French franc which was subject to an expansive economic policy. This asymmetry of the European currencies caused tension among the currencies of the Member States, and thus undermined the calculation basis of the CAP and customs duties.[129]

In addition, worldwide deregulation of capital markets had promoted global capital movements from beginning of the 1970s, and also in 1985 the SEA outlined the free movement of capital within the Community as one of its goals.[130] At this point, the "impossible trinity" theory suggests that a fixed exchange rate, highly mobile capital and independent monetary policy cannot be attained simultaneously.[131] Thus, the free movement of capital within the Community could also work as a "*Sachzwang*", and political leaders were compelled to take measures to respond to these "*Sachzwänge*".

b) Lesson 6: Economic convergence with coordinated economic and monetary policies

Economic convergence is an important factor in forming a currency area.[132] At this point, the year 1983 was a turning point[133] when *Mitterrand* and *Delors* abandoned

129 *Selmayr*, (fn. 22), pp. 134-144; ECB, (fn. 21), p. 17.

130 Art. 8A of new TEEC amended by Art. 13 SEA.

131 *Romer*, Advanced Macroeconomics, 3rd ed. 2006, p. 241.

132 As to the application of the theory of Optimum Currency Area (OCA) to the real economy, we shall discuss this later in Chapter D. There were discussions on the procedure of introduction of monetary union for a long time during the history of EMU. During the negotiations after the Werner report in 1970s, member states discussed how to realise the EMU from two blocs; "economist" and "monetarist". The "economist" states such as Germany and the Netherlands maintained that currency union comes only after high convergence of economies. On the side of "economists", there was a historically established idea, so-called "coronel theory" ("*Krönungstheorie*") in which a single currency comes only after the completion of a political union. This reflects the history of German monetary unification in the 19th century. By contrast, the "monetarist" states such as France and Italy claimed that monetary integration comes in advance and the irreversible fixing of exchange rates forces the necessary economic convergence. In the end, the Maastricht Treaty reflected mainly "economist" approach in the sense that the candidates for a single currency should fulfil Convergence criteria. *Issing*, The Euro: Does a Currency Need a State?, International Finance 11 (2008), pp. 302-304.

133 *Tietmeyer*, (fn. 28), p. 82 et seq., states the exchange market situation after the introduction of the EMS: "*Es fehlte damals ganz offenbar noch eine hinreichend gemeinsame wirtschaftspolitische Grundorientierung für ein längerfristig stabiles Fixkurssystem in Europa.* [...] *Dauerhafte Stabilität zwischen den EWS-Währungen konnte letztlich nur durch eine stärkere Angleichung der nationalen Politikorientierungen auf der Grundlage interner Stabilität erreicht werden. Für einen längerfristigen Erfolg des EWS waren genau hier entsprechende Weichenstellungen in den entscheidenden Ländern unausweichlich.*"

expansive economic policies and adopted neoliberal economic policies such as price stability, sound budgetary and monetary policy and central bank independence as necessary conditions for stable economic growth.[134] Also, it should be noted that the Community had been making the effort to pursue economic convergence from its beginning by way of a customs union, competition policy and other Community policies.

However, the Maastricht Treaty left a structural asymmetry in the economic and monetary union.[135] Monetary policy is exclusively within the competence of the ESCB and the ECB, i.e. at a supranational level, while economic and fiscal policies are mainly in the hands of each Member State.[136] This structural asymmetry of economic and monetary policy has become especially visible during the sovereign debt crises of a number of euro area Member States. These were triggered by the global financial crisis which in turn was caused by the subprime mortgage crisis in 2007 and the insolvency of Lehman Brothers in 2008.

To respond swiftly to the sovereign debt crisis, (1) all euro area Member States (except Slovakia) and the IMF helped Greece with guarantees respectively of 80 billion euro and 30 billion euro, a total of 110 billion euro, (2) a wide safety net composed of the European Financial Stabilisation Mechanism (EFSM), the European Financial Stability Facility (EFSF) and the IMF was established to provide financial assistance to a Member State which is experiencing severe economic and financial difficulties beyond its control.

Table 2: Financial assistance framework in the EU[137]

Financial Assistance by	Amounts (billion euro)	Overall Amounts (billion euro)
European Financial Stabilisation Mechanism (EFSM)[138] * Financed by EU budget	60	750
European Financial Stability Facility (EFSF)[139] * Financed by euro area Member States	440	
IMF[140]	250	

134 *Dyson/Featherstone*, (fn. 39), p. 791.

135 *Selmayr*, (fn. 22), p. 221: "*Der Vertrag von Maastricht hat keine dieser beiden Lehren in Reinform implementiert. Bei der Terminfrage setzten sich jedoch am Ende die Monetaristen durch.*" *Seidel*, Konstitutionelle Schwächen der Währungsunion, EuR 2000, pp. 860-878.

136 *Streinz*, Europarecht, 6th ed. 2003, para. 849. On this point, *Issing*, (fn. 132), pp. 297-319.

137 Source: *Ito*, NLI Research Institute Report, October 2010.

In addition to this crisis management framework, the EU adopted a new architecture for EU economic governance called European Semester to coordinate the economic and fiscal policies of Member States by means of the Annual Growth Survey and other measures.[141]

Thus, the European endeavours seen above show us the factors essential to forming a stable and sustainable monetary union in the long term, i.e. the need for a common mechanism for financial crisis management[142] and also better coordinated economic and fiscal policies within the monetary union.

c) Lesson 7: The existence of the anchor currency

The existence of the anchor currency functioned as a barometer for the currencies of other Member States, and contributed to the stable exchange rates within the Community together with Lesson 6. Under the ERM in the Period 2, the German Mark, the only "hard currency" in the same framework, became the anchor currency[143] because of the Bundesbank's disinflationary monetary policy and Germany's economic power. Other participating states in the ERM followed the

138 Art. 122(2) TFEU; Council Regulation (EU) No. 407/2010 of 11 May 2010 establishing a European financial stabilisation mechanism. Note that this mechanism essentially reproduces for all EU Member States the basic mechanism of the existing Balance of Payment Regulation for non-euro area Member States.

139 EFSF, http://www.efsf.europa.eu/attachment/faq_en.pdf (1/9/2011): "The European Financial Stability Facility (EFSF) is a company which was agreed by the 16 countries that share the euro on May 9th 2010 and incorporated in Luxembourg under Luxembourgish law on June 7th 2010. The EFSF's objective is to preserve financial stability of Europe's monetary union by providing temporary financial assistance to euro area Member States in difficulty. In order to reach its objective the EFSF can with the support of the German Debt Management Office (DMO) issue bonds or other debt instruments on the market to raise the funds needed to provide loans to countries in financial difficulties. Issues would be backed by guarantees given by euro area Member States of up to € 440 billion on a pro rata basis, in accordance with their share in the paid-up capital of the European Central Bank (ECB)."

140 Council Conclusions of the Economic and Financial affairs Council Extraordinary meeting, Brussels, 9/10 May 2010, http://www.consilium.europa.eu/uedocs/cmsUpload/Conclusions_Extraordinary_meeting_May2010-EN.pdf (1/9/2011): "The IMF will participate in financing arrangements and is expected to provide at least half as much as the EU contribution through its usual facilities in line with the recent European programmes."

141 MEMO/11/14: "The European semester means the EU and the euro zone will coordinate ex ante their budgetary and economic policies, in line with both the Stability and Growth Pact and the Europe 2020 strategy."

142 For crisis management in the field of a financial supervision framework in the EU, see the high-level group of financial supervision in the EU, so called "De Larosière report" of 25 February 2009.

143 *Dyson/Featherstone*, (fn. 39), p. 25.

monetary policy of the Bundesbank and adopted a disinflationary policy in order to obtain the credibility and reputation of the German Mark.[144] Economically speaking,[145] to follow the monetary policy of the German Bund was said to have a positive result for the other Member States, because they could gain the credibility of the "hard currency"[146] based on sound economic and monetary policy. Therefore, the existence of the anchor currency was, together with economic convergence, an important precondition to EMU.

III. Conclusion

As we have seen in this chapter, we discussed 7 lessons to be learnt from the history of EMU as regards political, institutional and economic backgrounds. As a conclusion, we again emphasise the difference between Period 1 where the attempt to EMU failed and Period 3 where it succeeded. Unlike in Period 1, Community law functioned as a corset to legally bind political decisions (Lesson 3), and also Community institutions, especially the President of the Commission (*Delors*), was an important driving force for EMU and played a decisive role in Period 3 (Lesson 4). These are useful lessons for when we examine the East Asian situation in Chapter D.

D. European lessons for an Asian currency

In Chapter C, we examined 7 lessons based on the history of EMU that could be taken as a series of conditions, or as a barometer for the idea of an Asian currency. Based on the starting point that the idea of an Asian currency might be a long term project, we will now try to apply the European lessons to the East Asian situation.

I. East Asian regionalism: De facto economic integration in East Asia

As referred to briefly in Chapter B., we have seen a constant development of intra-regional trade within East Asia due to globalisation in the 25 years since mid-1980s.[147]

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144 Ibid., p. 25 et seq.

145 Politically, such a dominant position of Bundesbank and German Mark was no longer acceptable to other Member States, and this led to the co-opetition game on the French side in Period 3, as we have seen in Lesson 1.

146 *Selmayr*, (fn. 22), p. 173, fn. 666.

The intra-regional trade ratio of East Asia in 2004 was 55.5 % which is close to that of the 25 EU countries in 1985 (59.8 %), whereas the ratio of East Asia in 1985 (37.1 %) was less than two-thirds of that of the EU countries at that time.[148] When we look at the change in the intra-regional trade ratio from 1985 to 2004, the increase of intra-regional trade ratio in East Asia (18.1 %) is much higher than of intra-regional trade ratio in NAFTA (7.7 %), though the intra-regional trade ratio of NAFTA in 1984 (38.7 %) was at a similar level to East Asia's (37.1 %). This shows a distinctive feature of the East Asian economic integration process in the last two decades.

As to this feature, *Sakakibara* calls it a "market-driven regional integration" in which *de facto* economic integration has been driven by trade and FDI with production networks of multinational companies rather than by governments and regional institutions.[149]

In addition to the phenomenon of *de facto* integration, East Asian countries, especially ASEAN+3 countries, have promoted regional co-operation policies since the Asian financial crisis in 1997/1998. There are three main features of this movement.

1) Monetary regionalism[150]: After the failure of the plan for an Asian Monetary Fund,[151] the ASEAN+3 countries promoted East Asian financial corporation. To achieve this aim, they established bilateral currency swap agreements, the so-called Chiang Mai Initiative[152] as a countermeasure to future financial crises. They also established the Asia Bond Market Initiative[153] to promote the usage of their local currencies by promoting bond issues in local currencies.

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147 Other than the progress of globalisation which could be observed in other geographic areas, the specific reasons for this movement in the East Asian area are (1) relocation of Japanese manufacturers to abroad after the Plaza Accord in 1985, (2) strong concern of (South) East Asian countries about U.S. trade policy (unilateralism and protectionism) which was based on the US trying to open other markets by threatening to close its market. See *Munakata*, (fn. 1), p. 170 et seq.

148 *Kawai*, Challenges of Asian Economic Integration after the East Asia Summit (Japanese title: Higashi ajia samitto go no ajia keizaitougou no kadai), Kokusai-kinyu No. 1163, 2006, quoted by *Murase*, (fn. 6), p. 216.

149 *Sakakibara/Yamakawa*, (fn. 14), pp. 37, 43.

150 See Chapter B.

151 As to the detailed study on the proposal of the AMF, see *Lee*, Japan and the Asian Monetary Fund: An Identity-Intention Approach, International Studies Quarterly 50 (2000), pp. 339-366.

152 Originally, the Chiang Mai Initiative aimed to create a network of bilateral swap arrangements (BSA) among ASEAN+3 countries to address short-term liquidity difficulties in the region and to supplement the existing international financial arrangements. From March 2010, the CMI was strengthened and became a multilateral agreement. Ministry of Finance Japan, http://www.mof.go.jp/english/if/100324press_release.pdf (1/9/2011).

153 Ministry of Finance Japan, http://www.mof.go.jp/english/if/regional_financial_co-operation.htm#ABMI (1/9/2011): "The Asian Bond Markets Initiative aims to develop efficient and

2) A race for FTAs[154]: The FTA networks have developed in this area after 2000. As of 2008, 19 FTAs projects had been initiated within East Asia (with 15 concluded) and 86 in the Asia-Pacific area (with 60 concluded),[155] whereas the number of FTAs in Asia-Pacific region in 1998 was only 8.[156]

3) Political Dialogues and administrative level Co-operation: Since 2000, there has been much political dialogue and building up of administrative co-operation frameworks in East Asia. These include the ASEAN+3 Summit, the East Asia Summit, the Trilateral co-operation including the leadership level, ministerial level and daily administrative level.[157]

Considering these circumstances, we will now examine the idea of an Asian currency and its conditions by using the European lessons described in Chapter C.

II. Application of European lessons

Before turning to applying European lessons to East Asia, it must be noted that we should generalise European lessons, because the political situations, institutional settings, economic situations and cultural backgrounds in Europe and East Asia are different from each other.[158]

1. Political backgrounds (Lesson 1 and 2)

When we discuss a monetary union, it is important to examine geo-political backgrounds, because a monetary union is the most advanced type of regional integration and thus it contains inevitably geo-political elements. In East Asia, the geo-political situation has dramatically changed since the 1990s such as China's rise

liquid bond markets in Asia, enabling better utilization of Asian savings for Asian investments. Activities of the ABMI focus on the following two areas: (1) facilitating access to the market through a wider variety of issuers and types of bonds, and (2) enhancing market infrastructure to foster bond markets in Asia."

154 *Munakata*, (fn. 1), pp. 133-168, overviews this "race" for the FTAs in East Asian area from the strategies of Japan, the US and China.

155 *Dent*, Free Trade agreements in the Asia-Pacific a decade on: evaluating the past, looking to the future, International Relations of the Asia-Pacific 2010. p. 11.

156 Ibid., p. 2.

157 Japan-China-ROK Trilateral Summit, Joint Statement for Tripartite Partnership, http://www.mofa.go.jp/region/asia-paci/future/speech0905.html (1/9/2011).

158 *Kim*, Regionalization in Europe and East Asia: Divergent Path or Distinct Finalities?, Regional Integration in Europe and Asia 2009, p. 68, also emphasises on this point: "I acknowledge that the European model of regional integration cannot be applied to Asia in an unmodified or mechanical fashion."

and Japan's slowdown. Under these circumstances, many studies have observed a move that each player pursues its interests by seeking for their most favourable regional frameworks. For instance, *Munakata* assumes the possible shape of the future East Asian regionalism as being determined by the interaction of Japan, the US and China, while the regional policies of the three countries are partly under the influence of the ASEAN and South Korea in the sense that they sometimes make groundbreaking proposals but mainly act as a mediator.[159] Also *Dent* claims that the recent FTA-active tendency is realised by the most dominant trade powers, China, Japan and the US.[160] On the other hand, these players share economic interests interdependently. Considering these facts, they could play co-opetition games in this area, too.

We must notice that these co-opetition games would be played under the regional framework of ASEAN+3, ASEAN+6 and APEC,[161] and the games under these frameworks would represent a distinctive feature of the East Asian regionalism in the twenty-first century.

Table 3: Top three trade partners of Japan, China and South Korea[162]

	Japan (2009)		China (2008)		South Korea (2008)	
	Export	Import	Export	Import	Export	Import
1	China (19 %)	China (22 %)	US (18 %)	Japan (13 %)	China (22 %)	China (18 %)
2	US (16 %)	US (11 %)	Hongkong (13.4 %)	Korea (10 %)	US (11%)	Japan (14 %)
3	Korea (8 %)	Australia (6 %)	Japan (8 %)	Taiwan (9 %)	Japan (7 %)	US (9 %)

In addition to these co-opetition games, one of the most important preconditions for monetary union might be a shared philosophy of regional integration which flows through generations of political leaders (Lesson 2). Monetary union is a long

159 *Munakata*, (fn. 1), p. 22.

160 *Dent*, (fn. 155), p. 31.

161 APEC formulates a code of FTA "Best practice" to harmonize FTAs in this region. Ibid., p. 33.

162 The date is on the website of the Japan External Trade Organization (JETRO), http://www.jetro.go.jp/world/asia/ (1/9/2011).

process in which nations are to loose their sovereign rights, and such a long process needs a consistent philosophy which promotes the project even during difficult domestic political situations. Also personal trust among political leaders has been the precondition of co-opetition games in the history of EMU (Lesson 1). Whatever motivations bring it to light, a strong philosophy of regional integration and leaders' mutual trust might be crucial and the core for the idea of an Asian currency.

2. Institutional backgrounds (Lesson 3 and 4)

Political backgrounds are not presenting a sufficient condition for a long-term regional project like an Asian currency. As we have seen in Lesson 3 and 4, legalisation and regional institutions played an important role to the institutionalisation of political commitments. A monetary union would be fragile if it could not be based on sufficient institutional commitments which becomes clear when we consider the differences of the legal basis between Period 1 and Period 3 in the history of EMU (Lesson 3). Though there exists no corresponding supranational legal system in the East Asian area, legalisation will be necessary to establish a realisable monetary union. We should notice that the establishment of a supranational legal system itself does not directly contribute to the regional integration. For instance, the Andean Community of Nations in South America has an EU type supranational legal system with a Court of Justice.[163] However, the level of regional integration in the Community remains at a lower level,[164] because of the lack of political will or consensus to keep up the Community.[165] This shows that the effective legal system should be abreast with a consistent political will to support regional integration.

As regards institutional settings (Lesson 4), we can observe a change in the concept of the institutionalisation in the East Asian regionalism. For a long time, the decision making system in ASEAN countries was conceptualised as the so-called

163 A study on the effect of the legal order on the regional integration in Andean Community, *Saldías*, Supranational courts as engines of disintegration, The case of the Andean Community, Berlin Working Paper on European Integration No. 5/2007.

164 The intra-regional trade ratio is law level: 10.2 % in 2006 (4.1 % in 1990). *Baumann*, Integration in Latin America – Trends and Challenges, 2008, p. 2.

165 The Andean Community could not coordinate national interests within the member countries during the negotiation of FTA with the USA, and Venezuela had withdrawn from it in April 2006. In 2006, Venezuela had withdrawn from the Andean Community, because it objected to the negotiation policy of other member states during the FTA negotiation with the US. Note that the Andean Community is already 3 years from its beginning, but could not bear the burden of FTA negotiation which is listed in lower level regional integration according to *Balassa's* theory (See Chapter B). This showed the importance of political will to formulate a well-knit regional integration.

"ASEAN Way" which emphasises informal networking with consensus in decision making and non-interference in the domestic affairs of its members.[166] Although there are many studies which claim that this tendency still prevails in ASEAN countries today,[167] it has been changed over time and institutionalisation in this area has been advanced, especially after the Asian financial crisis when ASEAN countries faced serious regional currency and economic crises, and they recognised the need for institutionalisation through these crises.[168]

As to the institutional setting of financial co-operation, the CMIM is an institutional approach to the financial crisis under the framework of the ASEAN+3. ASEAN+3 countries are now preparing the establishment of an independent regional surveillance unit of the CMIM.[169]

As a whole, institutionalisation in East Asian regionalism is now at the starting point with some outcomes. So far, these attempts are intergovernmental co-operation from legislative, executive and judicial aspects. A higher level of legalisation such as transference of sovereignty to supranational institutions might be a necessary condition for deeper regional co-operation. This requires, needless to say, a strong and consistent political will of each country for regional integration. Another indispensable condition for economic and monetary union is that an Asian currency would have to be independent from the individual interests of participating countries in order to win the confidence of the markets.

3. Economic conditions (Lesson 5, 6 and 7)

Economic conditions are determinant factors to be considered whenever we think of a monetary union.

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166 *Kahler*, Legalization as Strategy: The Asia-Pacific Case, International Organisation 54 (2000), p. 552.

167 *Ravenhill*, East Asian regionalism: Much Ado about Nothing?, Review of International Studies 35 (2009), p. 235.

168 *Munakata*, (fn. 1), p. 35 et seq. "ASEAN Charter" is one of the most remarkable developments of ASEAN as a regional community from an institutional and legal point of view. In 2007 ASEAN adopted the ASEAN Charter which aims at a rule-based approach among ASEAN countries, i.e. it provides for the legal personality of ASEAN (Charter Art. 3), the basic principles and rules of conduct shared among its member states in operating the ASEAN institution (Charter Art. 2), its institutional framework (Charter Art. 7-15), and basic decision-making and decision implementing rules (Charter Art. 20-21). See *Nakamura*, (fn. 93), p. 198 et seq. While the recent development in financial regionalism in East Asia has been mainly led by the framework of ASEAN+3, the institutional development of ASEAN itself is a noticeable subject in the East Asian regionalism, and a further study of it should be conducted.

169 Ministry of Finance Japan, http://www.mof.go.jp/english/if/100324press_release.pdf (1/9/2011).

How can we learn from Lesson 5 (the development of the Common Market as a "*Sachzwang*")? Although there is no corresponding common policy such as the CAP and the Customs union, the development of a regional market in East Asia could potentially require a certain level of currency policy co-operation as a "*Sachzwang*" in the future.

As to Lesson 6 (economic convergence with coordinated economic and monetary policies within East Asia), there are numerous arguments about whether East Asia is an Optimum Currency Area, which analyse the underlying shocks across, the degree of openness, labour mobility, and financial market integration among the countries in the area.[170] We should also notice that economic convergence has been playing, regardless of the applicability of OCA theory in Europe,[171] a quite important role for the creation of EMU, when we review the distinctive turning point of the French economic policies in 1983 and also the shift from the keynesian economics to neoliberalism.

As to the existence of the anchor currency (Lesson 7), we should note that the important difference between Europe and Asia is that the European anchor currency was the German Mark (endogenous factor), whereas the main currency used within East Asian trade is the US dollar (exogenous factor).[172] Most of the East Asian currencies were *de jure* or *de facto* US dollar pegged before the crisis and, some studies show that some countries have returned to the US dollar-pegged system also after the crisis.[173] As a recent regional policy, the Asian Bond Markets

170 *Park/Wyplosz*, (fn. 18). The Bank of Japan, (fn. 7), summarised 14 economic researches and concludes that some of East Asian countries are seen as an OCA.

171 On this point, there is an economic argument about the endogenous nature of the OCA criteria, i.e. a common currency promotes business cycles with the area and reduces asymmetric shocks, and thus ex-ante economic convergence is not strictly required. However, we should notice the importance of ex-ante economic convergence in the political meaning, because many candidates for the third stage of EMU made effort to attain sound budgets, as we can see in the 1990s, and this could contribute to the exchange rate stability in Europe before the introduction of the Euro.

172 *Padoa-Schioppa*, (fn. 4), p. 31; *Kawai*, (fn. 2), p. 15. As to the US monetary policy's impact on East Asian currencies, Asian Development Bank, International Monetary Transmission and Exchange Rate Regimes: Floaters vs. Non-Floaters in East Asia, Asian Development Bank Institute Working Paper Series No. 181/2009.

173 Current studies on this issue: *McKinnon/Schnabl*, The East Asian dollar standard, fear of floating, and original sin, Review of Development Economics 8 (2004), pp. 331-360, suggest that the dollar's predominant weight in East Asian currencies in the post-crisis period (1999-2003) had returned to its pre-crisis (1994-1997) levels by examining the currencies of China, Hong Kong, Indonesia, Korea, Malaysia, the Philippines, Singapore, Taiwan and Thailand. *Click*, The ASEAN dollar standard in the post-crisis era: A reconsideration, Journal of Asian Economics 20 (2009), pp. 269-279, by contrast, suggests that original ASEAN 5 countries (Indonesia, Malaysia, the Philippines, Singapore and Thailand) plus Vietnam are not clear US dollar bloc by using data of 1999 to 2007.

Initiative (ABMI) started from 2003.[174] The ABMI aims to facilitate efficient and liquid local currency bond markets in Asia[175] which would promote the utilisation of Asian savings for Asian investments. Together with the CMIM, the ABMI is one of the main pillars of regional financial co-operation in East Asia today.

E. Conclusion

Reviewing the location of economic and monetary union in the framework of regional integration theories in Chapter B, we can conclude the following lessons from the European experiences in Chapter C.

First, from the viewpoints of political science, the co-opetition games between Germany and France (Lesson 1) together with the philosophy of European integration (Lesson 2) played a primary role for EMU, and these two elements reinforced each other.

Second, as to the viewpoint of institutionalisation, Community law (Lesson 3) and Community institutions (Lesson 4) functioned as a binding force for the political decisions and a driving force of regional integration respectively.

Third, from an economic viewpoint, the development of the Common Market (Lesson 5) and economic convergence with coordinated economic and monetary policies (Lesson 6) were important conditions for EMU. In addition, the existence of an anchor currency (Lesson 7) contributed to the credibility of the ERM.

Then, in Chapter D, we examined the latest economic and political situation of regional integration in East Asia.

First, it is true that there is a possibility of co-opetition games among the countries of this area (Lesson 1), but to share a strong philosophy of regional integration will be a necessary condition to an Asian currency (Lesson 2).

Second, the institutionalisation of regionalism in this area has developed in the past ten years, but a higher level of institutionalisation including legalisation would be indispensable for fixing political decisions in order to attain the confidence of the markets (Lesson 3 and 4).

174 Asian Development Bank, http://asianbondsonline.adb.org/index.php (1/9/2011).

175 While most of the Asian countries are net saving countries, these savings are not invested in the region, but are directed to foreign capital markets. This asymmetry of capital flow was one of the causes of the Asian financial crisis in 1997/1998.

Third, economically, a "*Sachzwang*" by the development of regional market could require a further coordination of currencies within the area (Lesson 5). The existence of a local anchor currency may contribute to the stabilisation of exchange rates in the area (Lesson 7). The most important economic element could be economic convergence with coordinated economic and monetary policies (Lesson 6) and this may be an important barometer for examining the economic condition for an Asian currency.

Finally, this paper emphasises the need for the study of East Asian regionalism from institutional and legal standpoints. As Chapter D demonstrates, the institutionalisation of the East Asian area has been attempted since the end of 1990s, and studies in this field are mainly from political and economic points of view. In Europe, there has been a variety of studies from institutional and legal aspects. Although this is because of a long tradition of legal and institutional study in Europe and also because of its early start in regional integration, the important fact might be that the institutional and legal studies themselves have contributed to European integration and the activities of the EU. As we have discussed, an Asian currency would be a long-term project, even if it were to occur. However, there are many other issues to be solved at a regional level in East Asia. When analysed thoroughly, we can extract a lot of lessons about regional integration from the European experiences.