Statement by Gordon Brown on EMU (27 October 1997)

Caption: On 27 October 1997, Gordon Brown, Chancellor of the Exchequer, describes the British Government's position on the third stage of Economic and Monetary Union (EMU) and on the United Kingdom's possible adoption of the euro.

Source: Statement by the Chancellor on the Economic and Monetary Union, 27 October 1997. [ON-LINE]. [London]: Her Majesty's Stationery Office, [23.08.2005]. Disponible sur http://www.hm-treasury.gov.uk/newsroom_and_speeches/speeches/statement/speech_statement_271097.cfm.

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Statement on Economic and Monetary Union by the Chancellor of the Exchequer (27 October 1997)

With permission, Madam Speaker, I want to make a statement on Economic and Monetary Union.

Since the end of the Second World War Britain has faced no question more important and more contentious than that of our relationship with Europe.

Divisions within governments of both parties, and hence indecision, have made British policy towards Europe, over many years, inconsistent and unclear.

The economic consequences of these weaknesses have been a loss of international initiative and influence, recurrent instability and continuing questioning of our long-term economic direction.

To break with this legacy, and to establish clear national purpose, which has eluded us for decades, economic leadership is essential, and Britain must now make the difficult decisions on Europe, however hard.

The decision on a single currency is probably the most important this country is likely to face in our generation. Yet until now, there has been no detailed examination by government of the practical economic issues of EMU. There has been no proper preparation for a decision, because no previous Government could agree on whether they supported it in principle, nor whether there was an overriding constitutional objection on grounds of sovereignty or not; nor whether, even if a single currency worked and worked well, the Government would wish to be part of it. Forms of words like 'keeping the option open' - while no preparations were ever made to render the option practicable - have similarly served as a pretext for postponing the hard choices

Now is the time to make these hard choices and set a long-term direction for our economic future in Europe.

So I will deal, in turn, with the question of principle, the constitutional implications of EMU, and the economic tests that have to be met. In each area, I will set down the Government's policy.

When we came into Government I asked the Treasury to carry out an assessment of the economic tests that have to be met. Accompanying my statement is this comprehensive and detailed Treasury assessment which I am publishing today, copies of which are available in the Vote Office.

Issues Of Principle

I start with the question of principle. The potential benefits for Britain of a successful single currency are obvious: in terms of trade, transparency of costs and currency stability. Of course, I stress it must be soundly based. It must succeed. But if it works economically, it is, in our view, worth doing.

So in principle, a successful single currency within a single European market would be of benefit to Europe and to Britain.

Secondly, it must be clearly recognised that to share a common monetary policy with other states does represent a major pooling of economic sovereignty.

There are those who argue that this should be a constitutional bar to British participation in a single currency, regardless of the economic benefits it could bring to the people of this country.

In other words, they would rule out a single currency in principle, even if it were in the best economic interests of the country.

That is an understandable objection and one argued from principle. But in our view it is wrong. If a single currency would be good for British jobs, business and future prosperity, it is right, in principle, to join.

The constitutional issue is a factor in the decision, but it is not an over-riding one. Rather it signifies that in order for monetary union to be right for Britain the economic benefit should be clear and unambiguous.

So I conclude on this question of principle: if, in the end, a single currency is successful, and the economic case is clear and unambiguous, then the Government believes Britain should be part of it.

There is a third issue of principle - the consent of the British people. Because of the magnitude of the decision, we believe - again, as a matter of principle - that whenever the decision to enter is taken by government, it should be put to a referendum of the British people. So whenever this issue arises, under this Government there will be a referendum. Government, Parliament and the people must all agree.

So we conclude that the determining factor as to whether Britain joins a single currency is the national economic interest and whether the economic case for doing so is clear and unambiguous.

The Five Economic Tests

I now turn to the Treasury's detailed assessment of the five economic tests that define whether a clear and unambiguous case can be made.

These are:

1. Whether there can be sustainable convergence between Britain and the economies of a single currency.
2. Whether there is sufficient flexibility to cope with economic change.
3. The effect on investment.
4. The impact on our financial services industry.
5. Whether it is good for employment.

i. Economic Cycles

Of these, the first and most critical is convergence: can we be confident that the UK business cycle has converged with that of other European countries so that the British economy can have stability and prosperity with a common European monetary policy? That convergence must be capable of being sustained and likely to be sustained - in other words, we must demonstrate a settled period of convergence.

Currently Britain's business cycle is out of line with our European partners. Interest rates here are 7 per cent. This is the level the Bank of England has set in order to achieve our inflation target. But in Germany and France interest rates are close to 3 per cent. Across the continent, because business cycles are more coincident, short-term interest rates have been converging for sometime.

This divergence of economic cycles is, in part, a reflection of historic structural differences between the UK and other European economies, in particular the pattern of our trade and North Sea oil. These differences are becoming less distinct as trade with the rest of Europe grows and the single market deepens.

But divergence is also a legacy of Britain's past susceptibility to boom and bust: the damaging boom of the late 1980s and the severe recession of the early 1990s.

Since coming into office, the Government has introduced long-term measures to ensure that we are capable of maintaining stability by giving operational responsibility for interest rates to the Bank of England and by implementing our deficit reduction plan for public borrowing.

We will need a period of stability with continuing toughness on inflation and public borrowing. The Treasury's assessment is that, at present, the UK's economic cycle is not convergent with our European partners and that this divergence could continue for some time. To demonstrate sustainable convergence will take a period of years.

ii. Flexibility

To be successful in a monetary union, countries will need even more flexibility to adjust to change and to unexpected economic events once the ability of countries to vary their interest rates and exchange rates has gone and the Euro and a single European interest rate are in place. Flexibility may be particularly important for the UK if there is any risk that our business cycle has not fully converged with those of the other EMU members.

The Treasury assessment of the second test is that, in Britain, persistent long-term unemployment and lack of skills - and in some areas lack of competition - point to the need for more flexibility to adapt to change and to meet the new challenges of adjustment. The Government has begun to implement a programme for investing in education and training, helping people from welfare into work and improving the workings of our markets.

Of course, other European countries need to tackle unemployment and inflexibility to make sure Europe as a whole is able to withstand any shocks that arise. The government will continue to argue that employability, flexibility and stronger competition policies must be a top priority so that monetary union can be successful.

iii. Investment

The third test is investment: whether joining EMU would create better conditions for businesses to make long-term decisions to invest in Britain. The Treasury assessment is that, above all, business needs long-term economic stability and a well-functioning European single market. It concludes that membership of a successful single currency would help us create the conditions for higher and more productive investment in Britain.

But the worst case for investment would be for Britain to enter EMU without proper preparations and without sufficient convergence and with all the uncertainty that would entail.

iv. Financial services

The fourth test asks what impact membership of the single currency would have on our financial services industry. EMU will affect that industry more profoundly and more immediately than any other sectors of the economy.

The Treasury's assessment is that we can now be confident that the industry has the potential to thrive whether the UK is in or out of EMU, so long as it is properly prepared. But the benefits of new opportunities from a single currency could, however, be easier to tap from within the Euro zone. This could help the City of London strengthen its position as the leading financial centre in Europe.

v. Employment

For millions of people, the most practical question is whether membership of a successful single currency would be good for prosperity and jobs. The Treasury assessment is that our employment-creating measures, and welfare state reform, must accompany any move to a single currency. Ultimately, we conclude that whether a single currency is good for jobs in practice comes back to sustainable convergence. A successful single currency would provide far greater trade and business in the Europe.

The Treasury assessment is that in vital areas the economy is not yet ready for entry and that much remains to be done. The previous policy of keeping options open, without actively making preparations, has left parts of the economy un-prepared.

Our overall assessment is that Britain needs both a period for preparation and a settled period of sustainable convergence. Both require stability.

The Government's Conclusions on EMU

Applying these five economic tests leads the Government to the following clear conclusions.

British membership of a single currency in 1999 could not meet the tests and therefore is not in the country's economic interests. There is no proper convergence between the British and the other European economies now. To try to join now would be to accept a monetary policy which would suit other European economies but not our own. We will therefore be notifying our European partners, in accordance with the Maastricht Treaty, that we will not seek membership of the single currency on 1 January 1999.

The issue then arises as to the period after 1st January 1999. We could simply leave the options open, as before, but with no clear direction either way for the rest of the Parliament. That would be politically easy but wrong.

There would be instability, perpetual speculation about "in or out", "sooner or later", which would cause difficulties in the financial markets and for business and industry.

It would make it harder to prepare for the possibility of a single currency because every step in preparation, every time the issue was discussed, would feed fresh bouts of speculation.

It must be in the country's interest to have a stable framework within which to plan.

And we are fortified in this because on the economic tests we have set out, the practical difficulties of joining a single currency in this Parliament all point to the same conclusion.

There is no need, legally, formally or politically, to renounce our option to join for the period between 1st January 1999 and the end of the Parliament, nor would it be sensible to do so. There is no requirement under the Treaty for this. What is more, no government can ever predict every set of economic circumstances that might arise.

What we can and should do is to state a clear view about the practicability of joining monetary union during this period. Applying our economic tests, two things are clear. There is no realistic prospect of our having demonstrated, before the end of this parliament, that we have achieved convergence which is sustainable and settled rather than transitory. And Government has only just begun to put in place the necessary preparations which would allow us to do so. Other countries have for some years been making detailed preparations for a single currency. For all the reasons given, we have not.

Therefore, barring some fundamental and unforeseen change in economic circumstances, making a decision, during this Parliament, to join is not realistic. It is also therefore sensible for business and the country to plan on the basis that, in this Parliament, we do not propose to enter a single currency.

There are those who urge us to seek consent, in principle, in a referendum now or soon, but with a view to entering sometime later. Any serious gap between the referendum and the actual entry date would undermine the conclusions of the referendum.

Because the essential decision is economic, it can be taken only at a time when government and then the people can judge that sustainable convergence has been established.

So in our view the interval between the decision to join and our joining must not be unduly protracted.

Preparations

I have said that if a single currency works and is successful Britain should join it. We should therefore begin now to prepare ourselves so that, should we meet the economic tests, we can make a decision to join a successful single currency early in the next Parliament. At present, with no preparation, it is not a practical option. We must put ourselves in the position for Britain to exercise genuine choice.

The questions of preparation are immense - practical questions for business, as well as for government. Euro notes and coins will, for example, be circulating across Europe from January 1st 2002. Some companies, like Marks and Spencer, have already decided to prepare to accept Euros in Britain. Others, will want advice on what is best for them.

Because both the Government and business must prepare intensively during the next years, we will:

commence work on the detailed transition arrangements for the possible introduction of the Euro in Britain, including the introduction of notes and coins, should we wish to enter;

step-up the work on what business should do now to prepare for the introduction of the Euro in 1999, whether we are in or out;

work with business on what government must do to prepare for EMU, should we decide to join it in the next parliament.

To help with essential preparations, I have invited the Governor of the Bank of England and Sir Colin Marshall, the President of the CBI, to join me and the President of the Board of Trade in leading a standing committee on Preparations for EMU. I am pleased to say that they have agreed. I am also inviting the President of the Association of British Chambers of Commerce to join us. I can also announce that, from January a series of regional and sectoral conferences on preparations for monetary union will be held.

Also, the Prime Minister has today decided to extend Lord Simon's Treasury responsibilities to include European Business Preparations in the government, covering the long -term planning of the new standing committee.

In addition to these practical preparations, there are reforms we can take which are both right in themselves, in the national economic interest, and which will help us to meet the five economic tests.

We will promote greater flexibility in the UK economy and in Europe through our "Getting Europe to Work" initiative;

We will be introducing new competition legislation, which draws on the best of European and wider international policy and practice as well as continuing to negotiate to secure the best interests of our financial sector and for the opening up the single market in financial services.

We will set as one of the key objectives of our EU Presidency completion of the European single market.

In my Mansion House speech I said that if we succeed in strengthening the ability of the British economy to sustain growth with low inflation, and if international conditions permit, I would hope to lower the inflation target. So we will monitor our inflation target and do so in the light of the European Central Bank;

And we will ensure that our fiscal rules, and our deficit reduction plan, continue to be consistent with the terms of the stability pact, thus underlining our commitment to avoid an excessive deficit under Article 104c of the Treaty, and supporting greater coordination in ECOFIN;

In Britain's interests, we need to keep inflation low and public borrowing firmly under control.

The single currency will affect Britain, in or out of it. It is in the British national interest for it to work. Vital decisions will be made during our EU Presidency in the first half of next year. We will use our position constructively and supportively and we will play a full part in ensuring its launch is successful - something that is in Britain's interests as well as Europe's.

Conclusions

To sum up:

we believe that, in principle, British membership of a successful single currency would be beneficial to Britain and to Europe; the key factor is whether the economic benefits of joining for business and industry are clear and unambiguous. If they are, there is no constitutional bar to British membership of EMU;

applying the economic tests, it is not in this country's interest to join in the first wave of EMU starting on 1st January 1999 and, barring some fundamental and unforeseen change in economic circumstances, making a decision, this Parliament, to join is not realistic;

but in order to give ourselves a genuine choice in the future, it is essential that the Government and business prepare intensively during this Parliament, so that Britain will be in a position to join a single currency, should we wish to, early in the next Parliament.

On Europe, Madam Speaker, the time of indecision is over. The period for practical preparation has begun. Today we begin to build a new consensus - modern and outward looking - for a country that throughout its history has looked outward to the world.

We are the first British government to declare for the principle of monetary union. The first to state that there is no over-riding constitutional bar to membership. The first to make clear and unambiguous economic benefit to the country the decisive test. And the first to offer its strong and constructive support to our European partners to create more employment and more prosperity.

The policy I have outlined will bring stability to business, direction to our economy, and long term purpose to our country. It is the right policy for Britain in Europe. More important it is the right policy for the future of Britain and I commend it to the House.