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Democratic accountability and the exchange-rate policy of the euro area[1]

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ABSTRACT

This article examines the consequences of the political ‘incompleteness’ of the monetary union for the democratic accountability of its external monetary policy, comparing the euro area to the United States. In most countries, exchange-rate policymaking is substantially delegated to the finance ministry and central bank; oversight by other domestic actors is relatively weak. While this is true of the United States, the role of the Congress provides the possibility for ‘democratic override’ when policy diverges substantially from the preferences of a broad set of private sector interests. Europe's monetary union, by contrast, lacks such a mechanism; no institution can provide an effective check on the policies pursued by the core actors, the ECB and Eurogroup. A comparison of the postures of the United States and euro area toward Chinese exchange rate policy suggests that these institutional differences affect policy outcomes.

KEYWORDS:

The euro | exchange-rate policy | accountability | interest groups | China | euro governance

Notes

[1] Sources: Eurostat database and U.S. Census Bureau, Foreign Trade Division.

[1] Sources: Eurostat database and U.S. Census Bureau, Foreign Trade Division.

1. Prepared for the project on ‘Legitimacy and Efficiency: Revitalizing EMU ahead of Enlargement’, organized by Erik Jones, Tal Sadeh and Amy Verdun. The author would like to thank Jacqueline Best, Daniel Daco, Andreas Falke, Kathleen McNamara, Jonathan Kirshner, Georges Pineau, Jens van Scherpenberg and two anonymous reviewers for comments on previous versions, as well as the editors and other authors and participants at the project meeting at SAIS Bologna in December 2005. He also wishes to acknowledge the valuable research assistance of Alina Milasiute and Bella Nestorova.

2. This framework thus adopts a concept of accountability that is procedural, institutional and rationalist. A normative concept, grounded in constructed norms and rights, represents an alternative that is certainly worth pursuing in scholarship on the accountability of policy within the euro area and European Union. Without intending to foreclose these alternative approaches, however, this article adopts the more institutional concept because it can be applied directly to the exchange-rate policymaking apparatus of the euro area, has been neglected in previous articles, and is particularly suitable for a comparison of accountability in the United States and euro area.

3. See also Freeman 2002, which evaluates the applicability of the concept of ‘expert democracy’ to monetary policy.

4. The Nice treaty changed the decision rule for external representation from unanimity to qualified majority.

5. The IMF staff drew attention to lack of transparency of the exchange-rate policymaking process in its 2001 report on the euro area, IMF 2001.

6. The latter is examined in Henning (2006).

7. These are critical contributions to a debate over global current account adjustment that is broad ranging. This paper does not hinge on the normative questions in this debate – such as the sustainability of the imbalances and the responsibility of the United States, euro area and East Asia, among other actors, for reducing them – interesting as such questions are. The argument developed here hinges instead on the impact of China's exchange rate policy on the economies of the United States and euro area and the responses of the two authorities.

8. See http://www.chinacurrencycoalition.org/members.html. Accessed December 11, 2006.

9. Search conducted on http://thomas.loc.gov/home/c109query.html in December 2006. Hufbauer et al. (2006) count 23 such bills between February 2003 and March 2006.

10. European Commission, 'Bilateral Trade Relations with China', accessed June 22, 2006 at http://ec.europa.eu/comm/trade/issues/bilateral/countries/china/index_en.htm

11. 'We continue to monitor exchange markets closely and cooperate as appropriate. In this context, we emphasize that more flexibility in exchange rates is desirable for major countries or economic areas that lack such flexibility to promote smooth and widespread adjustments in the international financial system, based on market mechanisms'. Statement of G-7 Finance Ministers and Central Bank Governors (2004).

12. A search on congressional hearings during 2003–2005 mentioning the 'exchange rate' generated 7 at which the phrase was mentioned more than 30 times, 2 at which the phrase was mentioned 20–29 times, 9 at which it was mentioned 10–19 times, and more than 100 at which it was mentioned 1–9 times. Thirty-two hearings addressed China specifically. Conducted in April 2006 at http://www.gpoaccess.gov/chearings/search.html.

13. Confindustria, Economic Outlook, September 2003 (especially p. 10) and December 2005, as well as its Report on Italian Industry, October 2004. Available at http://www.confindustria.it.

14. UNICE, ‘UNICE Position Paper on EU-China Relations’, Brussels, May 8, 2006, available at www.unice.org. Interestingly, Confindustria argued that renminbi undervaluation should be addressed within the International Monetary Fund, rather than through EU or euro area machinery. Confindustria, Economic Outlook, December 2003: 10

15. To the extent that the available data allow a comparison. See Eurostat database, Foreign Direct Investment, available at http://epp.eurostat.ec.europea.eu.

16. While applauding China's modest revaluation in mid-2005, Weber (2005) and Issing (2005) take this essential position. Ahearne and von Hagen (2005) and Pisani-Ferry and Sapir (2005) inveigh against European complacency with respect to the renminbi, which they also describe as pervasive.

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