

Hamburg 5 November 2008: European Monetary Policy and World Capital Markets

by Sir Michael Arthur

Americans will say today is an historic day. In Hamburg we can say that too. An historic conference. An historic line-up. And a real privilege for people of my generation to participate in the living history which is personified on this platform.

We are here today to talk about the global financial market challenges. But we are also here to honour Chancellor Schmidt in his 90th year, both a son of Hamburg and one of the greatest post-war Chancellors Germany has seen.

We are talking about future solutions to today's global financial challenges. Where better to start than reflecting on the dramatic initiatives taken by Chancellor Schmidt with his key partner President Giscard d'Estaing almost a generation ago.

Having them both here today makes Hamburg a historic venue, not to be disguised by some distractions in Washington.

Chancellor Schmidt was running Germany when I started my professional life. I grew up admiring his strong policy and intellectual lead. To come back to Germany as Ambassador and have the chance of a few conversations with him has been a real privilege and pleasure. Even through the smoked filled haze!

For a Briton, there is a particularly nice irony in talking with Chancellor Schmidt about the key issues of Europe, International finance and Monetary Union. As Herr Schmidt delights in telling me, he is a man with a deep conviction that quite a lot of what the UK stands for – our democracy, our values and goals – are excellent. But he chides us for never having developed our European vocation.

History will judge quite how “European” Britain has become. We may not have joined the Euro. But the last few weeks have clearly shown a strong commitment from Britain and led by Gordon Brown to be part of the **European** solution to today’s global financial challenge. I’ll come back to that.

But first one word on a different topic where Chancellor Schmidt also showed global leadership. I don’t mean his foresight in creating the precursors **of** the G7 / G8, although that too. I mean the brave political stance he took over nuclear weapons and the Soviet Union. I spent four years in Bonn in the mid-eighties working with the then German government of Helmut Kohl as we translated NATO’s INF decisions into reality; Cruise missiles, Pershing 00 loesung – remember that?

The antecedents of that game-changing stance by NATO go back to a speech by Chancellor Schmidt at the International Institute of Strategic Studies in London. If anything were strategic foresight and leadership that was it.

In my humble judgement two key policy roots led to the end of the Soviet Union, the end of the Cold War and the Reunification of our continent Europe. A robust strategic defence posture, epitomised by INF, and by NATO. And a sound market based economy standing in sharp contrast to the palpable failure of the Soviet COMECON model. Chancellor Schmidt was one of his generation’s leading drivers for both.

But today we will talk about finance and the future. Three basic principles must underline the way forward. I hope Herr Schmidt will recognise them all as today’s version of his crusades.

First, globalisation, and the tectonic shifts underway in the global economy, require a globally co-ordinated response. We now identify the problem. We don’t yet have consensus on the solution. But we recognise that this requires a modernised global architecture, particularly in the financial arena.

Second, Europe has to act together. When it does, we can demonstrate shared leadership at a global level.

Third, sound international economic policy. This should be built round principles like: transparency. Sound financial practice, **especially on risk and capital adequacy**. Suitably co-ordinated governmental oversight and regulation. **Management** responsibility, for example for risk.

All of those have a Schmidt-ian signature tune. I remember him telling me a year ago that the international banking structures could not continue as they were and were heading for a fall. I heard it again in September this year before the crisis really broke.

What has been remarkable about the last few weeks has been:

- How fast the institutional financial fire caught light and spread
- How well regulators and governments in the G7 / G8 world work together – contrast 1929
- How within Europe we did not let structural differences like membership of Eurozone come in the way of concerted action.
- How clearly leaders, Gordon Brown among them but last week with Frau Merkel in London, and President Sarkozy as President of the European Council, have plotted a route map for a European / G8 / G20 / international response.

The immediate challenge has been to stabilise markets, and ensure sufficient liquidity in the banking system to stop the motor grinding to a halt. We seem to have done that. But as Gordon Brown was the first to say (and has been saying for some time) we now need a far-reaching reform for the structure of the international financial architecture. We are not allowed to call this Bretton Woods II. But we all know what we mean.

So here is the final reason why today in Hamburg may prove historic. Not only do we have historic thinkers present. We are also meeting on exactly the right day (Post ECOFIN, pre-European Council), in exactly the right week (before the 15 November Washington Summit) to input some ideas into these crucial decision making forums.

I look forward to hearing what today's two great "Oracles", and the rest of you, now tell us to do.